UNIT 15 CAPITAL MARKET AND ITS REGULATION

Structure

15.0 Objectives

15.1 Introduction

15.2 Role, Significance and Functions of Capital Market

15.3 Stock Market Development in India

- 15.3.1 Motives for Reforms in the Stock Markets
- 15.3.2 Liberalisation
- 15.3.3 Monopoly of Association type of Exchange
- 15.3.4 Open Outcry System
- 15.3.5 Clearing, Settlement and Risk Management Problems
- 15.3.6 The Scams in the Decade of 1990s

15.4 Stock Market Reforms Since 1992

- 15.4.1 Establishment of SEBI
- 15.4.2 Market Determined Allocation of Resources and Investor Protection
- 15.4.3 Demutualisation and Establishment of NSE
- 15.4.4 Screen Based Trading
- 15.4.5 Risk Containment at the Clearing Corporation
- 15.4.6 Risk Management
- 15.4.7 Dematerialisation
- 15.4.8 Derivatives Trading
- 15.4.9 Globalisation
- 15.4.10 Rolling Settlement and Ban on Deferral Products

15.5 Structure and Performance of Indian Stock Market

15.6 Equity Derivatives in India

- 15.6.1 Exchange-Traded and Over-the-Counter Derivative Instruments

15.7 Foreign Exchange Market Development in India

15.8 Currency Derivative Market in India

- 15.8.1 Exchange Traded Currency Derivatives in India

15.9 Long Term Government Bond and Corporate Debt Market in India

- 15.9.1 Outlook for Development of Corporate Debt Market

15.10 Let Us Sum up

15.11 Exercises

15.12 Some Useful Books

15.13 Answers or Hints to Check Your Progress Exercises

15.0 OBJECTIVES

The primary objective of this unit is to develop an understanding of the organisational structure, role, function and performance of the Indian capital market. After going through this unit, you will be able to :

- Explain the radical restructuring of the Indian capital market in the wake of new economic policy in 1991; and
- Explain the role, function and structure of Indian Equity Market, Currency Market, Derivative Market and Corporate Debt Market.

15.1 INTRODUCTION

The dynamic and efficient financial system plays a very pivotal role for any economy for efficient allocation of resources from surplus segment to deficit segment. The financial system consists of financial markets, financial intermediation and financial products or instruments. A thriving and vibrant economic system requires a well developed financial structure with multiple intermediaries operating in the market with different risk profiles. The financial sector in India is characterised by progressive liberal policies, vibrant equity and debt markets and prudent banking norms. Further, a financial system helps to increase output by moving the economic system towards the existing production frontier. This is performed by transforming a given total amount of wealth into more productive forms. It induces public and investors to hold fewer saving in the form of precious metals, real estate land, consumer durables and ideal cash balances and to replace these assets by financial instruments such as bonds, shares, preference shares, units etc. A financial system also helps to increase the volume of investments. It becomes possible for the deficit spending units to undertake more investment because it would enable them to command more capital. It encourages the investment activity by reducing the cost of finance and risk. This is done by providing insurance services and hedging opportunities and by making financial services such as remittances, discounting, acceptance, and guarantees available. Finally, it not only increases greater investment but also raises the level of resource allocational efficiency among different investment channels. The broad picture of the Indian Financial System is presented in the schematic diagram below as Figure 15.1.

Indian Financial System

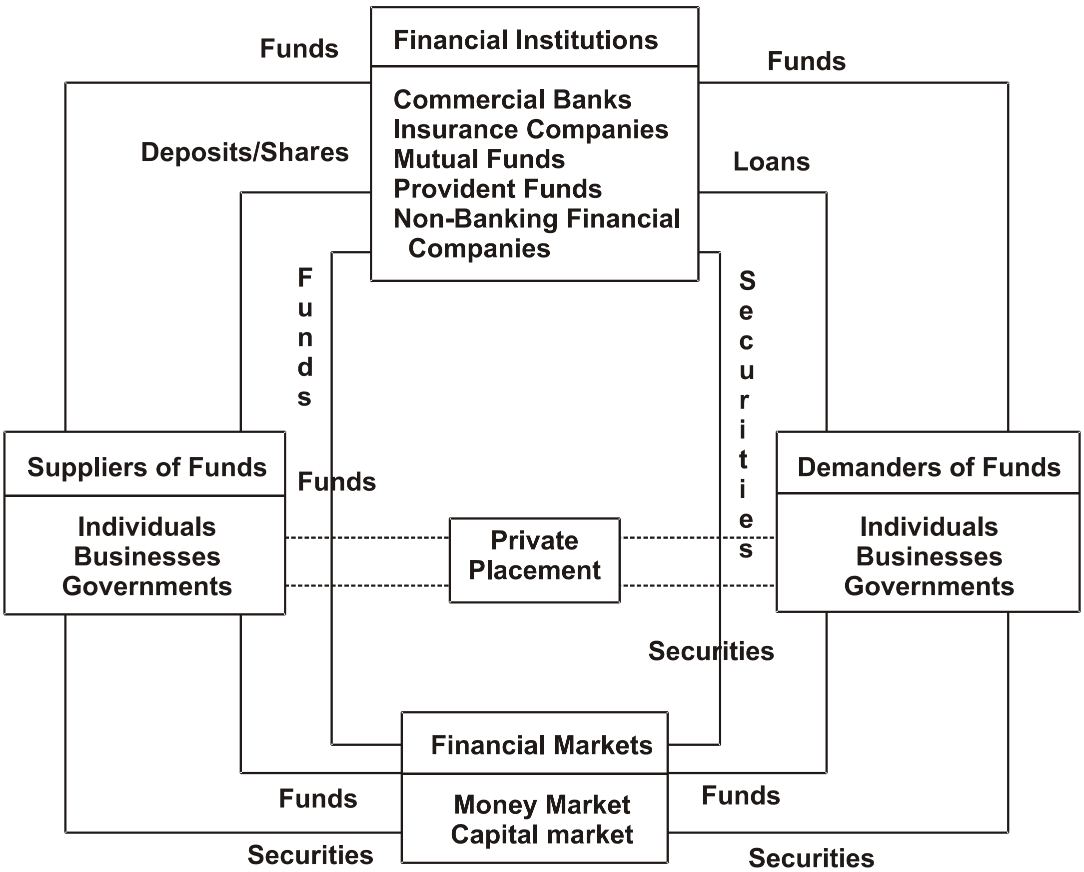

Figure 15.1

Capital market is an integral part of the financial market. The capital market is a market for financial assets which have a long or indefinite maturity. Capital market is broadly categorised into two parts such as primary and secondary market. In the primary market, new stock or bond issues are sold through a mechanism popularly known as underwriting. In the secondary market, issued shares are traded through organised exchanges such as stock exchanges, over the counter etc. The capital market consists of stock or equity market, debt market, derivative market, foreign exchange market and commodity market. These markets are providing the facilities for buying and selling of the variety of financial claims and services. The corporations, financial institutions, individuals and governments trade in financial products in these markets either directly or through brokers and dealers on organised exchanges or off exchanges. The capital market participants on the demand and supply sides of these markets are financial institutions, agents, banks, brokers, dealers, lenders, savers and others who are interlinked by the laws, contracts, covenants and communication networks. The primal role of the capital market is to channelise investments from investors who have surplus funds to the ones who are running a deficit. Financial regulator such as Security Exchange Board of India oversees the capital markets in their designated jurisdictions to ensure that investors are protected against fraud among other duties.

