

# How Does Internet Stock Trading in India Work?

Chandana Goswami

## Executive Summary

Internet trading started in India on 1st April 2000 with 79 members seeking permission to do so. Geojit Securities was the first to go online. On 1st February 2000, the National Stock Exchange (NSE) opened up the internet-based trading system for its members, the first stock exchange in India to do so. However, after two years of trading, only a dozen brokers continue offering online service. The SEBI Committee on Internet-based Securities Trading and Services has allowed the net to be used as an Order Routing System (ORS) through registered stockbrokers on behalf of their clients for execution of transactions. This paper aims at understanding the needs of the customers, comparing it with the offerings of the websites, identifying the gaps, and offering possible solutions for filling up the gaps. It is revealed that:

- Online traders took buying decisions on their own. A few backed it up by analysts' recommendations. Those who took decisions independently claimed to go through the websites, did fundamental and technical analysis, watched the trends, and then finally made a decision. No one solely followed brokers' recommendations blindly. Well-educated people in their 30s and 40s, who were highly informed and also knew how to tap sources of information, took decisions on their own and did not depend upon the broker. They were self-directed traders.
- The major perceived benefit of online system was its convenience. The broker's reliability followed by the execution speed was the key to logging on to a website.
- An analysis of the Indian sites indicated that they were mainly promotional and provisional in nature. Provisional information about stock quotes, database searches, research reports, etc. were provided in the site empowering the user to take independent decisions. Promotional activities in the form of facilities locator, educational forums, web designs, demos, etc. had lured many to visit their sites but whether this had converted into online clients could not be confirmed from the results of this study.
- Indian websites offered a basic plain package with lot of scope remaining for value addition. Excluding the technical and legal aspects over which the e-finance service providers did not have much control, certain value additions could be done on the existing websites. Moreover, the Indian investors having access to the foreign websites were quite well versed with what was being offered by the American counterparts and hence they were highly demanding customers.

The following services could make Indian sites more attractive to customers:

- Interactive counselling
- Customer care centre
- Investment tips
- Warning systems
- Extended hours trade
- Account management
- Inter-organizational alliances.

