ROLE OF CAPITAL MARKET IN INDIAN ECONOMY

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ABSTRACT

Capital market plays an extremely important role in promoting and sustaining the growth of an economy. It is an important and efficient instrument to channel and mobilize funds to enterprises, and provide an effective source of investment in the economy. With the pace of economic reforms followed in India, the importance of capital markets has grown in the last ten years. Corporate both in the private sector as well as in the public sector raise thousands of crores of rupees in these markets. The governments, through Reserve Bank of India, as well as financial institutes also raise a lot of money from these markets. The capital market serves a very useful purpose by pooling the savings. The capital markets encourage capital formation in the country. The capital markets mobilize savings of the households and of the industrial concerns. Such savings are then invested for productive purposes. Capital markets also facilitate the growth of the industrial sector, as well as the other sectors of the economy, provide funds for the projects in backward areas. Thus, Capital markets generate employment in the country. This paper tries to focus on the importance of capital markets in the economic development of India, trends in capital market, stock exchanges performance and how to take advantage of loopholes in Indian stock market.

Key words: Indian capital market, importance, trends, stock exchanges, stock traders.

INTRODUCTION

Capital market in any country plays a pivotal role in the growth of economy and meeting country's socio economic goals. They are an important constituent of the financial system, given their role in the financial intermediation process and capital formation of the country. The importance of the capital market cannot be underemphasized for developing economy like India which needs significant amount of capital for the development of strong infrastructure

The story of Capital Markets in India dates back to the 18th century when trading shares of East India commenced. The real story of India's Capital Markets started in July 1875 with the formation of Stock Exchange in Mumbai by the brokers. India's Capital Market in terms of GDP raised from 75 percent in 1995 to 130 percent of GDP in 2005. But the relative growth compared to US, Malaysia and South Korea remains low, indicating immense untapped potential.

Capital Market is a channel through which the wealth of savers are put into long-term productive use. Both the Equity and Bond markets are parts of Capital Markets. Governments and Companies use Capital Markets to raise money for their long-term investments. The capital is raised through debt and equity instruments. Modern capital markets are hosted on computer based electronic trading system which can be accessed by entities within the financial sector. The capital market can be divided into:

1) Primary Market: It deals with issue of new securities .Companies, government, and public sector institutions can obtain funds through sale of new stock or bonds issue.

2) Secondary Market: It deals with trading of existing securities. It is also called liquid market. In this market the securities are sold by or transferred from one investor to another. Thus, this market gives liquidity to the long term securities.

The role of capital markets is vital for inclusive growth in terms of wealth distribution and making capital safer for investors. Capital markets can create greater financial inclusion by introducing new products and services tailored to suit investors' preference for risk and return as well as borrowers' project needs and risk appetite. A well-developed capital market creates a sustainable low-cost distribution mechanism for multiple financial products and services across the country.

OBJECTIVES:

- To gain insight into the introduction on capital markets in India.
- To study the components of the capital market.
- To study the role of the capital market in economic development in India.
- To identify the loopholes in stock market and suggest a suitable course of action to avoid them.

COMPONENTS OF THE CAPITAL MARKET

The focus of the capital market is the investor. The other components of the market which include the government, regulators, issuers, exchanges and various types of intermediaries, all of whom work for the investor. Some of the market components work as regulators, some as mediators, some as issuers and some as investors. These are:

REGULATORS	Ministry of Corporate Affairs (MCA), Ministry of Finance (Stock Exchange Division), Securities and Exchange Board of India (SEBI), Reserve Bank of India (RBI), and Stock Exchanges.
INTERMEDIARIES	Participants in the Indian capital market (SEBI- regulated): • Stockbrokers, sub-brokers, share transfer agents, bankers to an issue, trustees, registrars to an issue, merchant bankers, underwriters, portfolio managers, investment advisers, and other such intermediaries; • Depositories, participants, custodians of securities, FIIs, credit rating agencies, and other such intermediaries
ISSUERS	Corporate (Primary & Secondary Market), venture capital funds and collective investment schemes, including mutual funds.
INVESTORS	These can be categorized as domestic and foreign investors, institutional and retail investors.