Reforming and liberalising financial markets began in the wake of the country's 1991 balance of payments crisis. The thrust of these reforms was to promote a diversified, efficient and competitive financial system, with the ultimate objective of improving the allocation of resources through operational flexibility, improved financial viability and institutional strengthening. The pace of reform was, however, slower than those in product markets, partly because the introduction of stricter prudential controls on banks revealed significant problems in asset portfolios. Prior to the reforms, state-owned banks controlled 90 per cent of bank assets – compared with approximately 10 per cent at end-2005 – and channelled an extremely high proportion of funds to the government. Interest rates were determined administratively; credit was allocated on the basis of government policy and approval from the Reserve Bank of India (RBI) was required for individual loans above a certain threshold. Capital markets were underdeveloped, with stock markets fragmented across the country. The major stock market acted mainly in the interest of its members, not the investing public. Derivative markets did not exist and comprehensive capital controls meant that companies were unable to bypass domestic controls by borrowing abroad. Concerns over the 1997/98 Asian financial crisis and its contagion effects further spurred Indian authorities to strengthen the domestic financial system. Reforms were, and continue to be, based on several principles: (i) mitigate risks in the financial system; (ii) efficiently allocate resources to the real sector; (iii) make the financial system competitive globally; and (iv) open the external sector. The goal was to promote a diversified, efficient and competitive financial system which would ultimately improve the efficiency of resource allocation through operational flexibility, enhanced financial viability and institutional strengthening.

15.2 ROLE, SIGNIFICANCE AND FUNCTION OF CAPITAL MARKET

Capital market facilitates the transfer of capital (financial) assets from savers to investors. It provides the significant amount of liquidity which refers to how easily an asset can be converted to currency without loss of value. A side benefit of a capital market is that the transaction price provides a measure of the value of the asset. The major functions of capital market includes disseminate information efficiently, enable quick valuation of financial instrument, provides insurance against market risk and price risk, enable wider participation, provide operational efficiency through simplified transaction procedure, lowering settlement timings and lowering transactional costs. The capital market also plays a vital role for developing integration among real and financial sector, equity and debt instruments, long term and short term funds, private sector and government sector, and domestic funds and external funds. It also directs the flow of funds into efficient channels through investment, disinvestment and reinvestment. The various roles of capital market include mobilisation of savings and acceleration of capital formation, promotion of industrial growth, raising of long term capital, provision of a variety of services, and efficient and optimum channelisation of funds. Some selective roles of the capital market are explained as follows.

1) **Mobilisation of Savings:** Capital market is an important source for mobilising idle savings from the economy. It mobilises funds from people for further investments in the productive channels of an economy. In that sense, it activates the ideal monetary resources and puts them in proper investments.

2) **Acceleration of Capital Formation:** Capital market helps in capital formation. Capital formation is net addition to the existing stock of capital in the economy. Through mobilisation of idle resources, it generates savings; the mobilised savings are made available to various segments such as agriculture, industry, etc. This helps in increasing capital formation.

3) **Provision of Investment Avenue:** Capital market raises resources for longer periods of time. Thus, it provides an investment avenue for people who wish to invest resources for a long period of time. It provides suitable interest rate returns also to investors. Instruments such as bonds, equities, units of mutual funds, insurance policies, etc. definitely provides diverse investment avenue for the public.

4) **Speed up Economic Growth and Development:** Capital market enhances production and productivity in the national economy. As it makes funds available for long period of time, the financial requirements of business houses are met by the capital market. It helps in research and development. This helps in, increasing production and productivity in economy by generation of employment and development of infrastructure.

5) **Proper Regulation of Funds:** Capital markets not only helps in fund mobilisation, but it also helps in proper allocation of these resources. It can have regulation over the resources so that it can direct funds in a qualitative manner.

6) **Service Provision:** As an important financial set up, capital market provides various types of services. It includes long term and medium term loans to industry, underwriting services, consultancy services, export finance, etc. These services help the manufacturing sector in a large spectrum.

7) **Continuous Availability of Funds:** Capital market is a place where the investment avenue is continuously available for long term investment. This is a liquid market as it makes fund available on continues basis. Both buyers and seller can easily buy and sell securities as they are continuously available. Basically capital market transactions are related to the stock exchanges. Thus, marketability in the capital market becomes easy.

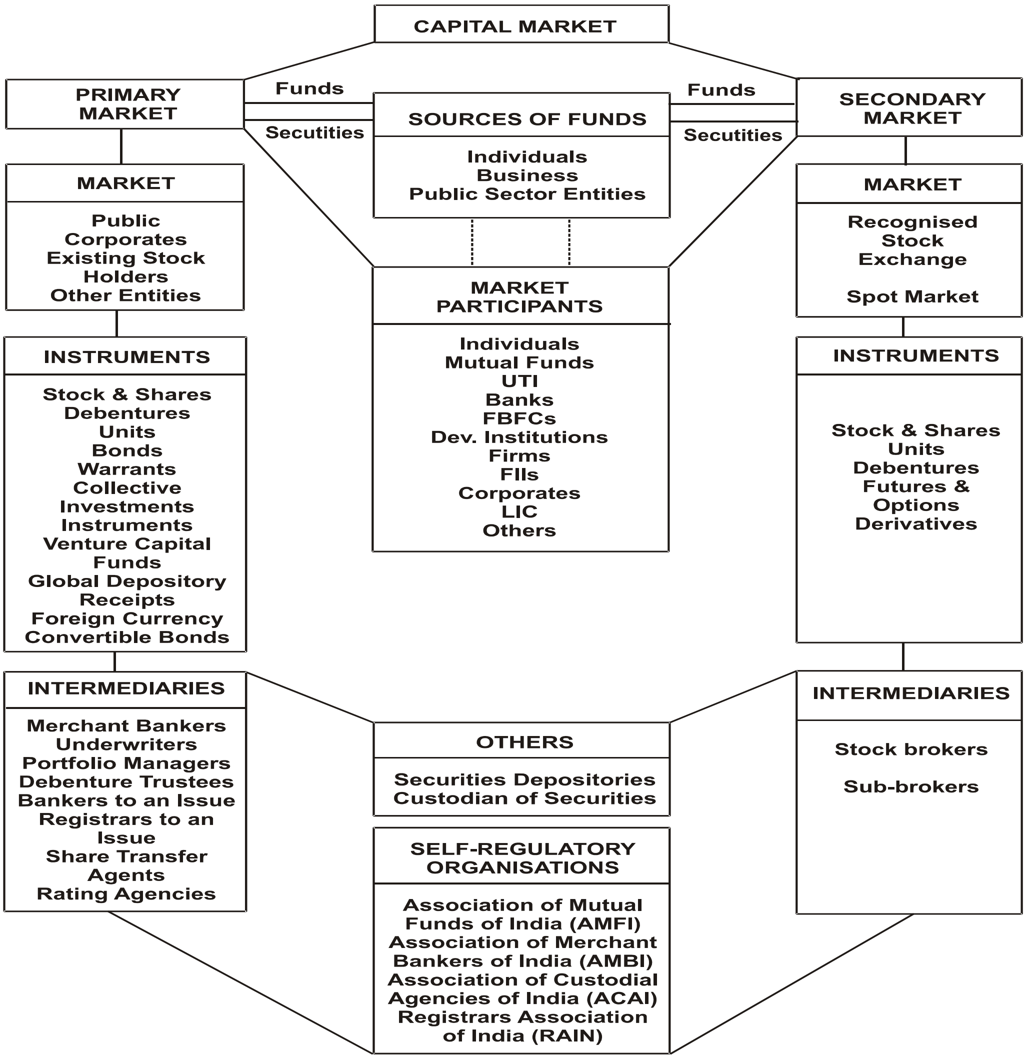

Figure 15.2 : Components of Indian Corporate Securities Markets

Check Your Progress 1

1) What are the constituents of financial system?

