



Investigating The Mechanisms Of The Indian Stock Market

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ABSTRACT

The stock market, a vital and dynamic element of the financial system, plays a crucial role in the progress of the economy. It provides a marketplace for individuals and organizations to engage in transactions involving shares, bonds, debentures, and various other financial instruments. Essentially, it functions as a trading venue for a range of assets and derivatives. Additionally, stock markets serve as indicators of the performance and growth of the Indian economy. The establishment of the Securities and Exchange Board of India (SEBI), influenced by global trends, marked the initial step towards reforming the Indian stock market. However, it was the 1991 stock market scandal that truly propelled these reforms forward. With the advent of SEBI and advancements in technology, the Indian stock market has achieved unprecedented heights, established new standards, and significantly contributed to our economy by enhancing the value of equities, debentures, bonds, and real estate.

Keywords: SEBI, Capital Market, Stock Market, Fiscal Policy and Financial Growth

Introduction:

In July 1991, a transformative phase began for the Indian capital market, marked by significant financial and economic liberalization. This period commenced with a 20% devaluation of the rupee, alongside a comprehensive overhaul of industrial policy that eliminated licensing requirements for all but 18 specified industry sectors. Subsequent reforms included the removal of restrictions imposed by the Monopolies and Restrictive Trade Practices Act (MRTP), a relaxation of the Foreign Exchange Regulation Act (FERA), and an increase in openness to foreign trade. Following these economic liberalization efforts, privatization, and globalization, India's capital market emerged as a pivotal force in financing and investment. The stock

market plays a crucial role in fostering economic growth by facilitating corporate finance, promoting entrepreneurship, and optimizing resource mobilization and allocation. The period after 1991 witnessed significant growth and development in India, largely due to innovative strategies and regulatory frameworks within the capital market, contrasting sharply with the previous era of low growth rates, high public savings, and a focus on self-reliance. The establishment of the Securities and Exchange Board of India (SEBI) was a key development aimed at regulating and advancing the market. The Bombay Stock Exchange, founded in 1875, played a vital role in revitalizing the financial sector. Since then, the stock market has become integral to Indian business financing, enabling trading in shares, debentures, and bonds, and attracting investors through its ability to provide liquidity and facilitate capital raising.

Emergence of a New Era:

The Seventh Five-Year Plan commenced in 1985, signaling the onset of liberalized economic policies. The Banking Companies Amendment Act of 1983 expanded the capabilities of banks, enabling them to offer a range of financial services, including leasing, hire-purchase, merchant banking, and non-funded activities. Public sector banks began establishing subsidiaries to provide mutual funds, lease finance, commercial banking, and various other services. Following 1992, private sector entities were allowed to engage in these financial services. In April 1992, the Securities and Exchange Board of India (SEBI), which had been in existence since April 1988, was granted legislative powers, transforming it into a fully autonomous body responsible for regulating and overseeing the Indian stock markets. Additionally, new institutions were established, such as the Stock Holding Corporation of India Limited (SHCIL) for clearing and share depository services, and Credit Rating Information Services of India Limited (CRISIL) for credit rating purposes.

Overview of the Indian Stock Market:

The Bombay Stock Exchange (B.S.E.), recognized as the oldest stock exchange in India, was established in 1855 when a collective of stockbrokers gathered beneath banyan trees in front of Mumbai's Town Hall. Over the years, the location of these meetings changed, leading to the formation of "The Native Share & Stock Brokers Association" in 1875. The B.S.E. received official recognition through the Securities Contracts Regulation Act in 1958, and in 1986, the Indian government introduced the BSE SENSEX index to monitor the overall market performance.

During the 20th century, additional exchanges such as the Ahmadabad Stock Exchange emerged. The National Stock Exchange (NSE) has played a pivotal role in the swift growth and evolution of India's stock market, notably reducing transaction costs while improving efficiency, transparency, and security. As a result, the Indian stock market now resembles many developed markets. Automated exchanges utilize advanced computer systems to facilitate trading. The Bombay Stock Exchange (B.S.E.) stands out as the world's largest exchange in terms of listed members, boasting over 5,000 listed companies.

United States Stock Exchange:

Established in 1993 following the recommendations of the Pherwani committee, the National Stock Exchange (NSE) introduced a national market system that enabled electronic trading and settlement across the country, featuring standardized pricing and fixed service fees or broker commissions. The Securities Contracts (Regulation) Act recognized the NSE as the 23rd stock exchange in India. As SEBI evolves, its focus will shift towards fostering development rather than solely regulating, while it continues to enforce stricter rules on exchanges. SEBI's regulatory scope encompasses businesses, brokers, intermediaries, and investors. The enhancement of service quality and efficiency will heavily rely on professional intermediaries and brokers equipped with the necessary education, training, and research capabilities.

National Market Framework:

The Pherwani Committee recommended the establishment of a national market framework inspired by the Mumbai Stock Exchange. To facilitate this system, the committee put forth the idea of several organizations that would offer high-quality trading, settlement, and depository services. Their three-tiered approach included the creation of regional stock exchanges in state capitals, additional trading floors managed by major or regional stock exchanges, and stock exchanges located in key cities such as Mumbai and Kolkata.