IMPORTANCE OF CAPITAL MARKETS

Since 2003, Indian capital markets have been receiving global attention, especially from sound investors, due to the improving macroeconomic fundamentals. The presence of a great pool of skilled labour and the rapid integration with the world economy increased India's global competitiveness. No wonder, the global ratings agencies Moody's and Fitch have awarded India with investment grade ratings, indicating comparatively lower sovereign risks.

The Securities and Exchange Board of India (SEBI), the regulatory authority for Indian securities market, was established in 1992 to protect investors and improve the microstructure of capital markets. In the same year, Controller of Capital Issues (CCI) was abolished, removing its administrative controls over the pricing of new equity issues. In less than a decade later, the Indian financial markets acknowledged the use of technology (National Stock Exchange started online trading in 2000), increasing the trading volumes by many folds and leading to the emergence of new financial instruments. With this, market activity experienced a sharp surge and rapid progress was made in further strengthening and streamlining risk management, market regulation, and supervision. Capital market plays an important role in mobilizing resources, and diverting them in productive channels. In this way, it facilitates and promotes the process of economic growth in the country. Various functions and significance of capital market are discussed below:

1. Allocation of Capital: One of the major economic benefits generated by development of the Capital Markets is improved allocation of capital. The prices of Equity and Debt respond immediately to change in market conditions and quickly embodied in current asset prices. The signal created by the price change encourages or discourages capital inflow to an industry/company.

2. Allocation of Risk: The other major economic benefit generated by development of the Capital Markets is improved allocation of Risk. Capital Markets facilitates investors to earn returns based on their risk taking ability. Investors invest in high-risk instruments either because they are less risk reluctant or because the new risk is unaffected or negatively correlated with other investments in the portfolio.

3. Mobilization of Savings: Capital Markets is a good channel to move idle savings to most productive units in the economy. In any economy savings are moved to borrowers through Capital Markets or through Banking Financial Corporations/ Non-Banking Financial Corporations. In the first case the transaction occurs through the exchange of securities. In case of common stock the transfer results in ownership and in case of debt there is a contractual obligation to pay interest rate and debt. The advantage of investing in Capital Markets is the price of the securities fluctuates in response to change in supply and demand and can be brought and sold to third parties. As a result, the investor usually has a good idea of what the securities are worth and can obtain liquid funds by selling the securities. On the other hand, in the second case the investor doesn't have claim over the ultimate beneficiary of the funds and the price of the claim doesn't fluctuate in response to shift in supply and demand.

4. Encouragement to Investment: The capital market facilitates lending to the businessmen and the government and thus encourages investment. It provides facilities through banks and nonbank financial institutions. Various financial assets, *e.g.,* shares, securities, bonds, etc., induce savers to lend to the government or invest in industry. With the development of financial institutions, capital becomes more mobile, interest rate falls and investment increases.

5. Policy Making: Capital Markets play an important role in improving policy framework of a country. This is because when policy makers embark on bad policies the equity and bond prices tend to fall. Capital markets anticipate the future prospects of a country thus they reduce politicians incentives to do things that provide short-term gains, but that brings long-term costs that will hurt the economy. The postponement of new GAAR proposal and Retrospective taxation amendments shows how Capital Markets impact policy making. After amendment of GAAR and Retrospective taxation amendments in budget year (2012) both FDI and FII inflows dropped and stock market fell down that led to fall in rupee value and credit rating by top rating agencies.

6. Setting up of SME Exchange: A substantial development in Indian Capital Markets have been coining by setting up of SME (Small and Medium Enterprises) exchange. The SME Exchange is a welcome move for the Small and Medium Scale Enterprises. In India BSE and NSE have created SME exchanges BSESME and EMERGE respectively. Setting up of SME platform by two leading Stock Exchanges, have opened opportunities for SMEs to raise funds from the market. It is an effective booster for Small and Medium Enterprises where raising of capital is a primary concern. Creating a trading platform for SMEs would enable the growth of SMEs (Small and Medium Enterprises) and thereby the growth of Economy.

