A STUDY ON GROWTH OF CAPITAL MARKETS IN INDIA

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ABSTRACT

Capital market deals with medium term and long term funds. It refers to all facilities and the institutional arrangements for borrowing and lending term funds (medium term and long term). The demand for long term funds comes from private business corporations, public corporations and the government. The supply of funds comes largely from individual and institutional investors, banks and special industrial financial institutions and Government.

Introduction

Capital market is the broad term which includes Primary market, secondary market, lending institutions, bank, investors and just about anybody and everybody who is engaged in providing long term capital (equity or debt) to the industrial sector. In this market medium term and long term capital is supplied and demanded. In Indian economy the dynamic growth of the capital market has been particularly marked during the period following the liberalization of economic policy in the industrial, financial and foreign trade sector in 1991. Though there have been shocking setbacks in certain years, the volume has no leaps and bounds.

Capital markets are markets for buying and selling equity and debt instruments. Capital markets channel savings and investment between suppliers of capital such as retail investors and institutional investors, and users of capital like businesses, government and individuals. Capital markets are vital to the functioning of an economy, since capital is a critical component for generating economic output. Capital markets include primary markets, where new stock and bond issues are sold to investors, and secondary markets, which trade existing securities.

BREAKING DOWN 'Capital Markets'

Capital markets are a broad category of markets facilitating the buying and selling of financial instruments. In particular, there are two categories of financial instruments that capital in which markets are involved. These are equity securities, which are often known as stocks, and debt securities, which are often known as bonds. Capital markets involve the issuing of stocks and bonds for medium-term and long-term durations, generally terms of one year or more.

Capital markets are overseen by the Securities and Exchange Commission in the United States or other financial regulators elsewhere. Though capital markets are generally concentrated in financial centers around the world, most of the trades occurring within capital markets take place through computerized electronic trading systems. Some of these are accessible by the public and others are more tightly regulated.

Other than the distinction between equity and debt, capital markets are also generally divided into two categories of markets, the first of which being primary markets. In primary markets, stocks and bonds are issued directly from companies to investors, businesses and other institutions, often through underwriting. Primary markets allow companies to raise capital without or before holding an initial public offering so as to make as much direct profit as

possible. After this point in a company's development, it may choose to hold an initial public offering so as to generate more liquid capital. In such an event, the company will generally sell its shares to a few investment banks or other firms.

At this point the shares move into the secondary market, which is where investment banks, other firms, private investors and a variety of other parties resell their equity and debt securities to investors. This takes place on the stock market or the bond market, which take place on exchanges around the world, like the New York Stock Exchange or NASDAQ; though it is often done through computerized trading systems as well. When securities are resold on the secondary market, the original sellers do not make money from the sale. Yet, these original sellers will likely continue to hold some amount of stake in the company, often in the form of equity, so the company's performance on the secondary market will continue to be important to them.

Capital markets have numerous participants including individual investors, institutional investors such as pension funds and mutual funds, municipalities and governments, companies and organizations, banks and financial institutions. While many different kinds of groups, including governments, may issue debt through bonds (these are called government bonds), governments may not issue equity through stocks. Suppliers of capital generally want the maximum possible return at the lowest possible risk, while users of capital want to raise capital at the lowest possible cost.

The size of a nation's capital markets is directly proportional to the size of its economy. The United States, the world's largest economy, has the largest and deepest capital markets. Because capital markets move money from people who have it to organizations who need it in order to be productive, they are critical to a smoothly functioning modern economy. They are also particularly important in that equity and debt securities are often seen as representative of the relative health of markets around the world.

On the other hand, because capital markets are increasingly interconnected in a globalized economy, ripples in one corner of the world can cause major waves elsewhere. The drawback of this interconnection is best illustrated by the global credit crisis of 2007-09, which was triggered by the collapse in U.S. mortgage-backed securities (MBS). The effects of this meltdown were globally transmitted by capital markets since banks and institutions in Europe and Asia held trillions of dollars of these securities.

STRUCTURE CAPITAL MARKET:-

Capital market is classified in two ways

1) CAPITAL MARKET IN INDIA

Gild – Edged Market Industrial Securities Market Development Financial Institutions (DFIs) Financial intermediaries

a) Gilt – Edged Market:-

Gilt – Edged market refers to the market for government and semi-government securities, which carry fixed rates of interest. RBI plays an important role in this market.

b) Industrial Securities Market:- It deals with equities and debentures in which shares and debentures of existing companies are traded and shares and debentures of new companies are bought and sold.

c) Development Financial Institutions:- Development financial institutions were set up to meet the medium and long-term requirements of industry, trade and agriculture. These are IFCI, ICICI, IDBI, SIDBI, IRBI, UTI, LIC, GIC etc. All These institutions have been called Public Sector Financial Institutions.

d) Financial Intermediaries: - Financial Intermediaries include merchant banks, Mutual Fund; Leasing companies etc. they help in mobilizing savings and supplying funds to capital market.

