B.Com. Program in Accounting
Semester-IV
CC-8: Capital Market

Unit 4: Stock Exchange

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Definition:

A stock exchange is an exchange where stock brokers and traders can buy and sell shares of stock, bonds, and other securities. Many large companies have their stocks listed on a stock exchange.

A stock exchange, share market or bourse is an organization which provides "trading" facilities for stock brokers and traders, to trade shares of the listed companies and other financial instruments such as Term Finance Certificates and Derivatives. Stock exchanges also provide facilities for the issue (listing), redemption (delisting) of securities and other capital events including the payment of income and dividends.

Role and Functions Stock Exchange:

1. Continuous and ready market for securities

Stock exchange provides a ready and continuous market for purchase and sale of securities. It provides ready outlet for buying and selling of securities. Stock exchange also acts as an outlet/counter for the sale of listed securities

2. Facilitates evaluation of securities

Stock exchange is useful for the evaluation of industrial securities. This enables investors to know the true worth of their holdings at any time. Comparison of companies in the same industry is possible through stock exchange quotations (i.e. price list).

3. Encourages capital formation

Stock exchange accelerates the process of capital formation. It creates the habit of saving, investing and risk taking among the investing class and converts their savings into profitable investment. It acts as an instrument of capital formation. In addition, it also acts as a channel for right (safe and profitable) investment.

4. Provides safety and security in dealings

Stock exchange provides safety, security and equity (justice) in dealings as transactions are conducted as per well-defined rules and regulations. The managing body of the exchange keeps control on the members. Fraudulent practices are also checked effectively. Due to various rules and regulations, stock exchange functions as the custodian of funds of genuine investors.

5. Regulates company management

Listed companies have to comply with rules and regulations of concerned stock exchange and work under the vigilance (i.e. supervision) of stock exchange authorities.

6. Facilitates public borrowing

Stock exchange serves as a platform for marketing Government securities. It enables government to raise public debt easily and quickly.

7. Provides clearing house facility

Stock exchange provides a clearing house facility to members. It settles the transactions among the members quickly and with ease. The members have to pay or receive only the net dues (balance amounts) because of the clearing house facility.

8. Facilitates healthy speculation

Healthy speculation, keeps the exchange active. Normal speculation is not dangerous but provides more business to the exchange. However, excessive speculation is undesirable as it is dangerous to investors & the growth of corporate sector.

9. Serves as Economic Barometer

Stock exchange indicates the state of health of companies and the national economy. It acts as a barometer of the economic situation / conditions.

10. Facilitates Bank Lending

Banks easily know the prices of quoted securities. They offer loans to customers against corporate securities. This gives convenience to the owners of securities.

11. Raising capital for businesses

Exchanges help companies to capitalize by selling shares to the investing public.

12. Mobilizing savings for investment

They help public to mobilize their savings to invest in high yielding economic sectors, which results in higher yield, both to the individual and to the national economy.

13. Facilitating company growth

They help companies to expand and grow by acquisition or fusion.

14. Profit sharing

They help both casual and professional stock investors, to get their share in the wealth of profitable businesses.

15. Corporate governance

Stock exchanges impose stringent rules to get listed in them. So listed public companies have better management records than privately held companies.

16. Creating investment opportunities for small investors

Small investors can also participate in the growth of large companies, by buying a small number of shares.

17. Government capital raising for development projects

They help government to raise fund for developmental activities through the issue of bonds. An investor who buys them will be lending money to the government, which is more secure, and sometimes enjoys tax benefits also.

Stock Exchange In India

1. Bombay Stock Exchange BSE: BSE is the leading and the oldest stock exchange in India as well as in Asia. It was established in 1887 with the formation of "The Native Share and Stock Brokers' Association". BSE is a very active stock exchange with highest number of listed securities in India. Nearly 70% to 80% of all transactions in the India are done alone in BSE. Companies traded on BSE were 3,049 by March, 2006. BSE is now a national stock exchange as the BSE has started allowing its members to set-up computer terminals outside the city of Mumbai (former Bombay). It is the only stock exchange in

India which is given permanent recognition by the government. At present, (Since 1980) BSE is located in Mumbai.

2. National Stock Exchange NSE: Formation of National Stock Exchange of India Limited (NSE) in 1992 is one important development in the Indian capital market. The need was felt by the industry and investing community since 1991. The NSE is slowly becoming the leading stock exchange in terms of technology, systems and practices in due course of time. NSE is the largest and most modern stock exchange in India. In addition, it is the third largest exchange in the world.
3. Multi Commodity Exchange(MCX): Multi Commodity Exchange of India Ltd (MCX) is an independent commodity exchange based in India. It was established in 2003 and is based in Mumbai. It is India's largest commodity derivatives exchange where the clearance and settlements of the exchange happens and the turnover of the exchange for quarter ended September 2018 was 1.78 billion rupees. MCX offers options trading in gold and futures trading in non-ferrous metals, bullion, energy, and a number of agricultural commodities (mentha oil, cardamom, crude palm oil, cotton and others).

