Abstract

A security is a tradable financial asset. The term commonly refers to any form of financial instrument, but its legal definition varies by jurisdiction. In some jurisdictions the term specifically excludes financial instruments other than equities and fixed income instruments. In some jurisdictions it includes some instruments that are close to equities and fixed income, e.g. equity warrants. In some countries and/or languages the term "security" is commonly used in day-to-day parlance to mean any form of financial instrument, even though the underlying legal and regulatory regime may not have such a broad definition. This paper is an attempt to explore the evolution and structure of security market in India.

1. Introduction

A financial system consists of institutional units and markets that interact, typically in a complex manner, for the purpose of mobilizing funds for

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1 An institutional unit is an entity such as a household, a corporation, or government agency that is capable in its own rights of owing assets incurring liabilities, and engaging in economic activities and transactions with other entities.
investment and providing facilities, including payment systems, for the financing of commercial activity. The role of financial institutions within the system is primarily to intermediate between those that provide funds and those that need funds, and typically involves transforming and managing risk. Particularly for a deposit taker, this risk arises from its role in maturity transformation, where liabilities are typically short term (for example, demand deposits), while its assets have a longer maturity and are often illiquid (for example, loans). Financial markets provide a forum within which financial claims can be traded under established rules of conduct and can facilitate the management and transformation of risk. Financial systems are of crucial significance to capital formation. The adequate capital formation is indispensable to a speedy economic development is universally recognized in academic literature. The main function of financial system is the collection of savings and their distribution for industrial investment, thereby stimulating the capital formation and, to that extent, accelerating the process of economic growth. The process of capital formation involves three distinct, although interrelated activities:

i. Savings: The ability by which claims to resources are set aside and become available for other purposes.

ii. Finance: The activities by which claims to resources are either assembled from those released by domestic savings, obtained from abroad, or specially created usually as bank deposits or notes and then placed in the hands of the investors.

iii. Investments: The activity by which resources are actually committed to production.

The volume of capital formation depends upon the intensity and efficiency with which these activities are carried on. The effective mobilization of savings, the efficiency of the financial organization/systems and the channelization of these savings into the most desirable and productive forms of investment are all inter-
connected and have a great bearing on the contribution of capital formation to economic development.

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Securities market is a component of the wider financial market where securities can be bought and sold between subjects of the economy, on the basis of demand and supply. Securities markets encompasses equity markets, bond markets and derivatives markets where prices can be determined and participants both professional and non professionals can meet.

2 Objectives and Research Methodology

Objectives of study:

1. To explore the evolution of Security Market in India.
2. To find the structure of Indian security Market.
3. To analyze the contribution of Security Market towards the Economic.

Research Methodology

It is always important to be critical of the information presented in sources, especially since the material might have been gathered to address a different problem area. Moreover, many secondary sources do not clearly describe issues such as the purpose of a study, how the data has been gathered, analysed and interpreted making it difficult for the researcher to assess their usefulness. In
order to address this problem I have tried to triangulate the secondary data by using numerous independent sources.

The information about the problem is collected from the Research Journals, Trade Magazines, Annual Reports of Banks and the Internet. For evaluating ‘Evolution and Structure of security Market in India’, we have focused on as recent material as possible. In order to get access to the latest developments in this area we have used a number of articles published in academic journals and trade magazines. We have also used secondary information from Internet based discussion forums.

3. Evolution of Securities Market in India:

The securities markets in India have witnessed several policy initiatives, which has refined the market micro-structure, modernised operations and broadened investment choices for the investors. The irregularities in the securities transactions in the last quarter of 2000-01, hastened the introduction and implementation of several reforms. While a Joint Parliamentary Committee was constituted to go into the irregularities and manipulations in all their ramifications in all transactions relating to securities, decisions were taken to complete the process of demutualisation and corporatisation of stock exchanges to separate ownership, management and trading rights on stock exchanges and to effect legislative changes for investor protection, and to enhance the effectiveness of SEBI as the capital market regulator. Rolling settlement on T+5 basis was introduced in respect of most active 251 securities from July 2, 2001 and in respect of balance securities from 31st December 2001. Rolling settlement on T+3 basis commenced for all listed securities from April 1, 2002 and subsequently on T+2 basis from April 1, 2003. All deferral products such as carry forward were banned from July 2, 2002.