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2) Name the participants of capital market.

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3) Identify the major functions of capital market.

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15.3 STOCK MARKET DEVELOPMENT IN INDIA

The role of a stock market in the process of development has been well recognised. A developed stock market is considered as the major barometer of economic growth because (a) it provides an additional channel (along with banks and financial institutions) for encouraging and mobilising domestic savings, (b) ensures improvements in the productivity of investment through market allocation of capital, (c) increases managerial discipline through the market for corporate control. In brief, the various indictors of stock market development are Market Capitalisation Ratio (MCR)[1], which is considered as a measure of stock market size. In terms of the economic significance, market capitalisation as a proxy for the market size is positively related to the ability to mobilise capital and diversify risk. The next major indicator is market liquidity, which is measured by value-traded ratio and turnover ratio. Value traded ratio equals the total value of traded shares in the stock market divided by GDP. While, in turn, turnover ratio is the value of total shares traded divided by market capitalisation. The next important indicator of stock market development is the volatility parameter, which conceptualises the asset price movement in a stock market and conveys important signals for its development.

In the early stage of 1990s, there has been a marked change in the Indian securities market. A range of reforms such as measures for liberalisation, regulation and the development of the securities market have been introduced with the objectives of improving market efficiency, enhancing transparency, preventing unfair trade practices and bringing the Indian market up to international standards.

At the same time, the decade of the 1990s was marred by a steady procession of episodes of market misconduct, which regularly hit the front pages of newspapers. These episodes of market misconduct have been extremely disruptive of the core functions of the equity market, i.e. (a) pricing efficiency, and (b) intermediation between households investing in shares and firms financing projects by issuing shares. Many observers feel that the two major pieces of reform on the equity market – the creation of NSE in 1993 and the migration to rolling settlement and derivatives in 2001 – would not have taken place without the pressure of a recent crisis.

15.3.1 Motives for Reforms in the Stock market:

In brief, we can discuss the motives/problems behind reforms in the securities markets in the 1990s.

15.3.2 Liberalisation

The first motive of liberalisation through the new economic policy of 1991 has been giving freedom to the markets. This meant a shift away from administrative control of credit and government controls on prices of securities such as shares or government bonds and created a need to introduce an apex self-regulated body for regulation and development of the markets.

15.3.3 Monopoly of Association Type of Exchange

As of 1992, the Bombay Stock Exchange (BSE), an association of brokers, and imposed entry barriers, which led to elevated costs of intermediation was a monopoly

[1] The MCR is defined as the value of listed shares divided by GDP.

in the stock market. Membership was limited to individuals and limited liability firms could not become brokerage firms.

Due to Association nature of the Exchange, a lot of manipulative practices abounded, so that external users of a market often found themselves at the losing end of price movements as BSE was run by the brokers themselves.

Retail investors and particularly users of the market outside Bombay, accessed market liquidity through a chain of intermediaries called "sub-brokers". Each sub-broker in the chain introduced a mark-up in the price, in the absence of the unbundling of professional fees from the trade price. It was not uncommon for investors in small towns to face four intermediaries before their order reached the BSE floor, and to face mark-ups in excess of 10 per cent as compared with the actual trade price.

So a need was felt to establish a demutualised body in which the Trading members or brokers of the Exchange are separate from the management of the Exchange so that proper decision making as well as trading could be facilitated without the loss to any external investor.

15.3.4 Open Outcry System

Trading took place through 'open outcry' on the trading floor, which was inaccessible to users as it was being done through the gestures and body signs. It was routine for brokers to charge the investor a price that was different from that actually transacted at. Normal market practice was that the brokers were charging user's one single consolidated price without giving the full details of the trades, transactions and brokerage fees. The system was non-transparent and there was a need to have a transparent system in which the details about each and every transaction can be available.

15.3.5 Clearing, Settlement and Risk Management Problems

The market used 'futures-style settlement' with fortnightly settlement the period of which was running between 14 to 30 days. This means that trading was supposed to take place for a fortnight until a predetermined 'expiration date'. Open positions on the expiration date only would go into actual settlement, where funds and securities were exchanged. In practice, there was little discipline on ensuring a reliable fortnightly settlement cycle. A peculiar market practice called *badla* allowed brokers to carry positions across settlement periods. In other words, even open positions at the end of the fortnight did not always have to be settled. So a need was felt to have a timely as well as accurate and fast reliable settlement system.

The efficiencies of the exchange clearinghouse only applied for the largest 100 stocks. For other stocks, clearing and settlement were done bilaterally, which introduced further inefficiencies and costs. The use of futures-style trading for a fortnight (or more), coupled with *badla*, is fraught with counterparty risk. Normally, collateral (margin) requirements are used to ensure capital adequacy, and reduce the weakness of the clearing system. A critical feature of the modern approach to clearing is "novation" at a clearing corporation; the existing association type exchanges had neither a Clearing Corporation nor novation. The clearing houses of such exchanges were not providing the guard against counter party risk. So, the concept of separate clearing house or clearing corporation was necessary to avoid such kind of situations.

The final flaw of the trade was physical settlement, where share certificates were printed on paper and on the settlement day the physical share certificates were transferred in exchange of the funds. The system of transfer of ownership was grossly inefficient as every transfer involved physical movement of paper securities to the issuer for registration, with the change of ownership being evidenced by an endorsement on the security certificate. In many cases, the process of transfer took much longer, and a significant proportion of transactions ended up as bad delivery due to faulty compliance of paper work. This was intrinsically vulnerable to theft, counterfeiting, inaccurate signature verification, administrative inefficiencies, and a variety of other malpractices. If stock splits, rights issues, or dividend payouts took place during this period, it was common for the purchaser to be away from the genuine benefits. So electronic transfer and dematerialisation of the securities were found necessary so that such problems of physical delivery of the stocks can be avoided.

15.3.6 The Scams in the Decade of 1990s

The first "stock market scam" was one, which involved both the GOI bond and equity markets in India by Harshad Mehta in 1992 involving around Rs. 54 billion, the biggest scam Indian market has ever faced. The manipulation was based on the inefficiencies in the settlement systems in GOI bond market transactions.

When anonymous trading and nation-wide settlement became the norm by the end of 1995, there was an increasing incidence of fraudulent shares being delivered into the market. It has been estimated that the expected cost of encountering fake certificates in equity settlement in India at the time was as high as 1 per cent (Shah & Thomas 1997). This scam gave a look and consideration at the need of dematerialised form of securities.

Second biggest scam of about Rs. 7 billion in Indian market after Harshad Mehta was in 1997 by CRB group, which was a conglomerate of finance and non-finance companies. The finance companies of the group sourced the funds from external sources, using manipulated performance numbers, which revealed the failures of supervision on the part of RBI and SEBI.

Another episode of 1992 Harshad Mehta scam came out in 1998. In this episode of market manipulation, the President, Executive Director and Vice President of the BSE had to resign as the top management of the BSE was found to tampering with records in the trading system in trying to avert a payments crisis.

The most discussed scam after Harshad Mehta and CRB group was the scam by *Ketan Parekh* who took leveraged positions on a set of 10 stocks called the "K10 stocks" stimulating the fall in the prices of IT stocks globally. There are allegations of fraud in this crisis with respect to an illegal *badla* market at the Calcutta Stock Exchange and banking fraud. Investigations for this are still under way.