## KEY WORDS

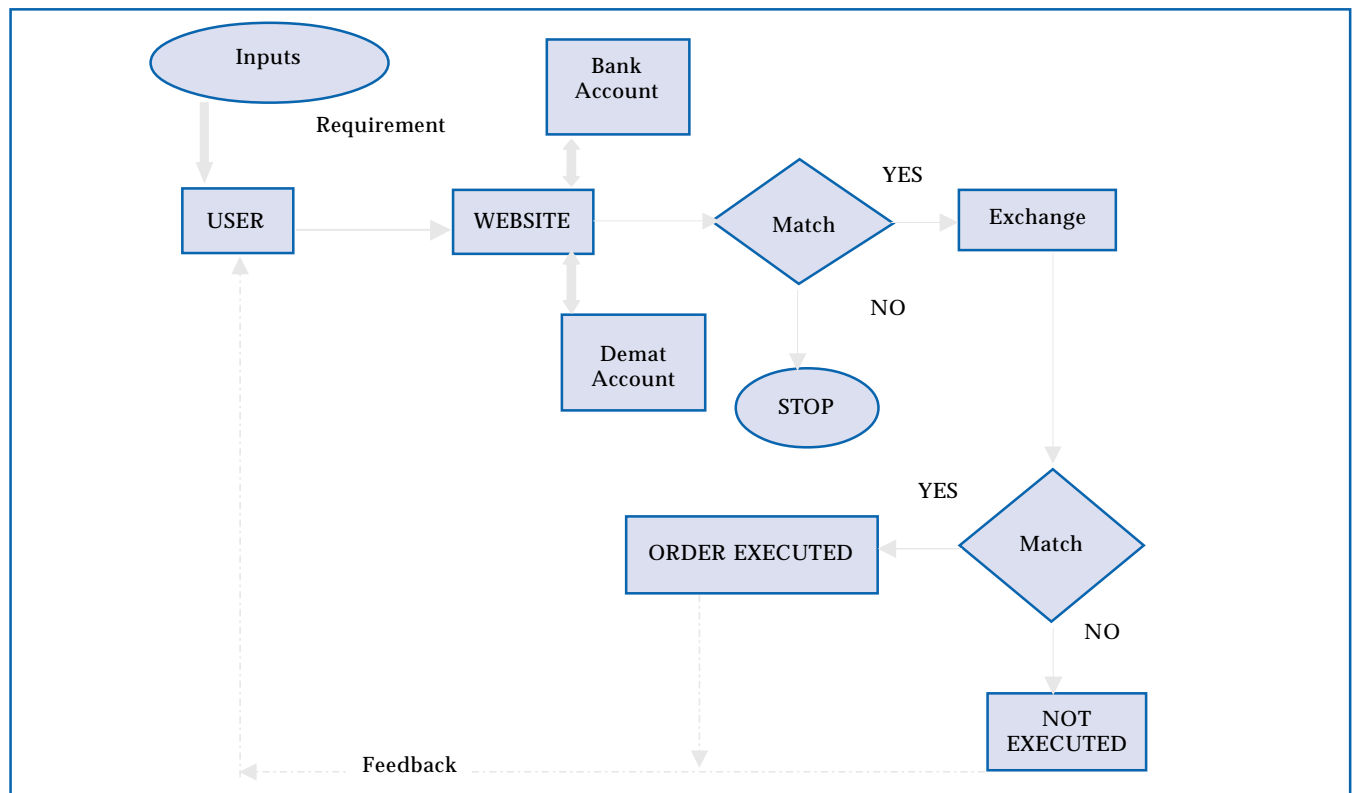
E-finance  
Online Trading  
Online Brokerage  
SEBI

In India, the Securities Exchange Board of India (SEBI) has allowed internet trading of stocks in a limited form. In internet stock trading, the net is used as a medium to communicate orders to the stock exchange through the broker's website. The user cannot directly trade in the exchange because trading is permitted only for registered brokers. The user can, however, place orders through a broker's site. These e-broking sites also provide the client with an opportunity to buy and sell securities from the confines of one's home or office. The client is able to track the fluctuations in a particular stock and the market as a whole while deciding to execute the order and also while the order is being executed. The confirmation of the executed order will be available in real time. Natarajan(2000) feels that prices will be determined by market forces and the availability of a particular product. Depending on the supply and a comparative list of similar products, the customer will be able to choose the best stocks available in the market.

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members, the first stock exchange in India to do so. However, after two years of trading, only a dozen brokers continue to remain ahead in offering online service. According to NSE data, there are around 2.3 lakh registered online traders. The SEBI Committee on Internet-based Securities Trading and Services has allowed the net to be used as an Order Routing System (ORS) through registered stockbrokers on behalf of their clients for execution of transactions. Under the ORS, a client enters his requirements (security, quantity, price, buy/sell) in the broker's site which are checked electronically against the client's account and routed electronically to the appropriate exchange for execution by the broker. The client receives a confirmation on execution of the order. At the same time, the customer's portfolio and ledger account gets updated to reflect the transaction [Figure 1]. Since all orders have to necessarily be routed through the exchange mechanism, it ensures transparency and security. The sites ensure security in the following way. The system permits only a registered client to log in using a user-id and password. This unique combination of user-id and password will permit entry into the electronic ring. Most sites use encryption technology to ensure that the transmitted information is safe and cannot be accessed by any outsider.

**Figure 1: Online Trading**



Ho(2000) found that the level of provisional value has increased substantially over the past couple of years to empower the investor in cyberspace. Provisional value was provided in the form of stock quotes, advertising employment opportunities, general database search, customized news report forecasting, financial reports, research data, comparisons and survey results, etc. Sensational value was in the form of free trials, discounts, and software demos. The growth in the popularity of sites charging low, fixed fees per trade was transforming the online trading industry.

