Indian Money, Capital, and Stock Markets and Their Important Segments

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ABSTRACT

"*Money is indeed the most important thing in the world, and all the sound and fruitful personal and national morality should have this fact for its basis*." George Bernard Shaw

In modern times we cannot imagine the world without the use of money. Money is the lifeblood of the present-day world, and all our economic activities are carried out through the use of money. For conducting business, we need resources, and one can buy resources only with the help of money. This shows us that money is an integral part of any economy. According to Bhalla, V.K., (2006), the financial markets in India fall under the categories of money markets, capital markets, and stock markets. This paper explores the nature of these markets in India and examines their societal importance.

(Keywords: India, national economy, money market, capital market, stock market)

INTRODUCTION

Money, Capital, and Stock Markets

The money market is tapped to raise short-term finance. The long-term funds markets are based on demand for and supply of long-term funds.

The capital market refers to all the facilities and the institutional arrangement for the borrowing and loaning of funds. In the capital market, the "demand" for funds comes from productive sectors, (i.e., agriculture, industry, trade, and Government). The "Supply" of funds comes from household savings, corporate savings, institutional investors, and the surpluses of the government entities.

The stock market is a market in which people trade financial securities, commodities, and value at low transaction costs and at prices that reflect supply and demand. Securities include stocks and bonds.

In this way, the savings of both individuals and the business sector are tapped to meet the requirements for funds by the industrial and commercial enterprises, the public institutions, and other statutory bodies. Thus, 'Capital Market' is the bloodline of economic growth.

For healthy economic growth, a vibrant capital market is essential. With the current state of liberalization, globalization, and opening up of the financial sector, the role of the capital market as a liaison between savings and entrepreneurship is laudable. (L.C. Gupta, 1992). According to V.K. Bhalla (2006), the importance of Capital Market can be summed up as:

1. A growing capital market helps to deploy the community's savings for productive investment.

2. The capital market offers the household sector to financials its savings by providing a memo to financial assets with varying degrees of risk, return liquidity and maturity.

3. The resources so mobilized will be channeled to the two deficit factors of the economy, namely the Public Sector and the Private Corporate Sector.

4. Through this financial intermediation process, the capital market.

    a. helps efficient use of primary factors of production.

    b. resulting in technological up-gradation.

    c. It is further resulting in improved productivity of the economy's investment.

5. The capital market performs a dynamic function by disseminating information regarding present expectations about future economic prospects.

6. One of the essential duties of the capital market is the creation of liquidity.

Were it not for the capital market, most of the capital market instruments would have been illiquid, thereby choking the investment process. Therefore, the healthy and orderly development of this market is of crucial importance for sustaining a high rate of investment, faster growth of output, and increasing employment in the economy, especially in the industrial sector (Jawaharlal, 1992).

Shah and Thomas (2003) review the changes which are in place in India's equity and debt markets in the decade of the 1990s. That is with a focus on the importance of crises as for obtaining the reforms. The simple meaning is that any future improvements are based on addressing the present crisis.

According to Jawaharlal (1992), during the last eight decades of the 20th century, the capital market has been playing a dynamic and constructive role in financing industrial development. It also witnessed a vibrant virtual quantum jump in the resources raised by both private and public sectors for financing new projects as well as for expansion, modernization, and diversification. According to the Centre for Monitoring the Indian Economy (CMIE) during the three months, April to June, or 1996, the mobilization of funds in the primary market amounted to Rs. Three thousand six hundred forty-nine crores (US equivalency exchange rate date Oct 14, 2017, is $564,135,400 USD), and during June 1996 alone, the average daily turnover of BSE and NSE were Rs. 588 crores and Rs. 1492 crores, respectively.

According to Jawaharlal (1992), the critical fundamental factors for distinct buoyancy in the Indian Stock Market have been the widening of an industrial base, diversity of financial instruments, and growing awareness of the household sector of financial assets for the channelization of savings. The Indian capital markets, both primary and secondary, have witnessed sustained buoyancy.

Equity Markets

Because of investments, the equity market is one of the essential segments of financial markets (Bhalla, 2006). This market helps the companies to raise long-term funds. That facilitates capital formation in the country.

All the existing studies in India found that the equity return has a significant positive impact on the FII (Agarwal, 1997; Chakrabarti, 2001; and Trivedi & Nair, 2003). In India, under the company law provisions, companies are allowed to issue both equity and preference shares. The issue of equity shares helps the companies to have the permanent source of funds unless it decides to purchase these shares and return money to the shareholders. As far as preference shares are concerned, the companies in India cannot issue irredeemable preference shares. They are allowed to issue preference shares for a maximum period of 20 years. The companies subject to legal provisions are free to issue shares at par value, premium, or discount.

This market is having the composition of the primary and secondary markets. The primary market is more about an issue of new shares. That is also known as a new issue market. While raising funds from the primary market, the companies must ensure the lower rising of funds cost. They also require disclosing all the information in the offer document. The secondary market is also critical as it provides liquidity for the existing securities. For support on the primary market, the secondary market needs to be :

i) active,

ii) disclose all information,

iii) less volatile and efficient regarding lowering transaction costs.