2) The Second way in which capital market is classified is as follows :-

CAPITAL MARKET IN INDIA

Primary market Secondary market

a) Primary Market: - Primary market is the new issue market of shares, preference shares and debentures of non-government public limited companies and issue of public sector bonds.

b) Secondary Market this refers to old or already issued securities. It is composed of industrial security market or stock exchange market and gilt-edged market.

GROWTH OF CAPITAL MARKET IN INDIA

After Independence capital market has shown a remarkable progress. The first organised stock exchange was established in India at Bombay in 1887. When the Securities Contracts (Regulation) Act 1956 was passed, only 7 Stock exchanges Viz. Mumbai, Ahmedabad, Kolkata, Chennai, Delhi, Hyderabad and Indore, received recognition. By end of March 2004, the number of stock exchanges increased to 23.

1) Primary I New Issues Market :- After liberalisation policy of 1991 and the abolition of capital issues control with effect from May 29,1992, the primary market got a tremendous , boost. This can be seen from following points :-

a) New Capital Issues by Private Sector :- The number of new capital issues by private sector was only 364 in 1990-91 and the amount raised by them was `.4,312 crore. The number of new capital issues rose to 1,678 in 1994-95 and the amount raised by them was `. 26,418 crore. Since 1995 the capital market was sluggish and the resources raised fell to `.. 10,409 crores in 1996-97. In 2003-04, the amount raised from new capital issues was only `.3,210 crores. In 2004 it increased again to `.33,475 crore and in 2005 `.30,325 crore of resources were raised on this market. The primary issues of debt securities felt a low of around `. 66 crore in 2005.

b)Public Sector Bonds :- The resources raised by issuing bonds by Public Sector undertakings rose from `.354 crores in 1985-86 to 7,491 crore in 2004-05.

c) Mutual Funds :- In 1997-98, the total number of mutual funds in the country was 34.

In 1997-98, the mutual funds were able to mobilise `.4,064 crore. In 1999-2000 mutual funds mobilised a record of `.22,117 crore. There was a massive resource mobilisation of `..41,570 crore by private sector mutual funds in 2003-04, pushing up the total resource mobilisation by all mutual funds to as high as `.47,873 crore. In 2004-05, resource mobilisation once again declined to `.3, 015 crore.

2) Secondary Market :-

a) Industrial Securities Market:- In 1991-92, there was a huge rise in the share prices. The RBI All India Index Number of Ordinary Share Prices rose to 1,485.4 in 1991-92 (base year 1980-81), showing a gain of 181.4%. In 1992-93 due to irregularities the Stock Market declined. The years 1993 and 1994 saw increased activity in stock market due to: – Better performance of companies, Improvement in Balance of Payment position, Increasing investment by Foreign Institutional investors etc.

India enjoys 2nd largest investor population in the world next to U.S.A.

b) Bombay Stock Exchange (BSE):- The scrip movements In Bombay Stock Exchange reflected the same trend as the RBI index (BSE sensitive index with base 1978-79 = 100).

Market capitalisation of Bombay Stock Exchange was `.12, 01,207 crore in 2003-04. It rose to `.30, 66,076 crore in 2008-09.

c) National Stock Exchange (NSE) :- The NSE of India was set up in 1992 and started its operations in 1994. It provides facility for trading of equity investments, warrants, debentures, preference shares etc. The market capitalisation of NSE reached to `.28, 96,194 crore in 2008-09.

d) Over The Counter Of Exchange Of India :- It was set in August 1989 and started .operating since 1992.

e) Financial Intermediaries :- Financial Intermediaries are the latest trend in Indian Capital Market. They have to play an important role in field of venture capital, credit rating etc.