7. Promotes Economic Growth: The capital market not only reflects the general condition of the economy, but also smoothens and accelerates the process of economic growth. Various institutions of the capital market, like nonbank financial intermediaries, allocate the resources rationally in accordance with the development needs of the country. The proper allocation of resources results in the expansion of trade and industry in both public and private sectors, thus promoting balanced economic growth in the country.

8. Stability in Security Prices: The capital market tends to stabilise the values of stocks and securities and reduce the fluctuations in the prices to the minimum. The process of stabilisation is facilitated by providing capital to the borrowers at a lower interest rate and reducing the speculative and unproductive activities.

9. Better Transparency: With the economic environment becoming more competitive and market-oriented, capital market has assumed a critical role. Indian capital market has undergone a sea change over the last three years. During the year, market continued to respond to increased demands for transparency, improvement in speed and efficiency of operations and sharp growth in activity levels.

10. Benefits to Investors: The credit market helps the investors, i.e., those who have funds to invest in long-term financial assets, in many ways:

(a) It brings together the buyers and sellers of securities and thus ensure the marketability of investments,

(b) By advertising security prices, the Stock Exchange enables the investors to keep track of their investments and channelize them into most profitable lines,

(c) It safeguards the interests of the investors by compensating them from the Stock Exchange Compensating Fund in the event of fraud and default.

Apart from the facts mentioned above, about the significance of Capital Markets, there is a vast amount of empirical data that supports the importance of Capital Markets facilitating economic growth. Below is the list of superior economic performance in five major respects in countries with good Capital Market environment.

- Higher productivity growth
- Higher real-wage growth
- Greater employment opportunities
- Greater macroeconomic stability
- Greater homeownership

TRENDS IN INDIAN CAPITAL MARKET

Performance of Primary Market: Primary market facilitates government as well corporate in raising capital to meet their requirements of capital expenditure and/or discharge of other obligation such as exit opportunity for venture capitalist/ Private Equity firm. The most common primary mechanism for raising capital is an Initial Public Offer (IPO), under which shares are offered to common public as a precursor to the trading in secondary market of an exchange. When securities are exclusively offered to the existing shareholders of company, as opposed to the general public it is called Rights Issue. Following (table 1) shows the mobilization of resources through primary market.

Table 1: Sector-wise Resource Mobilisation

Sector	2012-13		2013-14		Percentage share in total amount	
	No.of issues	Amount (₹ crore)	No.of issues	Amount (₹ crore)	2012-13	2013-14
1	2	3	4	5	6	7
Private	55	17,690	70	11,681	54.5	21.0
Public	14	14,765	20	43,970	45.5	79.0
Total	**69**	**32,455**	**90**	**55,652**	**100.0**	**100.0**

Source: SEBI Report 2014

Increase In Listed Companies: There has been a significant change in listed companies in the stock market. The number of listed companies at NSE and BSE continued to rise during the period from 2011-2012 to 2013-2014 as shown in Table 2.

Table 2: No. of Listed Companies

Year	NSE	BSE
	No. of Companies Listed	No. of Companies Listed
2011-12	1,646	5,133
2012-13	1,666	5,211
2013-14	1,688	5,336

Source: SEBI Report 2014

Turnover in Indian Stock Market: The trading volumes picked up in 2013-14 consistent with the uptrend witnessed in the current year. The turnover of all stock exchanges in the cash segment increased by 2.4 percent to 33,41,416 crore in 2013-14 from 32,61,701 crore in 2012-13 (Table 3). BSE and NSE together contributed 99.7 percent of the turnover, of which NSE accounted for 84.1 percent in the total turnover in cash market whereas BSE accounted for 15.6 percent of the total turnover.