Due to the procession of crises and scams coming out one after another a big question mark was there on the credibility of SEBI and its capability to regulate and develop the securities market. However, SEBI gave an appropriate response to these crises and scams by more regulated, efficient and transparent environment though imposition of investor protection guidelines, ban on *badla system*, introduction of rolling settlement and other measures.

15.4 STOCK MARKET REFORMS SINCE 1992

In response to the above mentioned motives and problems, the principal reform measures undertaken in Indian stock market since 1992 in detail can be discussed as follows:

15.4.1 Establishment of SEBI

Under the Capital Issues (Control) Act, 1947 any firm wishing to issue securities had to obtain approval from the Central Government for the decision of the amount, type and price of the issue. To cope up with the Liberalisation policy of 1991, the said Act was repealed in 1992 for market determined allocation of resources and another regulator Security Exchange Board of India (SEBI) was created and assigned with the main responsibilities for:

a) protecting the interests of investors particularly of small investors in securities,

b) promoting the development of the securities market, and

c) regulating the securities market.

Having been assigned the regulatory jurisdiction not only over the corporate in the issuance of capital and transfer of securities, but also over all intermediaries and persons associated with securities market, SEBI was given concurrent/delegated powers under certain provisions of the Companies Act and the SC(R) Act. Many provisions in the Companies Act having a bearing on securities market are administered by SEBI.

15.4.2 Market Determined Allocation of Resources and Investor Protection

Due to repeal of CC (I) A and establishment of SEBI, Government's control over issue of capital, pricing of the issues, fixing of premia and rates of interest on debentures etc. ceased and the allocation of resources for competing uses left to the market.

In the interest of investors, SEBI issued Disclosure and Investor Protection (DIP) guidelines containing a substantial body of requirements for issuers/intermediaries. SEBI specifies the matters to be disclosed and the standards of disclosure required for the protection of investors in respect of issues and accordingly SEBI has issued directions to all intermediaries and other persons associated with the securities market in the interest of investors or of orderly development of the securities market. Thus, The SEBI guidelines aim to secure fuller disclosure of relevant information about the issue, issuer and the nature of the securities to be issued so that investors can take informed decisions.

Department of Economic Affairs (DEA), Department of Company Affairs (DCA), SEBI have set up investor grievance cells and the Exchanges have for redressal of investor grievance. The exchanges maintain investor protection funds/consumer protection funds/trade guarantee funds to take care of investor claims, which may arise out of non-settlement of obligations by a trading member for trades executed on the exchange. DCA has also set up an investor education and protection fund for the promotion of investors' awareness and protection of interest of investors.

15.4.3 Demutualisation and Establishment of NSE

The idea of NSE was first contemplated seriously in 1993. At that time the OTCEI was a recent state-sponsored exchange, which had not shown a good record. And also the fear that NSE would be going up in competition against the established liquidity of the BSE. However, for the benefit of the investors and corresponding to the need of setting up of a demutualised Exchange, equity trading at NSE commenced in November 1994. Within one year of the commencement of equity trading at NSE, it became India's most liquid stock market. This was a remarkable outcome. The BSE responded rapidly by moving to similar technology to the NSE in March 1995. The benefits of demutualised Exchange with the improvements in the securities market led to regime-shift towards transparency, anonymity, Competition in the brokerage industry, Operational Efficiency etc.

For better implementation of the concept of demutualisation, the regulators focused on reducing dominance of members in the management of stock exchanges and advised them to reconstitute their governing councils to provide for at least 50 per cent non-broker representation. As the recommendation did not materially alter the situation, the Government proposed in March 2001 to corporate the stock exchanges by which ownership, management and trading membership would be segregated from one another. A few exchanges have already initiated demutualisation process. Government has offered a variety of tax incentives to facilitate corporatisation and demutualisation of stock exchanges.

15.4.4 Screen Based Trading

In order to provide efficiency, liquidity and transparency, NSE introduced a nation-wide on-line fully-automated screen based trading system (SBTS) where a member can punch into the computer quantities of securities and the prices at which he likes to transact and the transaction is executed as soon as it finds a matching sale or buy order from a counter party.

Providing the solution for the problems arising from the open outcry system, in terms of infrastructure, practices and approach, Indian market has become as modern as any developed market of the world. All Exchanges in India switched from floor trading to anonymous electronic trading by 1994.

15.4.5 Risk Containment at the Clearing Corporation

To effectively address the issue of assessing the credit risk of the counter-party and to guarantee the final settlement of the transaction, NSE introduced the concept of a novation, and set up the first clearing corporation, viz. National Securities Clearing Corporation Ltd. (NSCCL), which commenced operations in April 1996. Counterparty risk is guaranteed through a fine tuned risk management system and an innovative method of on-line position monitoring and automatic disablement. A large Settlement Guarantee Fund provides the cushion for any residual risk. In order to boost the process of corporatisation, capital gains tax payable on the difference between the cost of the individual's initial acquisition of membership and the market value of that membership on the date of transfer to the corporate entity was waived.

15.4.6 Risk Management

To prevent market failures and protect investors, the regulator/exchanges have developed a comprehensive risk management system, which is constantly monitored and upgraded by the Exchanges and the regulators. It encompasses capital adequacy of members, net-worth criteria, adequate margin requirements (comprising of initial margin, daily marked to market margin, variation margin), limits on exposure and turnover, indemnity insurance, on-line position monitoring and automatic disablement on crossing the limits, etc. They also administer an efficient market surveillance system to curb excessive volatility, detect and prevent price manipulations. Exchanges have set up trade/settlement guarantee funds for meeting shortages arising out of non-fulfilment/partial fulfilment of funds obligations by the members in a settlement.

15.4.7 Dematerialisation

To obviate the problems related to physical delivery of securities, the Depositories Act, 1996 was passed to provide for the establishment of depositories (NSDL and CDSL) in securities with the objective of ensuring free transferability of securities with speed, accuracy and security by (a) making securities of public limited companies freely transferable subject to certain exceptions; (b) dematerialising the securities in the depository mode; and (c) providing for maintenance of ownership records in a book entry form.

The stamp duty on transfer of demat securities was waived. Today, all actively traded scrips are held, traded and settled in demat form. Demat settlement accounts for over 99.9 per cent of turnover settled by delivery.

Before dematerialisation was started, SEBI used to get about fifty thousand complaints every year for non-transfer of shares. SEBI has an unenviable record of getting 2.7 million complaints in ten years. Lately of course the number of complaints came down, particularly after dematerialisation. This has also prevented cases where company management's delayed transfer of shares; it is now automatic.

To prevent physical certificates from sneaking into circulation, it has been made mandatory for all new IPOs to be compulsorily traded in dematerialised form. For making a public or rights issue or an offer for sale, the admission to a depository for dematerialisation of securities has been made compulsorily as a pre-requisite. It has also been made compulsory for public listed companies making IPO of any security for Rs.10 crore or more to do the same only in dematerialised form.

15.4.8 Derivatives Trading

A three-decade old ban on forward trading, which had lost its relevance and was hindering introduction of derivatives trading, was withdrawn in 1999 by way of an amendment in SC(R) Act, 1954. Considering the recommendations of L. C. Gupta Committee on derivatives trading, derivative trading was started in June 2000 on two exchanges namely, NSE and BSE. The market presently offers index futures and index options on two indices and stock options and stock futures on certain specified stocks. Recently, the interest rate futures have also started on NSE.

