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Impact on Capital Market Reforms in India

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ABSTRACT

It is a financial market in which long-term debt or equity-backed securities are bought & sold. Capital markets are defined as markets in which money is provided for periods longer than a year. Capital markets channel the wealth of savers to those who can put it to long-term productive use, such as companies/ governments making long-term investments. Financial regulators, such as the UK's Bank of England (BoE) or the U.S. Securities & Exchange Commission (SEC), oversee the capital markets in their jurisdictions to protect investors against fraud, among other duties. A well-developed financial system is the backbone of any developed as well as fast developing economies. Capital market provides the financial backbone for business entities. Indian capital market has undergone tremendous changes after the Commencement of Securities & Exchange Board of India (SEBI) in 1992. A number of measures are taken by SEBI, Ministry of Finance, RBI & other regulators to make Indian stock market a dependable platform for Foreign Institutional Investors (FIIs), High Net worth Individuals (HNIs). Domestic Institutional Investors (DIs), & Retail Investors. Introduction of new products also helped in inviting potential investors (foreign as well as domestic) to Indian Capital Market. This paper discuss about the reforms of capital market in India & what is recent development in capital market

1. INTRODUCTION

Since independence, a number of steps have been taken by the Government of India to ensure the organized growth of capital market. The Capital Issues (control) Act 1948, The Companies Act 1956 and, The Securities Contracts (Regulation) Act 1956 are prominent among them. The Capital Issues (control) act 1948 was initiated to prevent, regulate and control investment by companies to protect the interests of the investors by examining the terms of capital issues, capital reorganization plans including mergers and amalgamations and foreign investment. The Companies Act 1956 envisaged an integrated pattern of relationship between the various components of corporate business. The main object of the Securities Contracts (Regulation) Act 1956 was to have a strong and healthy investment market and ensure investor confidence. The Monopolies and Restrictive Trade Practices Act (MRTP) which came into existence with effect from June 1, 1970 was to prevent concentration of economic power in private hands and to control restrictive trade practices. Moreover, a number of specialized financial and development corporations were established to finance large scale industrial development. Finally, the Reserve Bank of India and the government have been taken steps for the integration of organized and unorganized sectors of the capital market, development of rural credit, financial inclusion and the diversification of the functions of the commercial banks. In this section we summarize briefly the capital market reforms initiated since 1980s.

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2. OBJECTIVES OF THE STUDY

- To find out the capital reforms in India
- To know what are all the improvements that had brought into the capital markets
- To study about the capital market in India

Capital market is a market where buyers & sellers engage in trade of financial securities like bonds, stocks, etc. The buying/selling is undertaken by participants such as individuals & institutions. Capital markets help channelize surplus funds from savers to institutions which then invest them into productive use. Generally, this market trades mostly in long-term securities. Capital market consists of primary markets & secondary markets. Primary markets deal with trade of new issues of stocks & other securities, whereas secondary market deals with the exchange of existing or previously-issued securities. Another important division in the capital market is made on the basis of the nature of security traded, i.e. stock market & bond market

CAPITAL MARKET

The market where investment funds like bonds, equities & mortgages are traded is known as the capital market. The primal role of the capital market is to channelize investments from investors who have surplus funds to the ones who are running a deficit. The capital market offers both long term & overnight funds. The financial instruments that have short or medium term maturity periods are dealt in the money market whereas the financial instruments that have long maturity periods are dealt in the capital market. The different types of financial instruments that are traded in the capital markets are equity instruments, credit market instruments, insurance instruments, foreign exchange instruments, hybrid instruments & derivative instruments.

A capital market is a market for securities (both debt & equity), where business enterprises (companies) &governments can raise long-term funds. It is defined as a market in which money is lent for periods Greater than a year, as the raising of short-term funds takes place on other markets (e.g., the money market). The capital market includes the stock market (equity securities) & the bond market (debt).

CAPITAL MARKETS CONSISTS OF

- Primary market
- Secondary markets

PRIMARY MARKET

It is a part of the capital markets that deals with the issuance of new securities. Governments, Companies or public sector institutions can obtain funding through the sale of a new stock or bond issue. This is typically done through a syndicate of securities dealers. The process of selling new issues to investors is called underwriting. In the case of a new share issue, this sale is an initial public offering (IPO). Dealers earn a commission that is built into the price of the security offering, though it can be found in the prospectus.

ISSN:2277-2995
Vol-8-Issue-11-November-2019

The primary markets are where new stock & bonds issues are sold (via underwriting) to investors. The secondary markets are where existing securities are sold & bought from one investor or trader to another, over the counter, usually on a securities exchange, or elsewhere.