Major International Stock Exchanges:

1. New York Stock Exchange: The New York Stock Exchange (NYSE) is part of NYSE EURONEXT, which now has exchanges in the U.S. and Europe. It estimates that its exchanges represent a third of all equities traded in the world. The NYSE continues to be one of the primary exchanges in the world and the largest in terms of the nearly $10 trillion in stock market capitalization it represents.
2. Tokyo Stock Exchange: The Tokyo Stock Exchange (TSE) is the largest exchange in Japan and also number two behind the NYSE in terms of the more than $3 trillion in market capitalization the companies on its exchange represent. A stronger national currency is part of the reason behind the increasing size of the TSE. Around 2,000 firms are listed on the TSE.
3. London Stock Exchange: The London Stock Exchange (LSE) qualifies as a top five stock market, with an estimated $2.2 trillion in stock market capitalization from the companies listed on its exchange. Its estimated founding was 1801, or nearly a decade following the opening of the NYSE.
4. Hong Kong Stock Exchange: The Hong Kong Stock Exchange is one of the top 10 largest stock exchanges. The firms that are listed on the Hong Kong Stock Exchange represent close to $2 trillion in total market capitalization. Roughly 1,500 companies are listed on the exchange, which dates back to just prior to 1900, when it first started operating. Most importantly, the exchange represents one of the primary avenues for global investors to invest in China.
5. Shanghai Stock Exchange: The Shanghai Stock Exchange is one of the newest in the world. It opened in late 1990, and 1,500 companies trade on its exchange. Trading volume continues to increase, but has fallen dramatically since 2008, which marked a peak in terms of investment interest in China.
6. The Bottom Line: Exchanges that also deserve mention include the Nasdaq, which is also based in the U.S., The Bombay Stock Exchange in India, Sao Paulo Stock Exchange in Brazil and the Australian Stock Exchange also continue to grow in influence on the global stage. The current global recession has slowed the progress of emerging markets, but they are expected to continue to gain market share in the coming decades as their

economies grow and new firms go public and raise capital to serve a growing class of consumers, and continue to grow the worldwide network of exchanges.

Method of Trading In A Stock Exchange:

The Trading procedure involves the following steps:

1. Selection of a broker: The buying and selling of securities can only be done through SEBI registered brokers who are members of the Stock Exchange. The broker can be an individual, partnership firms or corporate bodies. So the first step is to select a broker who will buy/sell securities on behalf of the investor or speculator.

2. Opening Demat Account with Depository: Demat (Dematerialized) account refer to an account which an Indian citizen must open with the depository participant (banks or stock brokers) to trade in listed securities in electronic form. Second step in trading procedure is to open a Demat account.

3. Placing the Order:

After opening the Demat Account, the investor can place the order. The order can be placed to the broker either (DP) personally or through phone, email, etc.

Investor must place the order very clearly specifying the range of price at which securities can be bought or sold. e.g. "Buy 100 equity shares of Reliance for not more than Rs 500 per share."

4. Executing the Order:

As per the Instructions of the investor, the broker executes the order i.e. he buys or sells the securities. Broker prepares a contract note for the order executed. The contract note contains the name and the price of securities, name of parties and brokerage (commission) charged by him. Contract note is signed by the broker.

5. Settlement:

This means actual transfer of securities. This is the last stage in the trading of securities done by the broker on behalf of their clients. There can be two types of settlement.

(a) On the spot settlement:

It means settlement is done immediately and on spot settlement follows. T + 2 rolling settlement. This means any trade taking place on Monday gets settled by Wednesday.

(b) Forward settlement:

It means settlement will take place on some future date. It can be T + 5 or T + 7, etc. All trading in stock exchanges takes place between 9.55 am and 3.30 pm. Monday to Friday.

What is Online Trading?

Online trading involves the trading of securities through an online platform. Online trading portals facilitate the trading of various financial instruments such as equities, mutual funds, and commodities. Angel Broking offers Angel Speed Pro - an online trading platform that helps investors and traders to buy/sell stocks and other financial instruments.

Advantages of Online Trading:

The advantages are briefly discussed below:

1. It is convenient: When it comes to online trading, you only need to open a trading account via internet and you're good to go. You're not bound by time and place as long

as you have an internet connection. Hence, online trading is convenient and accessible from anywhere with limited hassle. It also saves time.