There is a category of investors who are well versed with the online trading systems of other countries and hence are very choosy about opting for an online trader. There is another category of investors who still prefer the good old broker to provide service. Also, there are a few investors who are willing to experiment with the new system and understand how it can be worked to one's benefit.

The objective of our study is to understand the needs of the customers, compare them with the offerings of the websites, identify gaps if any, and suggest possible solutions for filling up the gaps. Our findings, we believe, will provide a general sense of direction to the existing as well as potential broking houses who have or will have online trading services and help them in designing an appropriate website for the benefit of the customers and for creating volumes.

## DETAILS OF THE SURVEY

We conducted a survey questionnaire available on request. during August 1999 and February 2000 at Ahmedabad. Twenty nine respondents from different parts of the country were interviewed. Some of them were participants of management development programmes at the Indian Institute of Management, Ahmedabad. They were all qualified with a majority being professional graduates (agricultural, engineering, computer science, veterinary, medical or chartered accountants) and post-graduates (MA, MSc, M com, MD, MBA, MS, or Mtech).

Majority of the respondents (84%) belonged to the age group of less than 40 years followed by the people in the next age group of 40 to 60 years.

Out of the 29 respondents, there were two females. They, however, said that either they did not trade or it

was their husbands who were involved in trading and they had no inkling of what stock trading was. One of them was unmarried and the other was a chartered accountant in her late 40s. People in service and the business class comprised 92 per cent of the entire sample, and the remaining eight per cent consisted of students. It can be concluded that the average trader in this study is a person in his 30s or early 40s, is well educated, and is in service.

## FINDINGS

Since our survey is based on a small sample, we are not in a position to arrive at definite conclusions. We use the findings as a basis to discuss issues related to internet trading in India. We hope that more comprehensive studies will be conducted in the future to investigate these issues further.

### Decision Making

For the question, "How do you take buying or selling decisions," the survey of online traders revealed that they took buying decisions on their own. A few backed them up by analyst's recommendation. Those who took decisions independently claimed to go through the websites, did fundamental and technical analysis, watched the trends, and then finally made a decision. None of them followed broker's recommendations blindly. They were self-directed traders.

### Benefits of Online Trading

In response to the question on benefits of an online system, the respondents rated convenience, ability to help users to identify investment opportunities, low cost, and the quick confirmation of trade as the most important. Those who were not users of online trading services also mentioned that they used to surf the websites in search of investment tips and then took the decision to buy or sell.

### What Factors Influence Online Broker Selection?

The survey revealed that free gifts did not hold much importance in choosing a website. The broker's reliability followed by the execution speed was the key to logging on to a website. Those respondents who had not opted for online trading gave execution speed as an important criterion for not going online. Speed is all the more important for a day trader who has to

follow the price movements thoroughly in order to make profits or minimize losses. For such persons, it makes sense to use the NSE terminal of the broker (if allowed) or follow the CNN ticker on the television and place order over the phone as it is believed that the rates on the websites are seen after a delay of five minutes approximately.

### Selection of Online Services

The respondents used a variety of online services for trading. ICICIdirect.com appeared to be the favourite service followed by NSE and HDFC sites. This could be attributed to ICICI's large clientele base coupled with the fact that it is informative.

Even a year after the survey, ICICIdirect.com dominates 50 per cent of the market (*Economic Times*, 10 January 2002). Industry experts attribute the success of ICICIdirect.com to its ability to provide strong connectivity between the trading account, demat account, and bank account.

### Features of a Website

According to the respondents, the top ten requirements from an online trading website were:

- Feedback about trade execution
- Market analysis
- Tracking facilities
- Feedback about wrong trade
- New investment tips
- Fundamental analysis
- Technical analysis
- Live quotes
- Sector-wise analysis
- Personal portfolio management.