Table 3: Turnover at BSE and NSE: Cash Segment

Year / Month	BSE		NSE	
	Turnover (₹ crore)	Percentage Variation	Turnover (₹ crore)	Percentage Variation
1	2	3	4	5
2008-09	11,00,074	-30.3	27,52,023	-22.5
2009-10	13,78,809	25.3	41,38,023	50.4
2010-11	11,05,027	-19.9	35,77,410	-13.5
2011-12	6,67,498	-39.6	28,10,893	-21.4
2012-13	5,48,774	-17.8	27,08,279	-3.7
2013-14	5,21,664	-4.9	28,08,488	3.7

Source: SEBI Report 2014

Trends in Market Capitalisation: Market capitalisation figures are reflective of the expanding stock market activities. The market capitalisation of BSE has been higher than that of NSE in India reflecting large number of shares being listed in BSE. The market capitalisation of BSE rose by 16.1 percent to 74,15,296 crore in 2013-14 from 63,87,887 crore in 2012-13 (Table 4). On the other hand, at NSE market capitalisation increased by 16.6 percent to 72,77,720 crore in 2013-14 from 62,39,035 crore in 2012-13 (Table5).

Table 4: Market Capitalisation at BSE

Year/ Month	All Listed Companies	Percentage Variation
1	2	3
2008-09	30,86,075	-39.9
2009-10	61,65,619	99.8
2010-11	68,39,084	10.9
2011-12	62,14,941	-9.1
2012-13	63,87,887	2.8
2013-14	74,15,296	16.1

Source: BSE

Table 5: Market Capitalisation at NSE

Year/ Month	All listed Companies	Percentage Variation
1	2	3
2008-09	28,96,194	-40.4
2009-10	60,09,173	107.5
2010-11	67,02,616	11.5
2011-12	60,96,518	-9
2012-13	62,39,035	2.3
2013-14	72,77,720	16.6

Source: NSE

LOOPHOLES IN INDIAN STOCK MARKET

Almost every successful stock trader has learned ethical ways of how to hack the stock market. Not hack the stock market in illegal terms, but finding ethical ways to take advantage of certain stock loopholes. Taking advantage of market loopholes is one of the most common traits among the high achievers in trading stock. However, if you don't do it properly you may find yourself frustrated with your lack of results. Here It is discussed with you the most common mistakes stock traders make when learning how to use market loopholes to their advantage.

1. **They don't properly prime themselves on the trading market:** There is a wide range of stock traders, ranging from beginner to intermediate, to advance. Learning how to hack the stock

market, novices must learn the real truth of the market rather than academic fluff. The real truth as in other forces that influence the price of a stock. While advanced traders may need to rethink what they think they know.

2. They don't look for loopholes: Think of loopholes as a flaw in the system that is not caused by natural market forces that very occasionally pushed the price of a specific stock lower or higher. For example, it could be a group of traders acting from emotions or certain news that came out in the media, etc.

3. They don't calculate a fair price per share: It is critical to know how to value any share of stock. Most investors are very bad in valuing stocks and tend to buy stocks overpriced. To get the most return on investment when learning how to hack the stock market you must learn to buy stocks at a bargain. Most importantly, learning the criteria of picking a bargain stock

4. They don't follow a proven system for plan: When you know how to hack the stock market, you will not achieve maximum success until you formulate a system or plan that put it all together. A plan that includes, But not limited to, when to sale, when to buy, stop loss positions, triggers and most importantly what to buy. A trader can run into many mistakes that cause him/her to lose money. If you do not want to find yourself frustrated with your lack of results, learn from the four common mistakes mentioned above.

CONCLUSION

The Capital Markets play a significant role in any economy from allocation of Capital and Risk to Policy Making. If there is any single factor that makes a huge impact in improving the GDP of a country, it is the effective allocation of capital to the Industry and Government. Capital Market is the best channel to route the savings into long-term productive use. If we look in to the economy and find the enterprises that were hit by high cost of capital, one can observe that MSME that provides highest number of employment opportunities were worst hit by it. If a country develops and adopts best Capital Market practices they create multiple effects and helps in reviving the economy. The SME Exchange is a welcome move for the Small and Medium Scale Enterprises, but it is alone not enough to revive MSME. Capital market is the heart of any economy through which the savings are channelized into effective long-term investments. A developed and vibrant Capital Market will immensely contribute towards speedy economic growth and development.

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