FACTORS CONTRIBUTING TO THE GROWTH AND DEVELOPMENT OF CAPITAL MARKET

1) Growth Of Development Banks And Financial Institutions :-

For providing long term funds to industry, the government set up Industrial Finance Corporation in India (IFCI) in 1948. This was followed by a number of other development banks and institutions like the Industrial Credit and Investment Corporation of India (ICICI) in 1955, Industrial Development Bank of India (IDBI) in 1964, Industrial Reconstruction Corporation of India (IRCI) in 1971, Foreign Investment Promotion Board in 1991, Over the Counter Exchange of India (OTCEI) in 1992 etc. In 1969, 14 major commercial banks were nationalised. Another 6 banks were nationalised in 1980. These financial institutions and banks have contributed in widening and strengthening of capital market in India.

2) Setting Up Of SEBI :-

The Securities Exchange Board of India (SEBI) was set up in 1988 and was given statutory recognition in 1992.

3) Credit Rating Agencies :-

Credit rating agencies provide guidance to investors / creditors for determining the credit risk. The Credit Rating Information Services of India Limited (CRISIL) was set up in 1988 and Investment Information and Credit Rating Agency of India Ltd. (ICRA) was set up in 1991. These agencies are likely to help the development of capital market in future.

4) Growth Of Mutual Funds :-

The mutual funds collect funds from public and other investors and channelise them into corporate investment in the primary and secondary markets. The first mutual fund to be set up in India was Unit Trust of India in 1964. In 2007-08 resources mobilised by mutual funds were Rs. 1,53,802 crores.

5) Increasing Awareness :-

During the last few years there has been increasing awareness of investment opportunities among the public. Business newspapers and financial journals (The Economic Times, The Financial Express, Business India, Money etc.) have made the people aware of new long-term investment opportunities in the security market.

6) Growing Public Confidence

A large number of big corporations have shown impressive growth. This has helped in building up the confidence of the public. The small investors who were not interested to buy securities from the market are now showing preference in favour of shares and debentures. As a result, public issues of most of the good companies are now over-subscribed many times.

7) Legislative Measures :- The government passed the companies Act in 1956. The Act gave powers to government to control and direct the development of the corporate enterprises

in the country. The capital Issues (control) Act was passed in 1947 to regulate investment in different enterprises, prevent diversion of funds to non-essential activities and to protect the interest of investors. The Act was replaced in 1992.

8) Growth Of Underwriting Business :-

The growing underwriting business has contributed significantly to the development of capital market.

9) Development Of Venture Capital Funds :-

Venture capital represents financial investment in highly risky projects with a hope of earning high returns After 1991, economic liberalisation has made possible to provide medium and long term funds to those firms, which find it difficult to raise funds from primary markets and by way of loans from FIs and banks.

10) Growth Of Multinationals (MNCs) :-

The MNCs require medium and long term funds for setting up new projects or for expansion and modernisation. For this purpose, MNCs raise funds through loans from banks and FIs. Due to the presence of MNCs, the capital market get a boost.

11) Growth Of Entrepreneurs :-

Since 1980s, there has been a remarkable growth in the number of entrepreneurs. This created more demand for short term and long term funds. FIs, banks and stock markets enable the entrepreneurs to raise the required funds. This has led to the growth of capital market in India.

12) Growth Of Merchant Banking :-

The credit for initiating merchant banking services in India goes to Grindlays Bank in 1967,followed by Citibank in 1970. Apart from capital issue management, merchant banking divisions provide a number of other services including provision of consultancy services relating to promotion of projects, corporate restructuring etc.

REFORMS / DEVELOPMENTS IN CAPITAL MARKET SINCE 1991:-

The government has taken several measures to develop capital market in post-reform period, with which the capital market reached new heights. Some of the important measures are

1) Securities and Exchange Board Of India (SEBI):- SEBI became operational since 1992. It was set with necessary powers to regulate the activities connected with marketing of securities and investments in the stock exchanges, merchant banking, portfolio management, stock brokers and others in India. The objective of SEBI is to protect the interest of investors in primary and secondary stock markets in the country.

2) National Stock Exchange (NSE):- The setting up to NSE is a landmark in Indian capital markets. At present, NSE is the largest stock market in the country. Trading on NSE can be done throughout the country through the network of satellite terminals. NSE has introduced inter-regional clearing facilities.

3) Dematerialisation Of Shares:- Demat of shares has been introduced in all the shares traded on the secondary stock markets as well as those issued to the public in the primary markets. Even bonds and debentures are allowed in demat form. The advantage of demat trade is that it involves Paperless trading.

4) Screen Based Trading: - The Indian stock exchanges were modernised in 90s, with Computerised Screen Based Trading System (SBTS), It cuts down time, cost, risk of error and fraud and there by leads to improved operational efficiency. The trading system also provides complete online market information through various inquiry facilities.