The least desirable feature was the freebies on opening accounts. This answer corresponds to that obtained above where freebies again got the last rank.

The additional features that the respondents would like to have on their websites were:

- Downloading of the BSE index and NSE index movements.
- Instant credit to bank account.
- Monthly statement of trading and bank account to be sent by email.
- Record of all transactions done for future reference.
- Need for more detailed information on scrips and investment tips (particularly for NSE users).

These facilities could be introduced in the sites, and if existing, reinforced to retain clients.

### Reasons for Switching to Online Trading

According to the respondents, the major reason for switching over to online trading was its speed. This evidence supports the earlier response. Also, it was economical and instant feedback was available about the execution. In case of off-line trading, the client has to wait till the end of the day for the broker to send him/her a statement of transactions or inform over the telephone.

As of now, there has only been part conversion to online trading. This is due to the fact that online trading requires the shares to be in the dematerialized (demat) form, which the respondents may not have. Further, all the listed companies have not gone for demat as yet but will be converting very shortly out of legal necessity.

The respondents mentioned quite a few reasons such as margin money required before trading, lack of personal interaction, existing friendly brokers, no trust on online system, etc. for not fully switching over. These are some of the gaps that need to be addressed by the existing sites.

The top five reasons for not trading online were:

- Security reasons associated with disclosing bank account and demat account.
- Lack of inadequate infrastructure.
- Present broker is giving adequate service.
- Uncomfortable with computers.
- Wait and watch attitude.

### Online Stock Trading Sites

We visited several Indian sites to understand their service offering (Box 1). An analysis of the sites indicated that they are mainly promotional and provisional in nature. Provisional information about stock quotes, database searches, research reports, etc. have been provided in the sites, empowering the user to take independent decisions on his/her own. Promotional activities in the form of facilities locator, educational forums, web designs, demos, etc. have lured many to visit their sites but whether this has converted into online clients cannot be confirmed from the results of this study.

## ONLINE STOCK TRADING IN THE US

A survey of some of the prominent American online

## Box 1: List of Websites Visited

www.ameritrade.com	www.bizfinance.com	www.cybercash.com
www.dealcomposer.com	www.debtonthenet.com	www.dljdirect.com
www.emecklai.com	www.e*trade.com	www.efunds.com
www.equis.com	www.ecoins.net	www.growasia.com
www.icicidirect.com	www.jpmorgan.com	www.kotakstreet.com
www.mldirect.com	www.moneypore.com	www.nseit.com
www.sebi.gov.in	www.schwab.com	www.sharekhan.com
www.volbroker.com	www.5paise.com	

brokerage sites was done including DLJdirect, Merrill Lynch, Ameritrade, Etrade, and Charles Schwab which indicated that the sites offered combinations of the following facilities:

- News and research reports
- 24 hours customer care
- Account management
- Index movements of major international stock exchanges
- IPO, mutual funds, bonds/debentures centres
- Customized information
- Investment tips
- Stock analyser
- Alerts
- Freebies.

However, according to Sharma and Prasad (2000), all is not positive in the American scenario. There have been cases of slow connections, site outages, incorrect posting of accounts, and execution mistakes. There are also issues related to overtrading as costs of transactions continue to fall. The Securities Exchange Commission (SEC) has also launched an enquiry into the e-trade industry prompted by customer complaints of poor service and incorrect posting of accounts.

### How Do the Indian Sites Differ from the American Sites?

If the Indian sites in general are compared with the American sites, we can list what they are offering and what they are not. What the Indian sites are offering are :

- News and research reports
- BSE and NSE movements
- Stock analyser
- Freebies
- Some offer additional features as the IPO and mutual funds centres and movement of international stock exchanges.

What they do not offer are:

- Customer care centre
- Account management
- Investment tips
- Alerts
- Online approval.