SEBI, the Securities Exchange Board of India:

The stock market serves as a crucial platform for individuals to invest in securities, forming a fundamental component of a nation's economic framework. The Capital Issue (Control) Act of 1947 was enacted to enhance economic growth and protect the interests of investors. However, achieving effective regulation of the stock market remains a challenge. Established in 1992, the Securities and Exchange Board of India (SEBI) was created to address these issues, tasked with overseeing stock market development and safeguarding investor interests. SEBI is an essential regulatory authority that significantly influences India's financial markets. Below are further insights and analyses regarding SEBI's roles, importance, and its effects on the Indian economy.

- ❖ **Regulatory Functions:** SEBI undertakes a range of regulatory functions within the securities market, which encompasses stock exchanges, intermediaries, and market participants. It establishes norms and regulations while overseeing the issuance of securities, ensuring that capital raising processes are efficient, fair, and transparent.
- ❖ **Market Oversight:** SEBI is responsible for overseeing India's stock exchanges and other securities markets. It monitors trading activities, investigates potential market manipulation, and enforces regulations to maintain the integrity of the market.
- ❖ **Protection of Investors:** A primary objective of SEBI is to protect the interests of investors. It ensures that investors receive timely and accurate information, safeguards them against fraudulent activities, and upholds their legal rights within the securities market.
- ❖ **Capital Market Advancement:** SEBI plays a vital role in fostering innovation and the introduction of new financial products to enhance the development of the capital market. Its efforts are crucial in attracting

foreign investment and creating a conducive environment for both domestic and international businesses.

- ❖ **Evolution of Regulation:** The establishment of SEBI in 1992 marked a significant transformation in India's regulatory landscape. Prior to SEBI, stock market regulation lacked consistency and coherence. The Capital Issue (Control) Act of 1947 imposed restrictions that hindered effective oversight. SEBI has since provided a comprehensive and modern regulatory framework, streamlining and enhancing the efficiency of the regulatory system.
- ❖ **International Recognition:** SEBI's regulatory framework and practices have garnered global acclaim. Efforts to align with international standards and best practices have made India's securities market increasingly attractive to foreign investors, resulting in a rise in international portfolio investments in Indian debt and equity assets.
- ❖ **Technology and Efficiency:** SEBI has taken a pioneering role in leveraging technology to enhance the efficiency of the securities market. Initiatives such as electronic trading, dematerialization of securities, and the establishment of depositories have led to greater market transparency and reduced settlement times.
- ❖ **Market Manipulation Prevention:** SEBI is proactive in combating insider trading and market manipulation. It has established regulations and monitoring systems designed to detect irregular trading activities and maintain the integrity of the market.
- ❖ **Regulation Enforcement:** SEBI imposes disciplinary measures on market participants who violate regulations. This can include fines, suspension of trading privileges, and barring individuals or entities from engaging in the securities market.
- ❖ **Adaptive Regulations:** SEBI consistently revises and updates its regulations to respond to new challenges and evolving market dynamics. This adaptability is vital for maintaining a stable and well-regulated financial ecosystem.

In summary, SEBI's establishment and ongoing initiatives have enhanced the transparency of the Indian securities market and made it more inviting for investors. Its role in investor protection, market development, and regulatory oversight is crucial for ensuring the stability and growth of the Indian economy. SEBI has played a significant role in positioning India as an attractive investment destination and in bolstering confidence in the Indian securities market.

Individuals involved in the Depository:

A Depository Participant (DP) acts as an intermediary between private investors and depositories responsible for the custody and management of electronic securities in dematerialized format, thereby playing a crucial role in the Indian financial system. The following information and analyses outline the functions and significance of DPs within the Indian securities market.

- ❖ A Depository Participant (D.P.) plays a crucial role in facilitating the process for investors to establish demat accounts, which are essential for engaging in electronic trading and investment in securities. They aid investors in transitioning their physical securities, represented by paper certificates, into a digital

format. Additionally, account holders can access vital services such as account statements, transaction records, and more through D.P.s. They also assist with trade settlements, the transfer of securities, and related operations.