15.4.9 Globalisation

Indian companies have been permitted to raise resources from abroad through issue of American Depository Receipts (ADRs), Global Depository Receipts (GDRs), Foreign Currency Convertible Bonds (FCCBs) and External Commercial Borrowings (ECBs). ADRs/GDRs have two-way fungibility. Indian companies are permitted to list their securities on foreign stock exchanges by sponsoring ADR/ GDR issues against block shareholding. Non Resident Indians (NRIs) and Overseas Corporate Body (OCBs) are allowed to invest in Indian companies.

FIIs have been permitted to invest in all types of securities, including government securities. The investments by FIIs enjoy full capital account convertibility. They can invest in a company under portfolio investment route upto 24 per cent of the paid up capital of the company. This can be increased up to the sectoral cap/ statutory ceiling, as applicable, provided this has the approval of the Indian company's board of directors and also its general body.

Indian Stock Exchanges have been permitted to set up trading terminals abroad. The trading platform of Indian exchanges is now accessed through the Internet from anywhere in the world. Mutual Funds have been permitted to set up offshore funds to invest in equities of other countries. They can also invest in ADRs/GDRs of Indian companies.

15.4.10 Rolling Settlement and Ban on Deferral Products

Due to long trading cycle and the large open positions which was running about 14 to 30 days, the counterparty risk was very high resulting into defaults and risks in settlement on many occasions. In order to reduce large open positions, the trading cycle was reduced over a period of time to a week.

The normal practice of trading a variety of deferral products like modified carry forward system, which was called, as *badla system* was also prevalent, which encouraged leveraged trading by enabling postponement of settlement. In 2001, "Future style settlement" and deferral mechanisms, which implied that the spot market featured leverage and futures market principles, were banned in favour of rolling settlement.

In 1998, rolling settlement on T+5 basis was introduced in respect of specified scrips reducing the trading cycle to one day. The exchanges, however, continued to have different weekly trading cycles, which enabled shifting of positions from one exchange to another. It was made mandatory for all exchanges to follow a uniform weekly trading cycle in respect of scrips not under rolling settlement. All scrips were moved to rolling settlement from December, 2001. In April 2002, T+3 rolling settlement were introduced replacing T+5 settlements. Now of course we have the rolling settlement, where settlements happen the same day.

Corresponding the necessity of the market, problems of irregulation and manipulation in the market and need of more transparent system in the Indian Securities Market, the above reforms were introduced in stages. As some deficiency is noted or some malpractice surfaces in the working of the market, the concerned authorities initiated further reforms and corrective steps. A number of steps have been taken to improve efficiency, transparency and confidence of the investors in the market. However, the process of reform in the securities market is far from complete.

15.5 STRUCTURE AND PERFORMANCE OF INDIAN STOCK MARKET

There are 22 stock exchanges in India, the first being the Bombay Stock Exchange (BSE), which began formal trading in 1875, making it one of the oldest in Asia. In 2010, the number of stock exchanges in India reduced to 19 as The Magadh, Mangalore, Hyderabad and Saurashtra Kutch stock exchanges have been derecognised by the market watch dog Securities Exchange Board of India (SEBI). Before 1994, India's stock markets were dominated by BSE. In other parts of the country, the financial industry did not have equal access to markets and was unable to participate in forming prices, compared with market participants in Mumbai (Bombay). As a result, the prices in markets outside Mumbai were often different from prices in Mumbai. These pricing errors limited order flow to these markets. Explicit nationwide connectivity and implicit movement toward one national market has changed this situation (Shah and Thomas, 1997). NSE has established satellite communications which give all trading members of NSE equal access to the market. Similarly, BSE and the Delhi Stock Exchange are both expanding the number of trading terminals located all over the country. The arbitrages are eliminating pricing discrepancies between markets. Over the last few years, there has been a rapid change in the Indian securities market, especially in the secondary market. Advanced technology and online screen based transactions have modernised the stock exchanges. In terms of the number of companies listed and total market capitalisation, the Indian equity market is considered large relative to the country's stage of economic development. The number of listed companies increased from 5,968 in March 1990 to about 10,000 by May 1998 and market capitalisation has grown almost 11 times during the same period. In the financial year 1990-91, the market capitalisation has increased in BSE from Rs. 90,836 crore to Rs. 61,65,619 crore in 2009-10. Similarly, the market capitalisation in case of NSE in 1994-95 has increased from Rs. 3,63,350 crore to Rs. 60,09,173 crore in the year 2009-10. During the same time the annual averages of stock price in case of BSE Sensex has increased from Rs.1,050 crore to Rs.15,585 crore in 2009-10. However the annual averages of share price in case of S&P CNX Nifty has increased from Rs. 364 crore to Rs. 4,658 crore. The annual turnover at Bombay Stock Exchange has increased from Rs.1,57,88,856 crore in 2007-08 to Rs.11,03,467 crore and at National Stock Exchange; the annual turnover has increased from Rs. 3551038 crore in 2007-08 to Rs. 35,77,412 crore in 2010-11. Likewise the Net investment in the Indian capital market has increased to Rs. 62,583.56 crore to Rs.1,10,718.27 crore in the the financial year 2010-11. The quantity of shares traded in the stock exchanges has increased from 5,04,149 lakh in 2001-02 to 33,42,947 lakh in 2009-10. The value of the shares delivered of stock exchanges has increased from Rs.1,36,225 to Rs. 12,28,612 crore in 2009-10.

Check Your Progress 2

1) Why does a developed stock market is considered the barometer of economic growth?

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2) What is market capitalisation Ratio?

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3) State the problems of stock market leading reforms in this sector during 1990s.

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4) What is Demutualisation? State the benefits of demutualised Exchange.

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5) Which steps have been taken by the regulations/exchanges to prevent market failures and protect the interest of investors?

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15.6 EQUITY DERIVATIVES IN INDIA

A derivative security is a financial contract whose value is derived from the value of something else, such as a stock price, a commodity price, an exchange rate, an interest rate, or even an index of prices. Derivatives may be traded for a variety of reasons. A derivative enables a trader to hedge some pre-existing risk by taking positions in derivatives markets that offset potential losses in the underlying or spot market. In India, most derivatives users describe themselves as hedgers (Fitch Ratings, 2004) and Indian laws generally require that derivatives be used for hedging purposes only. Another motive for derivatives trading is speculation (i.e. taking positions to profit from anticipated price movements). In practice, it may be difficult to distinguish whether a particular trade was for hedging or speculation, and active markets require the participation of both hedgers and speculators. A third type of trader, called arbitrageurs, profit from discrepancies in the relationship of spot and derivatives prices, and thereby help to keep markets efficient. Equity derivatives trading started in India in June 2000, after a regulatory process which stretched over more than four years. In July 2001, the equity spot market moved to rolling settlement. India's experience with the launch of equity derivatives market has been extremely positive, by world standards. NSE is now one of the prominent exchanges amongst all emerging markets, in terms of equity derivatives turnover. There is an increasing sense that the derivatives market is playing a major role in shaping price discovery.

15.6.1 Exchange-Traded and Over-the-Counter Derivative Instruments

OTC (over-the-counter) contracts, such as forwards and swaps, are bilaterally negotiated between two parties. The terms of an OTC contract are flexible, and are often customised to fit the specific requirements of the user. OTC contracts have substantial credit risk, which is the risk that the counterparty that owes money defaults on the payment. In India, OTC derivatives are generally prohibited with some exceptions: those that are specifically allowed by the Reserve Bank of India (RBI) or, in the case of commodities (which are regulated by the Forward Markets Commission), those that trade informally in "havala" or forwards markets. An exchange-traded contract, such as a futures contract, has a standardised format that specifies the underlying asset to be delivered, the size of the contract, and the logistics of delivery. They trade on organised exchanges with prices determined by the interaction of many buyers and sellers. In India, two exchanges offer derivatives trading: the Bombay Stock Exchange (BSE) and the National Stock Exchange (NSE). However, NSE now accounts for virtually all exchange-traded derivatives in India, accounting for more than 99 per cent of volume in 2003-2004. Contract performance is guaranteed by a clearinghouse, which is a wholly owned subsidiary of the NSE Margin requirements and daily marking-to-market of futures positions substantially reduce the credit risk of exchange-traded contracts, relative to OTC contracts (Asani Sarkar 2006).