5) Investor Protection :- The Central Government notified the establishment of Investor Education and Protection Fund (IEPF) with effect from 1st Oct. 2001: The IEPF shall be credited with amounts in unpaid dividend accounts of companies, application moneys

received by companies for allotment of any securities and due for refund, matured deposits and debentures with companies and interest accrued there on, if they have remained unclaimed and unpaid for a period of seven years from the due date of payment. The IEPF will be utilised for promotion of awareness amongst investors and protection of their interests.

6) Rolling Settlement:- Rolling settlement is an important measure to enhance the efficiency and integrity of the securities market. Under rolling settlement all trades executed on a trading day (T) are settled after certain days (N). This is called T + N rolling settlement. Since April 1, 2002 trades are settled' under T + 3 rolling settlement. In April 2003, the trading cycle has been reduced to T + 2 days. The shortening of trading cycle has reduced undue speculation on stock markets.

7) The Clearing Corporation Of India Limited (CCIL):- The CCIL was registered in 2001, under the Companies Act, 1956 with the State Bank of India as the Chief Promoter. The CCIL clears all transactions in government securities and repos and also Rupee / US $ forex spot and forward deals All trades in government securities below Rs. 20 crores would be mandatorily settled through CCIL, white those above Rs. 20 crores would have the option for settlement through the RBI or CCIL.

8) The National Securities Clearing Corporation Limited (NSCL) :- The NSCL was set up in 1996. It has started guaranteeing all trades in NSE since July 1996. The NSCL is responsible for post-trade activities of NSE. It has put in place a comprehensive risk management system, which is constantly monitored and upgraded to pre-expect market failures.

9) Trading In Central Government Securities :- In order to encourage wider participation of all classes of investors, Including retail investors, across the country, trading in government securities has been introduced from January 2003. Trading in government securities can be carried out through a nation wide, anonymous, order-driver, screen-based trading system of stock exchanges in the same way in which trading takes place in equities.

10) Credit Rating Agencies:- Various credit rating agencies such as Credit Rating Information services of India Ltd. (CRISIL – 1988), Investment Information and credit Rating Agency of India Ltd. (ICRA – 1991), etc. were set up to meet the emerging needs of capital market. They also help merchant bankers, brokers, regulatory authorities, etc. in discharging their functions related to debt issues.

11) Accessing Global Funds Market:- Indian companies are allowed to access global finance market and benefit from the lower cost of funds. They have been permitted to raise resources through issue of American Depository Receipts (ADRs), Global Depository Receipts (GDRs), Foreign Currency Convertible Bonds (FCCBs) and External Commercial Borrowings (ECBs). Further Indian financial system is opened up for investments of foreign funds through Non-Resident Indians (NRIs), Foreign Institutional investors (FIIs), and Overseas Corporate Bodies (OCBs).

12) Mutual Funds :- Mutual Funds are an important avenue through which households participate in the securities market. As an investment intermediary, mutual funds offer a variety of services / advantages to small investors. SEBI has the authority to lay down guidelines and supervise and regulate the working of mutual funds.

13) Internet Trading :- Trading on stock exchanges is allowed through internet, investors can place orders with registered stock brokers through internet. This enables the stock brokers to execute the orders at a greater pace.

14) Buy Back Of Shares :- Since 1999, companies are allowed to buy back of shares. Through buy back, promoters reduce the floating equity stock in market. Buy back of shares help companies to overcome the problem of hostile takeover by rival firms and others.

15) Derivatives Trading :- Derivatives trading in equities started in June 2000. At present, there are four equity derivative products in India Stock Futures, Stock Options, Index Futures, Index Options. Derivative trading is permitted on two stock exchanges in India i.e. NSE and BSE. At present in India, derivatives market turnover is more than cash market.
16) PAN Made Mandatory :- In order to strengthen the "Know your client" norms and to have sound audit trail of transactions in securities market, PAN has been made mandatory with effect from January 1, 2007.

Conclusion:
The capital market is a place where the suppliers and users of capital meet to share one another's views, and where a balance is sought to be achieved among diverse market participants. The securities decouple individual acts of saving and investment over time, space and entities and thus allow savings to occur without concomitant investment. Moreover, yield- bearing securities makes present consumption more expensive relative to future consumption, inducing people to save. The composition of savings changes with less of it being held in the form of idle money or unproductive assets, primarily because more divisible and liquid assets are available.

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