2. It is cheaper: In online stock trading, the stock broker fee which you will have to pay is lower when compared to the commission charged by traditional method. If you trade in a sufficiently large volume of stocks, it is possible for you to be able to negotiate your broker’s fees.
3. Anyone can monitor his investments anytime: Online trading allows you to buy or sell shares according to your convenience. It offers advanced interfaces and the ability for investors to see how their money is performing throughout the day. You can use your phone or your computer to evaluate your profit or loss.
4. It almost eliminates the middleman: Online trading allows you to trade with virtually no direct broker communication. Apart from reducing the overall trading cost, this benefit also makes the trading hassle free, making this service much more lucrative.
5. Investor has greater control: Online traders can trade whenever they wish to. On the other hand, in traditional trading, an investor may be stuck until he or she is able to contact their broker or when the broker is able to place their order. Online trading allows nearly instantaneous transactions.
6. Faster Transactions: Online banking is fast and efficient. Funds can be transferred between accounts almost instantly, especially if the two accounts are held at the same banking institution. All it takes to be able to buy or sell stocks is a single click of the mouse. Through this, a quicker exchange can be made which may also ensure quicker earnings.
7. Better understanding of one’s money: This is a hidden advantage of online trading which you wouldn’t want to pass up on. Just like conventional stock trading, you can predict the market behavior and use this to predict a rise or fall in price of the stock. You’ll be handling your own finances and be responsible for them. Over time, you become more experienced in understanding the market, and good investment opportunities from the bad ones. This knowledge about money is very useful, and having this on your resume makes you more marketable to companies looking to fill a well-paying position in the finance department. So while making a quick buck, you also manage to become financially smarter, in both your professional and personal life.

What is NSE-NEAT ?

NSE operates on the 'National Exchange for Automated Trading' (NEAT) system, a fully automated screen based trading system, which adopts the principle of an order driven market. NSE consciously opted in favour of an order driven system as opposed to a quote driven system. This has helped reduce jobbing spreads not only on NSE but in other exchanges as well, thus reducing transaction costs.

What is Stock Indices?

An index is an indicator or measure of something, and in finance, it typically refers to a statistical measure of change in a securities market. In the case of financial markets, stock and bond market indices consist of a hypothetical portfolio of securities representing a particular market or a segment of it.

A stock index or stock market index is a measurement of a section of the stock market. It is computed from the prices of selected stocks (typically a weighted average). It is a tool used by investors and financial managers to describe the market, and to compare the return on specific investments.

Defects of Indian Capital Market:

The Indian capital market suffers from the following deficiencies:

1. Lack of diversity in the financial instruments.
2. Lack of control over the fair disclosure of financial information.
3. Poor growth in the secondary market.
4. Prevalence of insider trading and front running.1
5. Manipulation of security prices.
6. Existence of unofficial trade in the primary market, prior to the issue coming into the market.
7. Absence of proper control over brokers and sub-brokers.
8. Passive role of public financial institutions in checking malpractices.
9. High cost of transactions and intermediation, mainly due to the absence of well-defined norms for institutional investment.

Recent developments in Capital Market:

We can pinpoint the following developments in Indian capital market that had helped India to compete with developed countries around the world.

1. Economic Liberalization due to Indian Capital Market:

The economic liberalization has led to more deregulation, liberalization and privatization of some of the public sector undertakings in India. This has resulted in the shares of some of the public sector undertakings being made available to the public. The Industrial policy adopted by the government earlier did not allow investment in core sector by either individuals or private sector. But, with the privatization of some of the public sector undertakings, the shares are now available to the public for contribution.

2. Promoting more private sector banks:

Opening of more private sector banks has resulted in the public contributing to the shares of these banks in Indian capital Market. Recently, the government has announced 74% equity participation by foreigners in private sector banks in India. This has not only promoted new banks but also paved the way for the merger of existing banks with other banks. Example: The merger of Bank of Madura with ICICI Bank.

3. Promotion of Mutual Funds:

The promotion of mutual funds by nationalized as well as non-nationalized banks has also improved the Indian capital market. They were helpful to the public by way of tax saving schemes.

4. Regulation of NRI Investments:

The Amendment of Foreign Exchange Regulation Act (FERA) into Foreign Exchange Management Act (FEMA) has given more encouragement to non resident investors. The percentage of NRI investment in Indian companies has been increased from 5% to 24%.

5. Direct Foreign Investment:

The Foreign Investment Promotion Board, consisting of the Secretaries of industries, finance and foreign affairs, have allowed more direct foreign investment in core sector, especially in power sector.