In the exchange-traded market, the biggest success story has been derivatives on equity products. Index futures were introduced in June 2000, followed by index options in June 2001, and options and futures on individual securities in July 2001 and November 2001, respectively. As of 2005, the NSE trades futures and options on 118 individual stocks and 3 stock indices. All these derivative contracts are settled by cash payment and do not involve physical delivery of the underlying product. Derivatives on stock indexes and individual stocks have grown rapidly since inception. In particular, single stock futures have become hugely popular, accounting for about half of NSE's traded value in October 2005. In fact, NSE has the highest volume (i.e. number of contracts traded) in the single stock futures globally, enabling it to rank 16 among world exchanges in the first half of 2005. Single stock options are less popular than futures. Index futures are increasingly popular, and accounted for close to 40 per cent of traded value in October 2005. NSE launched interest rate futures in June 2003 but, in contrast to equity derivatives, there has been little trading in them. One problem with these instruments was faulty contract specifications, resulting in the underlying interest rate deviating erratically from the reference rate used by market participants. Institutional investors have preferred to trade in the OTC markets, where instruments such as interest rate swaps and forward rate agreements are thriving. As interest rates in India have fallen, companies have swapped their fixed rate borrowings into floating rates to reduce funding costs. However, it may be noted that the detailed discussion of Equity Derivative instruments is beyond the scope of this unit.

Table 15.1 : Turnover in Indian Equity Derivatives Market.

Equity Derivatives				(' Crore)
Year	**Index Future**	**Index Options**	**Stock Futures**	**Stock Options**
2008-09	35,81,870	37,31,512	34,79,657	2,29,227
2009-10	39,34,485	80,28,103	51,95,247	5,06,065
2010-11	43,56,909	1,72,69,366	54,95,757	10,30,343
2011-12				
Apr	2,82,313	16,45,980	3,53,162	69,993
May	3,05,746	18,92,896	3,36,689	70,090
June	2,65,191	17,84,570	3,22,695	65,792

Source: RBI, BSE, NSE, CCIL and SEBI.

15.7 FOREIGN EXCHANGE MARKET DEVELOPMENT IN INDIA

Historically, the rupee was pegged to the pound sterling till late sixties. Under the Bretton wood system, as a member of IMF, India declared its par value of rupee in terms of gold. The RBI maintained par value of rupee within the permitted band of ±1 per cent using Pound Sterling as the intervention currency. India had to devalue its currency in June 1966. The par value of rupee was fixed at 0.118489 of fix gold per Indian Rupee. The corresponding Rupee sterling rate was fixed GBP1= Rs 18.

With the collapse of Bretton woods system in August 1971, major currencies discarded fixed exchange rate regime. Rupee was pegged to US$ and the exchange rate was fixed at US$1= Rs. 7.50. However, RBI retained with pound sterling as the intervention currency. The US$ and Rupee pegging was used to arrive at Rupee Sterling parity. After Smithsonian Agreement in December 1971, the Rupee was again delinked from US$ and again linked to Pound Sterling. This parity was maintained within a band of ±2 ¼ per cent. In 1972, Pound Sterling gradually started floating. As the Rupee was pegged to Sterling, as a result of which Rupee fluctuated with other currencies as the Sterling fluctuated vis-à-vis other currencies of the world. Afterwards, Pound Sterling was depreciated by 20 per cent by September 1975 because of the poor fundamentals of the British economy. Then Rupee got depreciated automatically against the other currencies of the world. It led to rise in inflation in India to undesired levels. With effect from September 25, 1975, Rupee was again delinked from Pound Sterling and was linked to basket of currencies. The currencies included in the basket as well as their relative weights were kept secret so that speculator could not identify the direction or the movement of exchange rate of the Rupee. The main advantage of linking Rupee with the basket of currencies was that it would no longer be dependent on the vagaries of a single currency. As a result, RBI was free to exercise its discretion to alter the currency components in the basket without allowing market to speculate on Rupee exchange rate.

The liquidity crunch in 1990 and 1991 on the forex front underpinned the significance of managing the exchange rate effectively. Thus on March 1st, 1992, RBI announced a new exchange rate system known as "Liberalised Exchange Rate Management System" (LERMS) with the prime objective to make balance of payments sustainable on ongoing basis by allowing market forces to play a greater role. As per LERMS, Rupee became convertible for all approved external transactions. The exporters were allowed to sell 60 per cent of their foreign receipts at market determined rates and required to surrender 40 per cent of their foreign receipts to RBI through authorised dealers' official rate. Thus, this system prevailed during 1992 in which the exchange rate regime in India was characterised by a daily announcement by the RBI of its buying and selling rates to authorised dealers for merchant transactions.

The process of liberalisation was continued further and Reserve Bank decided to make Rupee fully floating on the current account with effect from March 1, 1993.The new arrangement came to be called Modified Liberalised Exchange Rate Management System (MLERMS). With the introduction of MLERMS, all foreign exchange transactions under current account of balance of payments were being put through Authorised Dealers (Ads) at market determined exchange rates. Foreign exchange receipts and payments continued to be governed by Exchange Control

Regulations. Thus the introduction of MLERMS helped to bring more flexibility in the foreign exchange market such as removal of several trade restrictions, relaxation in exchange control particularly under current account transactions in order to achieve the full benefits of the integrating the Indian economy with world economic system etc.

With the continued process of liberalisation, RBI has been guided by the needs of further development of foreign exchange markets. On November 22, 1994, it has been decided to set up "The Expert Group on Foreign Exchange Markets in India" to examine the issues relating to products available for hedging forex risks, scope for further development of forex market and introducing of new derivative products in India under the chairmanship of Mr. O P Sodhani. The group studied the market in detail and the report finally came in June 1995 with 33 recommendations and out of these, 25 called for actions on the part of RBI. Some of the important recommendations of the committee were (i) the banks should be accorded significant initiative and freedom to participate in the forex market such as freedom to fix net overnight position limit and gap limits, although RBI is formally approving these limits, freedom to initiate trading position in the overseas markets, freedom to borrow or invest funds in the overseas markets (up to 15 per cent of Tier 1 capital), freedom to determine the interest rates (subject to a ceiling) and maturity period of Foreign Currency Non-Resident (FCNR) deposit (not exceeding three years), freedom to exempt inter-bank borrowings from statutory pre-emptions and freedom to use derivative products for asset liability management. (ii) Corporate should be permitted to take hedge upon declaring the existence of genuine exposure. But this facility has been temporarily suspended after the Asian crisis. Corporates having Exchange Earners Foreign Currency Accounts (EEFCAs) should be allowed margin trading by using the balances in their EEFC accounts. Corporates were given freedom to cancel or rebook forward contracts though currently due to the Asian crisis effect, freedom to rebook or cancelled contracts has been suspended while roll over is permissible, (iii) Authorised Dealers may be permitted to initiate cross currency positions abroad, (iv) market intervention by RBI should be on selective basis, (v) number of participants in forex markets should be increased by permitting financial institutions like IDBI, IFCI etc. to trade in the forex market. So far as the recommendations are concerned, some of them are also not yet implemented because of some constraints like speculation.