From this comparison, it can be concluded that the Indian websites offer a basic plain package with lot of scope remaining for value addition if we exclude the technical and legal aspects over which the e-finance service providers have not much control. Moreover, the Indian investors having access to the foreign websites are quite well versed with what is being offered by the American counterparts and hence are very demanding. Indian online brokerage houses will have to keep this factor in mind while offering value-added services.

Agarwala, Lal and Agarwala(2000) feel that the underlying theme behind the development of technologies and techniques for customer interfaces will be to make the customers' experience as close to real life as possible. It will bridge the gap between the electronic world and the real world and significantly add to the comfort level of the consumer.

Venkataraman(2000) feels articulating a strategic vision for dot-com business in precise terms is futile; the net is evolving at such a dizzying pace that it is nearly impossible to work towards a specific end-state. It is more useful to approach the issue as a continuous cycle involving building on current business models and creating future business models through selective experimentation.

### HOW TO MAKE THE INDIAN SITES MORE USEFUL TO CUSTOMERS?

The following steps could be taken for making the Indian sites more attractive to customers.



## Interactive Counselling

Unlike Schwab.com which offers different investment avenues for different needs, the Indian sites do not offer any such guidance. The general feeling is that those who are in trading are wanting to make money either overnight (day traders and speculators) or in the long run. Trading in stock is not thought of as an avenue for savings for future consumption. These sites can guide the investors in their choice of investment decisions since the average online investor is fairly educated and well informed and will require minimal guidance to fully convert to online trading. Thus, an interactive counselling feature will definitely give the feeling of personal guidance which seems to be lacking at the moment.

## Customer Care Centre

Customer care seems to be missing in almost all the sites except ICICI which offers initial care at the time of registration. Since ICICI has established retail outlets in most cities, the customers have accessibility to some sort of support.

To ensure proper customer care, a toll free telephone number, a centre at the website, and an office centre are essential. Although most of the clients are well educated and informative, they are still looking for some back-end support. This has been reflected in the answer to the reasons for not fully switching over to online trading. The websites must develop customer care centres to give this feeling of personal interaction. This will enhance the reliability of the service provider.

## Investment Tips

The response to the question regarding decision-making had revealed that most people took decisions on their own or took decisions after going through the analyst's recommendations. Informal discussions had revealed that the respondents surfed various websites looking for information or investment tips. This highlights the need for authentic and reliable tips. Introduction of investment tips, along with analysis, will be a definite value addition for online clients.

## Warning Systems

The trader in this study, being in service, does not spend all his time in front of the computer terminal. He checks out the figures on a daily basis for a particular scrip. It would be a great help to him if, therefore, an alert

message about price/volume fluctuations could be sent to him either through email or pager or any convenient media.

A year after the survey, we can see that 5paisa.com has started this service.

## Extended Trade Hours

This concept has been started by the Over The Counter Exchange of India (OTCEI). A study of the DLJ direct site indicates that they offer extended hour trade (equivalent to kerb trading) before and after the regular trading hours. The orders for this are valid only for the extended trading sessions and are not mixed up with normal trading. This will be advantageous to those clients who find it difficult to trade during normal trading hours. Although very few respondents gave importance to "inconvenience of trading hours," the websites could try it on an experimental basis to gauge the reaction of the users.

## Account Management

Personal portfolio management got the 10th rank in the priority requirements of the website. Clients would prefer to have shares and money instantly credited to their accounts when they buy and sell shares. As of now, one has to wait till the settlement day. A few websites have incorporated certain provisions to overcome this limitation. For e.g. Kotakstreet and Moneypore make it convenient for clients to get their money instantly through a discounted value scheme. The client can receive discounted value in lieu of waiting for the settlement period. (A year later, ICICI also introduced a similar scheme "Buy Today Sell Tomorrow." However, only 50 per cent to 70 per cent of the receivables will be available for sale). Some respondents desired that a monthly statement of trading and bank account details be sent by email. Another requirement mentioned was that the system should keep a record of all transactions done for future reference of the user.