At the end of March 2008, there were 1,381 companies listed at NSE and 1,236 companies were available for trading. The Capital Market segment of NSE
reported a trading volume of Rs.35,51,038 crore during 2007-08 and at the end of March 2008, the NSE Market Capitalisation was Rs.48,58,122 crore.

**Securities market** is a component of the wider financial market where securities can be bought and sold between subjects of the economy, on the basis of demand and supply. Securities markets encompasses equity markets, bond markets and derivatives markets where prices can be determined and participants both professional and non professionals can meet.

Securities markets can be split into two levels. Primary markets, where new securities are issued and secondary markets where existing securities can be bought and sold. Secondary markets can further be split into organised exchanges, such stock exchanges and over-the-counter where individual parties come together and buy or sell securities directly. For securities holders knowing that a secondary market exists in which their securities may be sold and converted into cash increases the willingness of people to hold stocks and bonds and thus increases the ability of firms to issue securities.

There are a number of professional participants of a securities market and these include; brokerages, broker-dealers, market makers, investment managers, speculators as well as those providing the infrastructure, such as clearing houses and securities depositories.

A securities market is used in an economy to attract new capital, transfer real assets in financial assets, determine price which will balance demand and supply and provide a means to invest money both short and long term.

**4. Structure of Security Market in India**

The structure of Indian security market can be explained properly with the help of a diagram.
4.1 Industrial Security Market: The industrial security market refers to the market for share and bonds of the existing companies, as well as those of new companies. This market is further divided into New Issue Market (NIM) and Secondary Market. The NIM is also called Primary Market. Likewise, secondary market is also termed as stock exchange.

However, it is important to emphasize that the New Issue Market and Stock exchange are inter-linked and work in conjunction with each other. Although they differ from each other in the sense that the New Issue Market only deals with issuance of new securities or we can say that the security are introduced in the market called new issue or primary market and stock exchange deals with those securities which have already been issued for the public or private.

i- Primary Market: Stocks available for the first time are offered through new issue market. The issuer may be a new company or an existing company. The primary market is concerned with the floatation of new shares or bonds. The merchant banking
division of commercial banks are asked by the company to advise on the viability of floatation of an issue before an issue is actually floated in the market.

The stock issuing companies also approaches the institutional underwriters like LIC, UTI, IDBI, and ICICI to ensure the marketability of an issue. The underwriter like LIC and UTI purchase securities from the new issue market to hold these in their own asset portfolio.

In Indian capital market there are two main ways for floating the new issue.

(a) Public purchase, and
(b) Right issue

(a) Public Purchase: The most popular method for floating securities in New issue market is through legal document called “Prospectus”. It is an open invitation to the public to subscribe to the issue at par or at premium.

(b) Right Issue: This method of the sale of the stock is normally used by existing companies whose shares are already listed in stock exchanges. Right issue represents an invitation to the existing shareholders to subscribe to a part or the whole of the new issue in a fixed proportion to their shareholding.

ii. Secondary Market: The market for long term securities like bonds. Equity stocks and preferred stocks is divided into primary and secondary market. The primary market deals with the new issues of securities whereas outstanding securities are traded in the secondary market, which is commonly known as stock market or stock exchange. In the secondary market, investors can sell or purchase
securities. Stock market predominantly deals in the equity market. The secondary market deals with the existing securities. This market provides both liquidity and marketability to such securities.