FEATURES OF PRIMARY MARKET

- This is the market for new long term equity capital. The primary market is the market where the securities are sold for the 1st time. Therefore it is also called the new issue market (NIM).
- In a primary issue, the securities are issued by the company directly to investors.
- The company receives the money & issues new security certificates to the investors.
- Primary issues are used by companies for the purpose of modernizing the existing business, new business etc.
- The primary market performs the crucial function of facilitating capital formation in the economy.
- The new issue market doesn't include certain other sources of new long term external finance, such as loans from financial institutions. Borrowers in the new issue market may be raising capital for converting private capital into public capital; this is known as "going public."
- The financial assets sold can only be redeemed by the original holder.

METHODS OF ISSUING SECURITIES IN THE PRIMARY MARKET ARE

- Initial public offering
- Rights issue (for existing companies)

An initial public stock offering (IPO) referred to simply as an "flotation" or" offering" is when a company issues common stock or shares to the public for the first time. They are often issued by smaller, younger companies seeking capital to expand, but can also be done by large privately-owned companies looking to become publicly traded.

A rights issue is offered to all existing shareholders individually & may be rejected, accepted in full or accepted in part. Rights are often transferable, allowing the holder to sell them on the open market. A right to a share is generally issued on a ratio basis (e.g. one-for-three rights issue). Because the company receives shareholders' money in exchange for shares, a rights issue is a source of capital.

SECONDARY MARKET

The secondary market, also known as the aftermarket, is the financial market where previously issued securities &financial instruments such as stock, bonds, options, &futures are bought & sold. The term "secondary market" is also used to refer to the market for any used goods or assets, or an alternative use for an existing product or asset where the customer base is the second market (for example, corn has been traditionally used primarily for food production feed stock, but a second- or third- market has developed for use in ethanol production).

Under a secondary market offering or seasoned equity offering of shares to raise money, a company can opt for a rights issue to raise capital. The rights issue is a special form of shelf

ISSN:2277-2995
Vol-8-Issue-11-November-2019
offering or shelf registration. With the issued rights, existing shareholders have the privilege to buy a specified number of new shares from the firm at a specified price within a specified time. A rights issue is in contrast to an initial public offering (primary market offering), where shares are issued to the general public through market exchanges. With primary issuances of securities or financial instruments, or the primary market, investors purchase these securities directly from issuers such as corporations issuing shares in an IPO or private placement, or directly from the federal government in the case of treasuries. After the initial issuance, investors can purchase from other investors in the secondary market. The secondary market for a variety of assets can vary from fragmented to centralized, & from illiquid to very liquid. The major stock exchanges are the most visible example of liquid secondary markets - in this case, for stocks of publicly traded companies.. Exchanges provide a centralized, liquid secondary market for the investors who own stocks that trade on those exchanges. Most bonds & structured products trade “over the counter,” or by phoning the bond desk of one’s broker-dealer.

FUNCTIONS OF SECONDARY MARKET

Secondary marketing is vital to an efficient & modern capital market. In the secondary market, securities are sold by & transferred from one investor or speculator to another. It is therefore important that the secondary market be highly liquid. As a general rule, the greater the number of investors that participate in a given marketplace, & the greater the centralization of that marketplace, the more liquid the market.

Fundamentally, secondary markets mesh the investor's preference for liquidity with the capital user's preference to be able to use the capital for an extended period of time

STOCK EXCHANGES

It is open markets that trade financial assets. Whether associated with a company or acting as an individual, a stock exchange is the place where stocks are bought & sold. There are a number of major stock exchanges around the world & each of these plays a part in determining the overall financial & economic condition of any economy. Stock exchanges deal with a number of financial instruments such as bonds, equities &stocks,. Both corporate & government bonds are traded in stock exchanges.

Equities include popular investment options, rights issues, bonus issues, & all other forms of shares & stocks. The actual trading of stocks takes place through mediators such as financial advisors, brokerage houses, & stockbrokers. A stock exchange, (formerly a securities exchange) is a corporation or mutual organization which provides "trading" facilities for stock brokers & traders, to trade stocks& other securities. It is also provide facilities for the issue & redemption of securities as well as other financial instruments & capital events including the payment of income &dividends. The securities traded on a stock exchange include: Stocks issued by companies, pooled investment products, bonds, derivatives & unit trusts. To be able to trade a security on a certain stock exchange, it has to be listed there.

Usually there is a central location at least for recordkeeping, but trade is less & less linked to such a physical place, as modern markets are electronic networks, which gives them advantages

ISSN:2277-2995
Vol-8-Issue-11-November-2019
of speed & cost of transactions. Trade on an exchange is by members only. The initial offering of stocks & bonds to investors is by definition done in the primary market& subsequent trading is done in the secondary market. It is often the most important component of a stock market. Supply &demand in stock markets are driven by various factors which, as in all affect the price of stocks (see stock valuation),free markets etc.