- ❖ **Regulation and SEBI Certification:** D.P.s are required to obtain certification from the Securities and Exchange Board of India (SEBI) to offer depository services. This regulatory framework ensures that D.P.s adhere to established guidelines, maintain the integrity of the system, and safeguard the interests of investors.
- ❖ **Various Types of D.P.s:** Examples of D.P.s include stockbrokers, Registrars and Transfer (R&T) agents, and non-banking financial companies (NBFCs). Each type of D.P. may specialize in different areas, catering to specific segments of the market. For instance, stockbrokers often provide a range of services beyond their role as D.P.s, including trading and market research.
- ❖ **Minimum Net worth Requirement:** According to the SEBI (Depositories and Participants) Regulations of 1996, entities such as stockbrokers, R&T agents, and NBFCs must maintain a minimum net worth of Rs. 50 lakh. This requirement ensures that D.P.s possess the necessary financial capacity to perform their responsibilities and meet any financial obligations that may arise in the course of their operations.
- ❖ **Market Growth:** The presence of numerous D.P.s under the Central Depository Services Limited (CDSL) and National Securities Depository Limited (NSDL) reflects the growth and accessibility of the dematerialized securities market in India. This environment fosters competition and enhances service quality, allowing investors to choose from a variety of service providers.
- ❖ **Diverse Service Offerings:** Investors benefit from enhanced portfolio management due to the extensive range of depository services provided by D.P.s. These services encompass securities transmission, pledge and hypothecation, dematerialization, and additional related functions.
- ❖ **Risk Reduction:** D.P.s play a crucial role in minimizing risks and curbing fraudulent activities within the securities market. By holding shares electronically, the risks associated with the loss or theft of physical share certificates are eliminated, significantly lowering the chances of fraud.
- ❖ **Enhancing Market Efficiency:** The use of dematerialized securities and D.P.s contributes to improved market dynamics. This approach simplifies trading and settlement processes, reduces paperwork, and accelerates transaction processing, ultimately leading to cost savings and enhanced liquidity.

In the financial landscape of India, Depository Participants play a vital intermediary role, enabling investors to engage with the securities market. By converting physical securities into electronic formats and providing a range of services, they enhance the efficiency of Indian capital markets, safeguard investors, and promote growth. To maintain investor trust in the securities market, it is imperative that D.P.s adhere to stringent standards and best practices, which is why regulatory oversight is in place to ensure compliance.

Commission for the Forward Market:

Prior to its integration with the Securities Exchange Board of India (SEBI) in September 2015, the Forward Markets Commission (F.M.C.) was the main regulatory authority overseeing commodities futures markets in India. It managed trading activities across 22 Indian markets and six national exchanges. Established in 1953 under the Forward Contracts (Regulation) Act of 1952, the F.M.C. operated under the auspices of the Ministry of Consumer Affairs, Food, and Public Distribution. The merger aimed to streamline the regulatory framework governing financial markets in India. The F.M.C. was instrumental in ensuring transparency and upholding the integrity of commodity futures trading within the nation.

Additional Information and Examination:

- ❖ **Regulatory Functions:** The F.M.C. undertook several essential regulatory functions, including the approval and oversight of commodity exchanges, ensuring compliance with the Forward Contracts (Regulation) Act of 1952, and monitoring trading activities on these platforms. It also formulated rules and standards for the trading and settlement of commodity futures contracts.
- ❖ **Risk Management:** The F.M.C. was responsible for establishing risk management protocols within commodity markets. It ensured that exchanges implemented robust risk control systems to mitigate the risks of defaults and market manipulation.
- ❖ **Investor Protection:** The F.M.C. aimed to safeguard the interests of market participants, particularly retail investors and hedgers, by fostering a fair and transparent trading environment. It also enforced regulations against fraudulent and manipulative trading practices.
- ❖ **Market Development:** The F.M.C. played a significant role in the growth and advancement of India's commodity futures markets. It facilitated the introduction of new trading commodities and encouraged innovation in product offerings.
- ❖ **Market Surveillance:** The F.M.C. conducted regular surveillance of the commodity futures markets to detect and prevent market abuses and irregularities. This included monitoring fluctuations in prices, trading volumes, and the activities of market participants.
- ❖ **International Collaboration:** The F.M.C. collaborated with international regulatory bodies to align with global best practices in commodity market regulation. This effort helped to ensure that India's regulatory framework met international standards.
- ❖ **Educational Programs:** The F.M.C. initiated programs aimed at educating market participants and the general public about the benefits and risks associated with trading in commodity futures. Its goal was to enhance awareness and ensure that traders made informed decisions.

A significant effort to enhance regulatory supervision of India's financial markets involved the 2015 consolidation of the Forward Markets Commission (F.M.C.) and the Securities and Exchange Board of India (SEBI). This merger aimed to create a more cohesive and consistent regulatory framework for both securities and commodities markets, establishing a single authority to manage all aspects of the financial markets. As a result of SEBI's oversight, the efficiency and effectiveness of regulation in India's financial landscape have

improved.

CONCLUSION:

1. In India, the primary objective of the stock market has been to generate capital and allocate it effectively to bolster the economy. Prior to the reforms of 1991, the country faced sluggish growth, rising public deficits, and challenges related to balance of payments. The protective policies aimed at shielding domestic industries from global competition hindered economic progress. The establishment of SEBI marked a transformative moment for the market, as it became an autonomous body that enhanced investor confidence and facilitated the development of the National Stock Exchange (NSE) and Depository Participants. Nevertheless, potential investors still harbor concerns. It is essential for the government to foster trust, provide transparent information, safeguard investor rights, and emphasize the stock market's role in economic development. In comparison to advanced economies such as the United States and Japan, India's economy could benefit from further support.

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