6. FERA Companies:
Under the Foreign Exchange Regulation Act, a FERA company is one which has 40% equity participation by foreigners. This limit has been removed and now even foreign companies are allowed to have 51% equity participation.
7. Online Trading in Indian Capital Market:
Some of the leading stock markets in India have introduced computer system for their trading activities. The brokers can get hooked-up and do their trading on Online basis. The computer terminals will enable the public and the brokers to know the price prevailing in the market at any time. This will prevent speculation activities.
8. Transparency through Online trading:
The online trading through computer has brought in transparency to the transactions in the market. People are able to know prices prevailing in the market at any time and as such the brokers cannot deprive their clients of their profits.
9. National Stock Exchange:
A new stock market called National Stock Exchange has been created which has a large number of companies listed. It is a big competitor to the Bombay Stock Exchange and it is able to even influence the Bombay Stock Exchange.
10. Sensitivity Index in Indian Capital Market:
The calculation of index number has also undergone a change. Sensitivity index has been introduced which represents important 30 companies whose volume and value of shares determines the market condition.
11. Circuit-Breaker in Indian Capital Market:
Wild fluctuations in the stock market is a thing of the past. There cannot be any more 'stock scam' as engineered by Harshad Metha. For this purpose, the Bombay stock market has introduced a cut-off switch which is called circuit breaker. Whenever the market index goes up by more than 10%, the circuit breaker will go off, bringing the entire operations in the market to a standstill. This will be for a period of 30 minutes after which the market will resume. This will bring down the share price. The stock market operates for two hours each day and any termination in the circuit breaker, after initial 1 and half hours of working will result in the market closing for the day. Since the market operations cannot be resumed for the day, share prices will fall. Wild speculation in shares will be a thing of the past.
12. Demating of shares in Indian Capital Market:
The introduction of demating has resulted in improving transactions further. Demating is a system under which physical delivery of shares is no more adopted. It is called "scripless trade". The shares of individual investors are held by stock holding company and a pass book is given to individual investors.
13. Market Makers in Indian Capital Market:
The share price of companies will be decided by the market forces of supply and demand. There are market makers who will ensure the supply and reasonable price for the stocks of companies. By the introduction of these market makers, manipulation of share price by the brokers is prevented.
14. Securities and Exchange Board of India:
The creation of Securities and Exchange Board of India (SEBI) is an important development in Indian capital market of India. SEBI has not only replaced the Controller of Capital issues, but has brought in uniformity in the transactions in all stock exchanges.

15. Renewal of Registration:
All the brokers and sub brokers have to register afresh with SEBI and any complaints against them will be inquired and if found guilty, punishment is given.
16. Over The Counter Exchange of India (OTCEI):
For the purpose of newly promoted companies, another stock exchange with lesser degree of conditions has been promoted and it is called Over The Counter Exchange of India (OTCEI).
17. Merchant banker:
Merchant bankers have been permitted to take part in the stock market. operations and their functions are also regulated by SEBI.
18. Non Banking Financial Companies:
The role of non-financial companies has also been controlled. RBI has introduced new conditions, restricting their activities. New norms with regard to capital of non banking financial companies have been introduced. For chit funds, a separate Act has been passed and it restricts the maximum bidding to 40%.
19. Forward trading in Indian Capital market:
Forward trading has been introduced since 9th June 2000 in Bombay Stock Exchange on a trial basis and if found successful, it will be extended. It will be helpful to the investors in ascertaining the true colors of existing companies.
20. Restrictions on Mutual Fund's Investment:
There have been restrictions on the role of mutual funds in the market. They cannot invest more than 10% of their investable funds in any single company and not more than 10% of single company's issue of shares can be purchased by mutual funds.
21. Educating Public:
Press and media have contributed a lot in popularizing the Indian capital market and they are highlighting the prices of securities everyday. The mutual funds and merchant banks have been asked to set apart a portion of their funds towards educating the public on the developments in the Indian capital market.
22. Government Securities Market:
After the stock scam, the Central Government has de-linked Government securities from trading along with company securities. In other words, there will be separate market for Government securities and they will not be dealt along with company securities in the stock market. The measure was taken by Dr. Manmohan Singh when he was the Finance Minister.
24. Future trading in Indian Capital Market:
Future trading is a contract to buy or sell a particular financial instrument on a future date at a specific price. The contract enables the parties to transfer according to the changes in the price from one person to another. By this, the risk is minimized.
24. Penalty for insider trading in Indian Capital Market:
In 2002, SEBI Act was amended to make insider trading punishable as a serious offense. The penalty rate has been enhanced to Rs. 1 lakh per day and the maximum penalty can go up to Rs. 25 crores.
25. Period of settlement in Indian Capital Market:
After removing the Badla, SEBI has introduced T+2…… – system for settling transactions in Indian capital market. Accordingly, all transactions entered in the capital market, should be completed within 2 days excluding the date of trading.

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