There is usually no compulsion to issue stock via the stock exchange itself, nor must stock be subsequently traded on the exchange. Such trading is said to be off exchange or over-the-counter. This is the usual way that derivatives &bonds are traded. Increasingly, stock exchanges are part of a global market for securities.

ROLE OF CAPITAL MARKET

The Major role of the capital market is to raise long-term funds for banks, governments, & corporations while providing a platform for the trading of securities. This fundraising is regulated by the performance of the stock & bond markets within the capital market.

The member organizations of the capital market may issue stocks & bonds in order to raise funds. Investors can then invest in the capital market by purchasing those stocks & bonds. The capital market, however, is not without risk. It is important for investors to understand market trends before fully investing in the capital market. To that end, there are various market indices available to investors that reflect the present performance of the market.

REGULATION OF THE CAPITAL MARKET

Every capital market in the world is monitored by financial regulators & their respective governance organization. The purpose of such regulation is to protect investors from fraud & deception. Financial regulatory bodies are also charged with minimizing financial losses, issuing licenses to financial service providers, & enforcing applicable laws.

CAPITAL MARKET’S INFLUENCE ON INTERNATIONAL TRADE

Capital market investment is no longer confined to the boundaries of a single nation. Today’s corporations & individuals are able, under some regulation, to invest in the capital market of any country in the world. Investment in foreign capital markets has caused substantial enhancement to the business of international trade.

THE PRIMARY & SECONDARY MARKETS

The capital market is also dependent on two sub-markets the primary market & the secondary market. The primary market deals with newly issued securities & is responsible for generating new long-term capital. The secondary market handles the trading of previously-issued securities, & must remain highly liquid in nature because most of the securities are sold by investors. A capital market with high liquidity & high transparency is predicated upon a secondary market with the same qualities.

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Vol-8-Issue-11-November-2019

REFORMS IN CAPITAL MARKET OF INDIA

Reforms in Indian Securities Market Since 1992 - October 15th, 2010
The development in Indian securities market since 1992 can be summarized as follows:

- Capital Issues (Control) Act of 1947 repealed and the office of Controller of Capital Issues abolished; control over price and premium of shares removed. Companies now free to raise funds from securities markets after filing prospectus with the Securities and Exchange Board of India (SEBI).
- The power to regulate stock exchanges delegated to SEBI by the Government.
- SEBI introduces regulations for primary and other secondary market intermediaries, bringing them within the regulatory framework.
- Reforms by SEBI in the primary market include improved disclosure standards, introduction of prudential norms, and simplification of issue procedures. Companies required disclosing all material facts and specific risk factors associated with their projects while making public issues.
- Listing agreements of stock exchanges amended to require listed companies to furnish annual statement to the exchanges showing variations between financial projections and projected utilization of funds in the offer document and actual figures. This is to enable shareholders to make comparisons between performance and promises.
- SEBI introduces a code of advertisement for public issues to ensure fair and truthful disclosures.
- Disclosure norms further strengthened by introducing cash flow statements.
- New issue procedures introduced—book building for institutional investors—aimed at reducing costs of issue.
- SEBI introduces regulations governing substantial acquisition of shares and takeovers and lays down conditions under which disclosures and mandatory public offers are to be made to the shareholders. Regulations further revised and strengthened in 1996.
- SEBI reconstitutes the governing boards of the stock exchanges and introduces capital adequacy norms for broker accounts.
- Private mutual funds permitted and several such funds already set up. All mutual funds allowed to apply for firm allotment in public issues—also aimed at reducing issue costs.
- Regulations for mutual funds revised in 1996, giving more flexibility to fund managers while increasing transparency, disclosure, and accountability.
- Over-the-Counter Exchange of India formed.
- National Stock Exchange (NSE) establishment as a stock exchange with nationwide electronic trading.
- Bombay Stock Exchange (BSE) introduces screen-based trading; 15 stock exchanges now have screened-based trading. BSE granted permission to expand its trading network to other centers.
- Capital adequacy requirement for brokers enforced.
- System of mark-to-market margins introduced in the stock exchanges.
- Stock lending scheme introduced.
- Transparency brought out in short selling.

ISSN:2277-2995
Vol-8-Issue-11-November-2019

- National Securities Clearing Corporation, Ltd. set up by NSE.
- BSE in the process of implementing a trade guarantee scheme.
- SEBI strengthens surveillance mechanisms and directs all stock exchanges to have separate surveillance departments.
- SEBI strengthens enforcement of its regulations. Begins the process of prosecuting companies for misstatements and ensures refunds of application money in several issues on account of misstatements in the prospectus.
- Indian companies permitted to access international capital markets through Euro issues.
- Foreign direct investment allowed in stock broking, asset management companies, merchant banking, and other non-bank finance companies.
- Foreign institutional investors (FIIs) allowed access to Indian capital markets on registration with SEBI.