## Inter-organizational Alliances

From our observations so far, it is clear that ICICI is in an advantageous position by offering IPOs and mutual funds in the same website. This has been possible because ICICI is a leading underwriter and lead manager to many public issues. The present websites can think of a tie-up with leading merchant bankers,

commercial banks or underwriters and also establish such centres in their websites. This will lead to an increase in the variety of products offered by the site and increase their clientele base.

### Portfolio Calculator

Another facility which the sites could adopt is the Portfolio Calculator. The client should be able to do a 'what if' analysis on his portfolio. He should be able to find out the value of his portfolio at today's market price and find out how much he will earn if sells some shares or how much the portfolio will be worth if he buys and sells various combinations of shares. This will help him in taking an optimal decision.

### Retaining Clients

In order to attract a client and ensure 'stickiness' (i.e. the amount of time a client spends browsing), the site will have to adopt a two-pronged strategy or a multi-tiered strategy adopted by Charles Schwab. Who have made themselves accessible through the web, telephones, and office sites. This is an important factor in getting new clients. Such an approach reassures the client that he can call the helpdesk anywhere and at any time as per his needs. There are times when a personal interaction is more desirable than the impersonal answers through the net. This will also enhance the reliability of the online brokerage house. The level of stickiness can be ensured by providing for *personalized home pages* so that the user can customize the unbundled products as per his requirements. This saves a lot of time that would otherwise be required to sort and seek information. Another method of saving time for the client would be to ensure that the site downloads very fast. This is possible if the home page does not have elaborate graphics. The *quick response time* is one of the enticing factors. Pricing strategy would also have to be adopted client-wise. DLJdirect and Mldirect use almost similar pricing strategies. A fixed rate of \$20 (DLJ) and \$29.95 (ML) is for trade up to 1,000 shares. DLJ charges \$0.02 per share for trade above 1,000 while ML charges \$0.03 for the same. Select

clients receive reduced commission rates. A similar strategy may be adopted by Indian sites also.

## CONCLUSION

The net can help lower the cost of transactions, improve customer data, increase cost-selling opportunities, and integrate new financial products. Although the initial development costs may be high, it can be overcome by volumes which can be created by encouraging more and more empowered customers to click on to the site. The Indian online brokerage sites are in a state of flux with new additions taking place rapidly. The sites which were studied have done value additions in a span of six months. Online trading requires a certain amount of sophistication on the part of the investor. It offers a distinct advantage to small time investors who are otherwise not entertained by the offline brokers. The client has to be self-motivated and self-directed and be familiar with computers as well as trading signals/languages. Online trading empowers the educated investor to make his own decisions. The results of the survey also show that educated investors usually take their own decisions and do their own research by browsing through various sites. This is where online sites can make the difference by allowing the investor access to variety of information about different avenues of investments (securities, debentures, bonds, mutual fund units, IPOs) and mass customization (ability to customize information by having personalized home pages).

The period between June 2001 and December 2001 saw an increase in the average daily turnover in online trading from Rs 10 crore to Rs 60 crore. This sudden spurt in online trading can partly be attributed to the introduction of rolling settlement by the SEBI. The present volume of online trading on the NSE is about 2 per cent of its total turnover. With the growth of the educated working class and business class and support from the SEBI, online trading in India is bound to grow at a faster pace than it is now. 🐦

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- Chandana Goswami** is a Reader in the School of Management Sciences at Tezpur University, Assam. A Ph.D. from Gauhati University, her areas of interest are finance and information technology. She attended the Faculty Development Programme at IIM, Ahmedabad during 2000-01.  
e-mail: chandanagoswami@rediffmail.com

### Sources of Ideas

*I have known songwriters who got inspiration from listening to crowd chants at basketball games, venture capitalists who spotted new opportunities by going to junk yards, educators who got ideas by going to prisons, advertising people who borrowed ideas from biology, and software programmers who were influenced by songwriters.*

**Roger von Oech**

*A Whack on the Side of the Head*