The secondary market of securities in India functions through following its two segments:

(a) Stock Exchange
(b) Over-the-Counter market

(a) **Stock Exchange:** Stock exchange is an organized market for sale and purchase of second hand listed industrial and financial securities. Listed securities are those securities which appear on the approved list of a stock exchange. Only listed securities are traded on the floor of the stock exchange. It is to be noted that an organized stock exchange is an ‘auction’ type of stock market, where the price of traded securities are settled by open bids and offers on the floor of the exchange.

(b) **Over The Counter Market:** The OTC Exchange Of India was founded in 1990 under the Companies Act 1956 and was recognized by the Securities Contracts Regulation Act, 1956 as a stock exchange but it started in 1992 after the establishment of NASDAQ (National Association of Securities Dealers Automated Quotation) and JASDAQ (Japanese Association of Securities Dealers Automated Quotation). The OTCEI was started with the objective of providing a market for the smaller companies that could not afford the listing fees of the large exchanges and did not fulfill the minimum capital requirement for listing.
4.2 Government Security Market: The term ‘Gilt edged’ means the best quality. Since government securities are of best qualities in the sense of liquidity and zero degree of risk of default, so these are called gilt-edged securities. In the gilt-edged market, the securities of Government of India and of the State Government are traded in; the securities guaranteed by the government are also traded in the market.

The importance of Government securities market, i.e., Gilt-edged market, as a segment of capital market, emanates from the fact that this market provides a mechanism for the management of public debt and open market operations to the Reserve Bank of India. It is therefore, imperative to emphasize that this market has a strong bearing on the formulation of fiscal policy of the Government of India and the monetary policy of the RBI.

Growth of the Central’s Government Securities: The growth of security market is an integral part of the process of economic growth in a free market economy. Of late, the RBI and Government of India have pursued certain measures to reform the security market. These reforms have been introduced in both the New issue market and the secondary market of industrial securities and government securities.

Products, Participants and Functions: Transfer of resources from those with idle resources to others who have a productive need for them is perhaps most efficiently achieved through the securities markets. Stated formally, securities markets provide channels for reallocation of savings to investments and entrepreneurship and thereby decouple these two activities. As a result, the savers and investors are not constrained by their individual abilities, but by the economy’s abilities to invest and save respectively, which inevitably enhances savings and investment in the economy.

Savings are linked to investments by a variety of intermediaries through a range of complex financial products called “securities” which is defined in the
Securities Contracts (Regulation) Act, 1956 to include: (1) shares, scrips, stocks, bonds, debentures, debenture stock or other marketable securities of a like nature in or of any incorporated company or body corporate; (a) derivatives; (b) units of any other instrument issued by any collective investment scheme to the investors in such schemes; (c) security receipt as defined in clause (zg) of section 2 of the Securitization and Reconstruction of Financial Assets and Enforcement of Security Interest Act, 2002; (d) units or any other such instrument issued to the investors under any mutual fund scheme; (e) any certificate or instrument (by whatever name called), issued to an investor by any issuer being a special purpose distinct entity which possesses any debt or receivable, including mortgage debt, assigned to such entity, and acknowledging beneficial interest of such investor in such debt or receivable, including mortgage debt, as the case may be; (2) government securities, (a) such other instruments as may be declared by the Central Government to be securities; and (3) rights or interest in securities.

There are a set of economic units who demand securities in lieu of funds and others who supply securities for funds. These demand for and supply of securities and funds determine, under competitive market conditions in both goods and securities market, the prices of securities which reflect the present value of future prospects of the issuer, adjusted for risks and also prices of funds.

It is not that the users and suppliers of funds meet each other and exchange funds for securities. It is difficult to accomplish such double coincidence of wants. The amount of funds supplied by the supplier may not be the amount needed by the user. Similarly, the risk, liquidity and maturity characteristics of the securities issued by the issuer may not match preference of the supplier. In such cases, they incur substantial search costs to find each other. Search costs are minimised by the intermediaries who match and bring the suppliers and users of funds together. These intermediaries may act as agents to match the needs of users and suppliers of funds for a commission, help suppliers and users
in creation and sale of securities for a fee or buy the securities issued by users and in turn, sell their own securities to suppliers to book profit. It is, thus, a misnomer that securities market disintermediates by establishing a direct relationship between the savers and the users of funds. The market does not work in a vacuum; it requires services of a large variety of intermediaries. The disintermediation in the securities market is in fact an intermediation with a difference; it is a risk-less intermediation, where the ultimate risks are borne by the savers and not the intermediaries.