Gradual liberalisation process in the development of forex market needed the requirement of capital account convertibility in the early stage of 1997. Reserve bank of India on February 28, 1997 set up a committee on Capital Account Convertibility, which is popularly known as Tarapore committee.

Tarapore committee quoted the definition of 'Capital Account Convertibility' as 'Capital Account Convertibility refers to the freedom to convert local financial assets into foreign financial assets and vice versa at market determined rates of exchange.' The major recommendations of the committee broadly related to foreign direct investment, portfolio investment, investment in joint ventures, project exports, opening of Indian corporate offices abroad, raising of EEFC entitlement to 50 per cent, allowing FIIs to cover forward in part of their exposures in the debt and equity market.

Emphasising the exchange rate policy, the committee strongly recommended that the RBI should have monitoring exchange rate band of ± 15 per cent around the neutral Real Effective Exchange Rate (REER). The RBI should ordinarily intervene when REER is outside the band. The committee stresses that the credibility of exchange rate policy should be vital in the context of Capital Account Convertibility (CAC), which will bring the transparency in the exchange rate policy.

The committee strongly recommended that in view of the growing degree of integration of the Indian economy, the size of the current account deficit can be sustained without encountering external constraint. In the context of moving to capital account convertibility, capital flows would have a more significant effect on balance of payments. The committee has specified some indicators of foreign exchange reserves such as reserves should not be less than the six months imports, reserve should not be less than the three months imports plus 50 per cent of debt service payments plus one month's imports and exports etc.

With the above recommendations, a significant progress has been noticed. In the money market, for improving the risk management, recent guidelines for interest rate swaps and Forward Rate Agreement (FRAs) have been issued to facilitate hedging of interest rate risks and orderly development of fixed income derivative markets. Measures have also been taken to develop Government securities market and permission has also been given to banks for fulfilling certain criteria to import gold for domestic sale. This aspect of gold policy is a major step in bringing off-market forex transactions into forex markets by officialising the import of gold.

15.8 CURRENCY DERIVATIVE MARKET IN INDIA

Currency derivative is a contract between the seller and buyer, whose value is to be derived from the underlying asset, the currency amount. A derivative based on currency exchange rates is a future contract which stipulates the rate at which a given currency can be exchanged for another currency as at a future date.

Foreign exchange derivatives are less active than interest rate derivatives in India, even though they have been around for longer period. OTC instruments in currency forwards and swaps are the most popular. Importers, exporters and banks use the rupee forward market to hedge their foreign currency exposure. Turnover and liquidity in this market has been increasing, although trading is mainly in shorter maturity contracts of one year or less. In a currency swap, banks and corporations may swap its rupee denominated debt into another currency (typically the US dollar or Japanese yen), or vice versa. Trading in OTC currency options is still muted. There are no exchange-traded currency derivatives in India.

15.8.1 Exchange Traded Currency Derivatives in India

The currency futures market in India remained active during 2010-11. The average daily turnover in currency futures on the three active exchanges (NSE, MCX-SX and USE) stood at US $ 8.0 billion in March 2011 as against US $ 7.1 billion in March 2010. Increased globalisation of the economy increases the foreign exchange exposure of Indian firms and individuals with exchange rate risk arising from domestic and global financial market developments. This has necessitated introduction of various instruments by the Reserve Bank to hedge the exchange exposure by the residents. Currently, residents in India are permitted to trade in futures contracts in four currency pairs on recognised stock exchanges. In order to expand the menu of tools for hedging currency risk, recognised stock exchanges were permitted to introduce plain vanilla currency options on spot US Dollar/Rupee exchange rate for residents. The exchange traded currency options market is functioning subject to the guidelines issued by the Reserve Bank and the Securities and Exchange Board of India (SEBI) from time to time. In view of the large positions held by the FIIs and considering the increased depth of the Indian forex market to absorb the impact on the exchange rate, FIIs have now been permitted to cancel and rebook up to 10 per cent of the market value of the portfolio as at the beginning of the financial year as against 2 per cent that was permitted earlier. The summary report of the Indian Currency Derivative market is presented as follows:

Table 15.2: Turnover in Indian Currency Derivatives Market.

Currency Derivatives			(in Rs. ' Crore)
Year	**Forward**	**Swap**	**Exchange Traded Currency Options and Futures**
2008-09	25,54,994	40,65,695	3,11,389
2009-10	20,35,879	31,45,402	37,27,262
2010-11	28,90,222	41,12,539	84,06,307
2011-12			
Apr	2,06,047	3,67,137	7,22,275
May	2,17,188	4,74,893	10,00,498
June	2,40,047	4,95,622	10,39,010

Source: BSE,NSE, CCIL and SEBI.

15.9 LONG TERM GOVERNMENT BOND AND CORPORATE DEBT MARKET IN INDIA

The corporate bond and long term Government Securities market is the vital segment of the capital market. The corporate bond market is at the budding phase in India. The corporate bond market remains restricted in regards to participants, largely arbitrage driven and also highly illiquid. The lack of development is anomalous for two reasons: First, India has developed world-class markets for equities and for equity derivatives supported by high-quality infrastructure. And second, the infrastructure for the bond market, particularly the government bond market, is similarly of high quality. Until 2007, information on Indian corporate bond market turnover was incomplete and largely anecdotal. In 2007, however, the Securities and Exchange Board of India (SEBI) launched initiatives to ensure more comprehensive reporting of the over-the-counter (OTC) bond market. Current volumes are running at low levels — around 140 transactions amounting to about USD80 million per day. But corporate bond markets worldwide are typically illiquid, so it may be overly optimistic to expect India to develop a uniquely liquid corporate bond market. Nonetheless, a more liquid market should eventually contribute to lower costs of capital for issuers. India's corporate turnover ratio is quite high at 70 per cent in 2007, comparing favourably with most other emerging East Asian corporate bond markets. However, the small total of outstanding corporate bonds in India means that the secondary market is small and relatively illiquid, irrespective of the turnover ratio. (ADB Working Paper Series No.22).

A significant momentum of functioning debt (G-sec) market in India was really initiated in the wake of New Economic Policy in 1991. Prescription of indirect instruments of monetary control such as 'Statutory Liquidity Ratio'(SLR) i.e. the ratio at which banks are required to invest in approved securities, though originally devised as a prudential measure, was used as the main instrument of pre-emption of bank resources in the pre reform period. The high SLR requirement created a captive market for government securities, which were issued at low administered interest rates. After the initiation of the reforms this ratio has been reduced in phases to the statutory minimum level of 25 per cent. Over the past few years numerous steps have been taken to broaden and deepen the government securities market and to raise the level of transparency. Government's deficit has been phased out and the market borrowings of the central government are presently undertaken through a system of auctions at market related rates. The various selective reforms in government securities market in India are as follows:

- Administered interest rates on government securities were replaced by an auction system for price discovery.
- Automatic monetisation of fiscal deficit through the issue of ad hoc Treasury Bills was phased out.
- Primary Dealers (PD) were introduced as market makers in the government securities market.
- For ensuring transparency in the trading of government securities, delivery versus Pay (DvP) settlement system was introduced.
- Repurchase agreements (repo) were introduced as a tool of short-term liquidity adjustment. Subsequently, the Liquidity Adjustment Facility (LAF) was introduced. LAF operates through repo and reverse auctions to set up a corridor for short-term interest rate. LAF has emerged as the tool for both liquidity management and also signalling device for interest rates in the overnight market.
- Market Stabilisation Scheme (MSS) has been introduced, which has expanded the instruments available to the Reserve Bank for managing the surplus liquidity in the system.
- 91-day Treasury bill was introduced for managing liquidity and benchmarking. Zero Coupon Bonds, Floating Rate Bonds, Capital Indexed Bonds were issued and exchange traded interest rate futures were introduced. OTC interest rate derivatives like Interest Rate Swap, Forward Rate Agreements were introduced.

