Recent reforms in Indian stock market and its impact (role of SEBI)

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Abstract

Financial markets have an important relationship with economic development. Regulation has been acknowledged to enable the orderly functioning of the securities market. The Securities and Exchange Board of India (SEBI) is the regulator charged with the orderly functioning of the securities market in India, protect the interests of investors and ensure development of the securities market. Since the establishment of SEBI in 1992, the Indian securities market has grown enormously in terms of volumes, new products and financial services. The literature examining the role of SEBI in this growth and development is limited and somewhat dated. This paper supplements the existing literature by updating the developments in the securities markets over the years. The paper focused on the Capital market reforms in India. The paper discussed about the regulatory framework of capital market in India. Any country growth rate depends on capital market. It shows the performance of the primary and secondary market. The paper also discusses the emerging issues of capital market in India. Capital Market plays a dominant role in Indian economy and securities Market.

Key words: Indian economy, securities Market, literature examining.

Overview of the Securities Market in India

The impressive growth in the number of participants and the volume of activity on the exchanges starting 1992-933 to-date is evident from Tables I Also notable is the emergence of activities that were new to the Indian securities market such as derivatives, venture capital funds and mutual fund management entities in the private sector, as may be noted from Table II.

The National Stock Exchange (NSE), established in 1994, has a higher turnover in the cash segment in terms of value as well as trades than the Bombay Stock Exchange (BSE) established in 1875. Trading activity on the sixteen regional exchanges has nearly disappeared in nearly all but three of them where trading has dwindled to negligible levels. Barring taxes on transactions, Indian securities markets provide one of the least cost trading platforms.

The large number of trades on the two exchanges points out to the importance of the securities trade to the Indian economy. As per NSE (2009) about 68.8% of the primary issuance of debt of Rs 6125 billion during 2008- 09 and 99.3 % of the secondary debt market turnover of Rs 62,713 billion was government paper indicating that both in terms of resource mobilization as well as in terms of trading activity the market for corporate debt remained insignificant. The corporate bond market in India, comprising mostly commercial paper and bonds of maturity ranging from one to twelve years is small by international standards in spite of various policy initiatives such as mandated a price / order matching of trades in and dematerialization. Purchases of securities by foreign institutional investors (FIIs) have steadily grown from about Rs. 56 billions in 1993-94 to over Rs. 6146 billions in 2008-09, the cumulative FII flows accounting for nearly 8% of the Bombay Stock Exchange market capitalization as of March 2009. FIIs have emerged as an important class of investors for more reason than one, as we will note later in this paper.

Market Participants

Issuers and Issuances: A whole range of organizations of Indian as well as foreign origin and ownership are allowed to issue securities in India. These include the central and the state governments, state owned and controlled bodies such as public sector undertakings, financial institutions and banks, private body corporates, mutual funds, collective investment schemes and special purpose vehicles established for securitization arrangements. A range of debt and equity instruments and hybrids are allowed to be issued in India. Securities that are permitted for trading and "dealing" in India are defined under law.5 Issuers are expected to ensure that the economic interests of investors are protected. Issuers may also be governed by pre-existing contractual obligations to those who could be affected by an issuance of securities. These obligations may be defined and enforced in a number of different ways. Issuances may be public or private. Public issues are offered to all domestic investors subject to certain quotas where applicable. Private placements, by definition, are limited to a set of investors identified by the investor. Participation by foreign investors in private as well as public issuances is subject to regulatory restrictions.

Investors: A range of investors, of Indian as well as foreign origin and domicile, participate in the Indian market. Domestic investors are free to subscribe to all offerings of securities to the extent made available to them by the issuer.

Intermediaries: A brief description of the role of the more common among these intermediaries is in Table III. The involvement and role of some of these intermediaries is mandated under law as in the case of a merchant banker.

Stock Exchange: Trade in securities in India is permitted only on recognized stock exchanges and is allowed only through members of the stock exchange. Trades are executed and settled through the stock exchange.

Clearing Corporation: It is a part of the stock exchange system responsible for the settlement of trades. The Clearing Corporation is usually the legal counter-party to net obligations of each brokerage firm and is responsible for eliminating counter-party risk.

Depository: Two depositories provide the service of maintaining the record for allotment and transfer of securities in an electronic format. The services of the two depositories are made available to investors through Depository Participants (DPs). It may be seen from the brief discussion above that the Indian securities market is a complex network of a host of economic agents. When they come together to execute a transaction they are tied together through a web of regulations, in addition to their commercial interconnectedness. Even the conduct of those that are not directly governed by securities regulations is indirectly influenced through their contractual obligations to other regulated intermediaries and / or the regulation on the outcome of the service they provide.

Review of literature

Shirai (2004) the study focused on financial capital reforms in India through the positive impact on both banking sectors and capital market .It showed that the relationship between bank loans and bank finance. The study focused on three major issues. Firstly firms characteristics and secondly, weak the overall substitution relationship between loans financial institutions and finally equity finance. **Bose .S. (2005)** the study highlighted the stock regulatory infrastructure of the Indian Securities market. The study also discussed the roles of the stock exchanges electronic data base in aiding the regulator in prevention ,discovery and convocation of securities of funds The study also suggested that there are rationalized to completely empower SEBI to carry out its functions as the regulators. **Venkata (2006)** the study examined the long run equilibrium between relationship Indian stock market and seven developed countries namely Switzerland ,France ,Germany, Japan ,U.K ,U.S.A and South Korea. It used multivariate co integration technique was used to developed market and developing markets .The study analyzed the short run influence of one market on the other factors which influence the Indian Capital Market .It concluded that the baring Japan ,the Asian stock market under study more attractive for international investors .**Dhanda, N and Sheokand ,A.(2008)** the study examined the recent trends in primary market .It also observed that the economic development process was required capital for the industrial growth of the country. The study observed that the SEBI had taken several initiatives to improve the operational efficiency and transparency in primary market .The study showed that the per centge share amount raised through right issued was ranging 4.33 percentage to37.7.The study analyzed the public issues and right issues contained to dominated the amount of capital raised during the study period. **Ahuja (2012)** the study focused on capital market structure.