The securities market, thus, has essentially three categories of participants, namely the issuers of securities, investors in securities and the intermediaries. The issuers and investors are the consumers of services rendered by the intermediaries while the investors are consumers (they subscribe for and trade in securities) of securities issued by issuers. In pursuit of providing a product to meet the needs of each investor and issuer, the intermediaries churn out more and more complicated products. They educate and guide them in their dealings and bring them together. Those who receive funds in exchange for securities and those who receive securities in exchange for funds often need the reassurance that it is safe to do so. This reassurance is provided by the law and by custom, often enforced by the regulator. The regulator develops fair market practices and regulates the conduct of issuers of securities and the intermediaries so as to protect the interests of suppliers of funds. The regulator ensures a high standard of service from intermediaries and supply of quality securities and non-manipulated demand for them in the market.

5. Contribution of Security Market in Economic Development

Three main sets of entities depend on securities market. While the corporate and governments raise resources from the securities market to meet their obligations, the households invest their savings in the securities.
**Corporate Sector:** The 1990s witnessed emergence of the securities market as a major source of finance for trade and industry. A growing number of companies are accessing the securities market rather than depending on loans from FIs/banks. The corporate sector is increasingly depending on external sources for meeting its funding requirements. There appears to be growing preference for direct financing (equity and debt) to indirect financing (bank loan) within the external sources.

The listing agreements have been amended recently requiring the companies to disclose shareholding pattern on a quarterly basis. As per the shareholding pattern of companies listed on NSE at end of March 2008, it is observed that on an average the promoters hold about 56.12% of total shares. Though the non-promoter holding is about 41.91%, Individuals held only 13.07% and the institutional holding (FIIs, MFs, VCFs-Indian and Foreign) accounted for 19.37%.

**Governments:** Along with increase in fiscal deficits of the governments, the dependence on market borrowings to finance fiscal deficits has increased over the years. During the year 1990-91, the state governments and the central government financed nearly 14% and 18% respectively of their fiscal deficit by market borrowing. In percentage terms, dependence of the state governments on market borrowing did not increase much during the decade 1991-2001. However, their dependence on market borrowing has been increasing since then to reach 38% during 2003-04. In case of central government, it increased to 73% by 2007-08. The central government and the state governments now-a-days finance about three fourth and one fourth of their fiscal deficits respectively through borrowings from the securities market.

**Households:** According to RBI data, household sector accounted for 84.8% of gross domestic savings in Fixed Income Investment instruments during 2006-07. They invested 55.7% of financial savings in deposits, 24.2 % in insurance/provident funds, and 6.5% in securities market including government
securities, units of mutual funds and other securities (out of which investment in Gilts has been 0.2%).

Though there was a major shift in the saving pattern of the household sector from physical assets to financial assets and within financial assets, from bank deposits to securities, the trend got reversed in the recent past due to high real interest rates, prolonged subdued conditions in the secondary market, lack of confidence by the issuers in the success of issue process as well as of investors in the credibility of the issuers and the systems and poor performance of mutual funds. The portfolio of household sector remains heavily weighted in favour of physical assets and fixed income bearing instruments.

6. Conclusion

With reference to the above study we may conclude that A security is a tradable financial asset. The term commonly refers to any form of financial instrument, but its legal definition varies by jurisdiction. In some jurisdictions the term specifically excludes financial instruments other than equities and fixed income instruments. This paper has undertook various studies and may conclude that security market has strengthened and contributed a lot towards the economic growth of India.

7. References


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