Recent Developments in Capital Market of India

The Indian capital market has witnessed major reforms in the decade of 1990s and thereafter. It is on the verge of the growth.
Thus, the Government of India and SEBI has taken a number of measures in order to improve the working of the Indian stock exchanges and to make it more progressive and vibrant.

The major reforms undertaken in capital market of India includes:-

Establishment of SEBI:

The Securities and Exchange Board of India (SEBI) was established in 1988. It got a legal status in 1992. SEBI was primarily set up to regulate the activities of the merchant banks, to control the operations of mutual funds, to work as a promoter of the stock exchange activities and to act as a regulatory authority of new issue activities of companies. The SEBI was set up with the fundamental objective, "to protect the interest of investors in securities market and for matters connected therewith or incidental thereto."

The main functions of SEBI are:-

- To regulate the business of the stock market and other securities market.
- To promote and regulate the self regulatory organizations.
- To prohibit fraudulent and unfair trade practices in securities market.
- To promote awareness among investors and training of intermediaries about safety of market.
- To prohibit insider trading in securities market.
- To regulate huge acquisition of shares and takeover of companies.

ISSN:2277-2995
Vol-8-Issue-11-November-2019

ESTABLISHMENT OF CREDITORS RATING AGENCIES

Three creditors rating agencies viz. The Credit Rating Information Services of India Limited (CRISIL - 1988), the Investment Information and Credit Rating Agency of India Limited (ICRA - 1991) and Credit Analysis and Research Limited (CARE) were set up in order to assess the financial health of different financial institutions and agencies related to the stock market activities. It is a guide for the investors also in evaluating the risk of their investments.

INCREASING OF MERCHANT BANKING ACTIVITIES:

Many Indian and foreign commercial banks have set up their merchant banking divisions in the last few years. These divisions provide financial services such as underwriting facilities, issue organizing, consultancy services, etc. It has proved as a helping hand to factors related to the capital market.

CANDID PERFORMANCE OF INDIAN ECONOMY:

In the last few years, Indian economy is growing at a good speed. It has attracted a huge inflow of Foreign Institutional Investments (FII). The massive entry of FIIs in the Indian capital market has given good appreciation for the Indian investors in recent times. Similarly many new companies are emerging on the horizon of the Indian capital market to raise capital for their expansions.

RISING ELECTRONIC TRANSACTIONS

Due to technological development in the last few years. The physical transaction with more paper work is reduced. Now paperless transactions are increasing at a rapid rate. It saves money, time and energy of investors. Thus it has made investing safer and hassle free encouraging more people to join the capital market.

GROWING MUTUAL FUND INDUSTRY

The growing of mutual funds in India has certainly helped the capital market to grow. Public sector banks, foreign banks, financial institutions and joint mutual funds between the Indian and foreign firms have launched many new funds. A big diversification in terms of schemes, maturity, etc. has taken place in mutual funds in India. It has given a wide choice for the common investors to enter the capital market.

GROWING STOCK EXCHANGES

The numbers of various Stock Exchanges in India are increasing. Initially the BSE was the main exchange, but now after the setting up of the NSE and the OTCEI, stock exchanges have spread across the country. Recently a new Inter-connected Stock Exchange of India has joined the existing stock exchanges.

ISSN:2277-2995
Vol-8-Issue-11-November-2019

INVESTOR'S PROTECTION

Under the purview of the SEBI the Central Government of India has set up the Investors Education and Protection Fund (IEPF) in 2001. It works in educating and guiding investors. It tries to protect the interest of the small investors from frauds and malpractices in the capital market.

GROWTH OF DERIVATIVE TRANSACTIONS

Since June 2000, the NSE has introduced the derivatives trading in the equities. In November 2001 it also introduced the future and options transactions. These innovative products have given variety for the investment leading to the expansion of the capital market.

INSURANCE SECTOR REFORMS

Indian insurance sector has also witnessed massive reforms in last few years. The Insurance Regulatory and Development Authority (IRDA) was set up in 2000. It paved the entry of the private insurance firms in India. As many insurance companies invest their money in the capital market, it has expanded.

COMMODITY TRADING

Along with the trading of ordinary securities, the trading in commodities is also recently encouraged. The Multi Commodity Exchange (MCX) is set up. The volume of such transactions is growing at a splendid rate.

3. CONCLUSION

Based on this paper Indian Capital Market is already in the growth face. A clear policy decision from government, vigilant eye from the regulators, transparency from the stock exchanges & prudent action by the brokers & financiers is the requirement of the day to maintain the growth rate on the Securities Market. A strong capital market provides the foundation for a developed economy.

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