Role of SEBI in India

The SEBI operates within the legal framework of the SEBI Act, 1992. The statutory objectives of the SEBI enshrined in the SEBI Act are fourfold-

- Protection of investors interests in securities
- Promotion of the development of the securities market
- Regulation of the securities market and
- Matters connected therewith and incidental thereto.

In keeping with these statutory objectives, the SEBI has set for itself strategic aims for each of the four key spheres which encompass SEBI's activities in relation to the investors, issuers, intermediaries and the regulatory regime. To the investors, the SEBI strives to assure that their rights are protected, they are enabled to make informed choices and decisions and a market which is fair in the financial dealings. To the issuers, the SEBI strives to provide a transparent and efficient market where they are enabled to raise resources at low cost, but conduct themselves in accordance with the highest standards of corporate governance and that they are conscious of and meet their regulatory obligations. To the intermediaries, the SEBI strives to render a market in which they can compete freely and operate in a manner which gives the investors and market participants the confidence that the market is efficient, orderly and fair. In the regulatory regime, the SEBI seeks to ensure that it always remains appropriate, proportionate and effective in which all "stakeholders" have the confidence. With these strategic aims in view the SEBI has been constantly reviewing and re apprising it existing policies and programmes formulating new policies and regulations to nurture areas hitherto unregulated / inadequately regulated and to implement them in a manner to promote the growth of the market with transparency, fairness, efficiency and integrity.

Major Reforms in the Primary Market

- Merit-based regime to disclosure-based regime. Disclosure and Investor Protection Guidelines issued.
- Pricing of public issues determined by the market.
- System of proportional allotment of shares introduced.
- Banks and public sector undertakings allowed to raise funds from the primary market.
- Accounting standards close to international standards.
- Corporate Governance Guidelines issued.
- Discretionary allotment system to QIBs has been withdrawn.
- Foreign Institutional Investors (FIIs) allowed to invest in primary issues within the sectoral limits (including GSec).
- Mutual funds are encouraged in both the public and private sectors and have been given permission to invest overseas.
- Guidelines were issued for private placement of debt.
- Securities and Exchange Board of India promotes Self-Regulatory Organizations.
- Allocation to retail investors increased from 25 percent to 35 percent.
- Separate allocation of 5 percent to domestic mutual funds within the QIB category.
- Freedom to fix face value of shares below Rs. 10 per share only in cases where the issue price is Rs. 50 or more.
- Shares allotted on a preferential basis as well as the pre-allotment holding are subjected to lock-in period of six months to prevent sale of shares.

  Source: Securities and Exchange Board of India (SEBI).

Major Reforms in the Secondary Market

- Registration of market intermediaries made mandatory.
- Capital adequacy norms specified for brokers and sub-brokers of stock exchanges.
- Guidelines issued on Listing Agreement between stock exchanges and corporates.
- Settlement cycle shortened to T+2.

- Stock exchanges and other intermediaries, including mutual funds, inspected.
- Regulation of Substantial Acquisition of Shares and Takeovers, 1997.
- Foreign institutional investors (FIIs) allowed to invest in Indian Capital Market, 1992.
- Order-driven, fully automatic, anonymous screen-based trading introduced.
- Depositories Act, 1996, enacted.
- Guidelines issued on corporate governance.
- Fraudulent and unfair trade practices, including insider trading, prohibited by Securities and Exchange Board of India.
- Straight-through processing introduced and made mandatory for institutional trades.
- Margin trading and securities lending and borrowing schemes introduced.
- Separate trading platform, Indonext, for small and medium-sized enterprises (SME) sector launched.
- Notification of corporatization and demutualization of stock exchanges.
- Settlement and trade guarantee fund and investor protection fund set up.
- Comprehensive risk management system (capital adequacy, trading and exposure limit, margin requirement, index-based market-wide circuit breaker, online position monitoring, automatic disablement of terminals) put in place.
- Comprehensive surveillance system put in place.
- Securities Appellate Tribunal set up July 28, 1997.
- Mutual funds and FIIs to began entering the unique client code (UCC) pertaining to the parent entity at the order-entry level and entered UCCs for individual schemes and subaccounts for the post-closing session.

Impact of reforms

- Reduction In Transaction cost
- Market determined pricing
- Electronic settlement
- Elimination of counter parity risk,
  Probabilities of hedging etc.
- Country wide market integration
- Global integration of markets
  (ADR/GDR FPI)
- Enhanced liquidity

Conclusion

Our review of SEBI's performance in the eighteen years since its establishment in its current incarnation as an adequately empowered and independent regulator indicates that there has been an all-round improvement in the institutional framework in which the securities trade in India is conducted. Progressively, over time, nearly every actor who is directly connected with the securities trade has been brought under the regulatory ambit of SEBI. A combination of registration, licensing, eligibility conditions, and incentives allows SEBI to rein in non-compliant behaviour that could potentially affect the functioning of the securities market adversely. Similarly, many of the important processes have been regulated such as takeover activities, insider trading, manipulative practices, issuance of employee share options and so on. It is thus reasonable to claim that the regulatory framework is fairly comprehensive in its coverage of the securities trade. Some of these regulatory steps may have played an important part in the orderly growth in activity of certain key categories of players such as FIIs and mutual funds.

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