The Indian Primary market in Corporate Debt is basically a private placement market with most of the corporate bond issues being privately placed among the wholesale investors i.e. the Banks, Financial Institutions, Mutual Funds, Large Corporate and other large investors. The proportion of public issues in the total quantum of debt capital issued annually has decreased in the last few years. Around 92 per cent of the total funds mobilised through corporate debt securities in the Financial Year 2002 were through the private placement route.

The Secondary Market for Corporate Debt can be accessed through the electronic order-matching platform offered by the Exchanges. BSE offers trading in Corporate Debt Securities through the automatic BOLT system of the Exchange. The Debt Instruments issued by Development Financial Institutions, Public Sector Units and the debentures and other debt securities issued by public limited companies are listed in the 'F Group' at BSE. The various types of corporate debt securities in

India issued consists of Non Convertible Debentures, Partly-Convertible Debentures/Fully-Convertible Debentures (convertible in to Equity Shares), Secured Premium Notes, Debentures with Warrants, Deep Discount Bonds, PSU Bonds/ Tax-Free Bonds.

15.9.1 Outlook for Development of Corporate Debt Market

The development of a corporate bond market in India has lagged behind in comparison with other financial market segments owing to many structural factors. While primary issuances have been significant, most of these were accounted for by public sector financial institutions and were issued on a private placement basis to institutional investors. The secondary market, therefore, has not developed commensurately and market liquidity has been an issue.

The Government had constituted a High Level Committee on Corporate Bonds and Securitisation (Patil Committee) to identify the factors inhibiting the development of an active corporate debt market in India and recommend necessary policy actions. The Committee made a number of recommendations relating to rationalising the primary issuance procedure, facilitating exchange trading, increasing the disclosure and transparency standards and strengthening the clearing and settlement mechanism in secondary market. The recommendations have been accepted in principle by the Government, RBI and SEBI and are under various stages of implementation.

The two stock exchanges, namely, the Bombay Stock Exchange (BSE) and the National Stock exchange (NSE), as well as the industry body Fixed Income, Money Market and Derivatives Association of India (FIMMDA) have since operationalised respective trade reporting platforms. While all the exchange trades in corporate bonds get captured by concerned exchange's reporting platform, OTC transactions can be reported on any of these platforms. The aggregated trade information across the platforms is being disseminated by FIMMDA on its website. BSE and NSE have also started order driven trading platforms in July 2007. In practice, however, trading still continues to be largely OTC. SEBI has also implemented measures to streamline the activity in corporate bond markets by reducing the shut period in line with that of G-sec, reducing the size of standard lots to Rs. one lakh and standardising the day count convention. Further, to streamline the process of interest and redemption payments, Electronic Clearing Services (ECS), Real time Gross Settlements (RTGS) or National Electronic Funds Transfer (NEFT) are required to be used by the issuers.

Further progress is anticipated in regard to rationalising the primary issuance procedures, which is a critical step for moving away from the pre-dominance of private placements. To reduce the settlement risk and enhance efficiency, the Patil Committee has also proposed setting up of a robust clearing mechanism. The settlement was proposed to be initially on DvP I basis (i.e. trade by trade basis) to address the counterparty settlement risk and gradually migrate to DvP III (net settlement of funds as well as securities) to impart enhanced settlement efficiency. (The delivery versus payment (DVP) modules can be broadly classified into three broad categories viz. DVP I, DVP II and DVP III. Under DVP I, the funds leg as well as the securities leg are settled simultaneously on a contract-by-contract basis. Under DVP 2, while the securities leg is settled on a contract-by-contract basis, the funds leg is settled for the net amount). Under DVP III, both the funds and the securities legs are settled for the net amounts.)

Patil Committee has recommended two important measures to be initiated by the Government, namely rationalisation of stamp-duty, and abolition of tax deduction at source, as in the case of government securities. As the corporate debt markets develop and RBI is assured of availability of efficient price discovery through significant increases in public issues as well as secondary market trading, and an efficient and safe settlement system, based on DvP III and STP is in place, RBI is committed to permitting market repos in corporate bonds. In the medium term, considering the overall macro-economic situation, the ceiling for foreign investment in both government securities and corporate debt will continue to be calibrated as an instrument of capital account management. In particular, a more liberalised access to foreign investment would be appropriate when, among other things, an efficient and safe settlement system is well entrenched, aggregate consolidated public debt to GDP ratio reaches a reasonable level, say less than 50 per cent, and the corporate debt market acquires depth and liquidity with significant role for insurance and pension funds in India. In the past, the government securities dominated the debt market in India, partly on account of the fiscal dominance and the absence of contractual savings. In the absence of contractual savings only banks tended to deploy their funds in the corporate bond market, mainly through private placement. RBI is hopeful that the recent slow but steady development of insurance sector, mutual funds etc. coupled with the existence of a reliable government securities market and the availability of robust reporting, trading and settlement mechanisms would lead to a rapid development of a vibrant corporate debt market. A framework for the development is already available through the recommendations of the Patil Committee, the implementation of which has already been taken up by the various agencies.

Check Your Progress 3

1) State the reasons for trading the derivatives.

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2) Which instruments are traded in the exchange traded markets?

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3) What is capital account convertibility?

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4) Name the regulators of exchange traded currency options markets.

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5) State the various selective reforms introduced in Government securities market in India.

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15.10 LET US SUM UP

Globalisation and financial liberalisation in India have ushered in a battery of changes in the financial architecture of the economy, as a result of which the resultant gain of the global integration of domestic and foreign financial markets has thrown open new opportunities but at the same time exposed the financial system to significant risks. While the capital market reforms are impressive, there are still areas that present major problems. The long term debt and corporate debt market presents the biggest problems. As a result of which, many large Indian companies look to foreign capital markets for longer term debt and equity. Despite of this, the prevailing economic conditions both at domestic and global level suggests that the Indian stock market will continued to grow even though USA and European markets have yet to recover from recession effect.

15.11 EXERCISES

1) Discuss the Role and scope of a well developed capital market in the growth process of an economy.

2) Trace the developmental reforms of capital market in India and assess the impact of these reforms in the growth of Equity and foreign exchange market?

3) Discuss the current scenario and shortcomings of the corporate debt market in India?

4) Discuss the functions of SEBI. Defines the significant steps of the SEBI to develop the Indian Equity Market?

15.12 SOME USEFUL BOOKS

Patil, R.H. (2000): “The Capital Market in 21st Century”, *Economic and Political Weekly*, November.

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15.13 ANSWERS OR HINTS TO CHECK YOUR PROGRESS EXERCISES

Check Your Progress 1

1) See Section 15.1

2) See Section 15.1

3) See Section 15.2

Check Your Progress 2

1) See Section 15.3

2) See Section 15.3

3) See Sub-section 15.3.1

4) See Sub-section 15.4.3

5) See Sub-section 15.4.6

Check Your Progress 3

1) See Section 15.6

2) See Sub-section 15.6.1

3) See Section 15.7

4) See Sub-section 15.8.1

5) See Sub-section 15.8.1