Both primary and secondary markets have a link with each other. If the secondary market is active and vibrant, then the primary market is also likely to be dynamic and energetic. The equity market is under deregulation now in India, and hence, the single companies are free to decide about the premium. In case of a public issue of shares in the primary market, it is mandatory to appoint a registered merchant banker to act as a lead manager. Therefore, new equity shares are under management with the help of a merchant banker. The unlisted shares can have an issue with the private placement.

As discussed earlier, the secondary market for equity is nothing but a stock exchange that provides liquidity and price discovery. At present, there are 21 stock exchanges in India. Of these, the Bombay Stock Exchange (BSE) Ltd. and National Stock Exchange (NSE) Ltd. are the largest and most significant stock exchanges in India. The shares are in a dematerialized form (Demat form). This market is much more volatile.

The above discussion presents a deep understanding of the Indian stock market to all the readers (Kuvalekar, 2015).

Segments of the Capital Market

The Capital Market has mainly two sections, namely:

1. Primary Market (New Issue Market), and

2. Secondary Market (Stock Market).

In the primary market, new issues may be made mainly in two ways, namely, public issues and the right issues. The public issue involves the sale of securities to residents where a rights issue consists of a sale of securities to the existing shareholders/debenture holders.

In the primary market, equity shares, fully convertible debentures, partially convertible debentures, and non-convertible debentures, bonds, are the securities commonly issued by public limited companies. At this juncture, it is to be used to be abreast with the main features of some securities prevailing in the capital market like equity shares, preference shares/debentures (Gupta, 2001).

Equity shares are also known as "Ordinary Shares." Equity shares are the chief cornerstone of the financial structure of a company, without which the company cannot come into existence. According to V.K. Bhalla (2006) holders of equity shares are the real owners of an enterprise because it is the shareholders who provide its "risk" capital. The holders of equity shares are the residual owners who have the unrestricted claim on income and assets, who possess all the voting powers in the company. They are also entitled to purchase additional equity shares (such an issue is called the" rights" issue).

Equity shares are the most popular form of raising funds because the firm gets a significant amount of funds without any obligation and also due to the more considerable amount of flexibility it provides to the enterprise. Thus, equity shares do not carry any preferential right concerning dividend and repayment of capital. The bonus on such shares is available only when profits are with a balance after paying the dividend on preference shares. (Bhalla, 2006).

According to Jawharlal (1992), preference shares refer to that kind of security, which is accorded preferential treatment over equity shares in respect of the distribution of earnings and assets of the firm except that preference shares do not carry voting rights. The preference shares are redeemable within ten years of the issue. Preference shares usually take dividends at a fixed rate. Preference shares can be convertible into equity shares and non-convertible.

A debenture is an acknowledgment of a debt under the seal of the company. Unlike equity and preference shares, debentures represent creditorship securities, which bring in loan capital for an extended period where after, the same borrowing company has to repay. Further, the debenture holders have a priority claim for income over stockholders and have legal recourse for enforcing their rights. They do not have the controlling power. Debentures can be convertible (wholly or partly) and non-convertible. Recently debentures are also being issued with or without detachable warrants. Such warrants have a conversion option into equity shares at a later date.

The scholar Shirai (2004) examines the impact of financial and capital market reforms on corporate finance in India. The study concluded that India's economic and capital market reforms since the early 1990s had a positive impact on both the banking and capital market sectors. The financial markets remain shallow, particularly with differentiating high-quality firms from low-quality ones. The importance of the above discussion is to show how an Indian stock market works in real conditions.

ISSUE OF SECURITY IN THE PRIMARY MARKET

As discussed by Bhalla (2006), in the primary market, issues are made either "at par" or" at the premium." Pricing for the new issues is governed by regulations under the guidelines on capital issues or what is also known as guidelines for disclosure and investor protection published by the Securities and Exchange Board of India (SEBI).

Companies entering the capital market are required to advertise in the newspapers announcing the proposed issue. Further, Bhalla (2006) stated that apart from announcements, companies also place advertisements in the press/ television/radio, in support of the public issue. There is a practice to distribute prospectus, application forms, and other literature regarding new issues among the investing public. Thus, information about new issues may be obtained by investors from the different sources viz newspaper, television, mail, stock exchange members, brokers and sub-brokers, investment advisory firms, friends, and colleagues.

Chakrabarti and Mohanty (2005) discuss how the capital market in India is in operation in the reform period. The authors further explained how the capital market operations are improving with the implementation of reforms for the welfare of small investors.

SECONDARY MARKET OPERATIONS

The secondary market differs from the primary market in a fundamental sense. In the secondary market, the outstanding issues (second-hand securities) of existing companies are having trade-in, and the investors exchange their holdings with other investors for liquidity (Gupta, 2001). Thus, the secondary market is primarily aimed to liquefy the investments made in the primary market and thereby perform a complementary role. Therefore, investors seeking both profitability and liquidity need both elementary and secondary markets. In the secondary market, the stock exchanges provide for the trading mechanism for the existing securities, thereby providing the underlying liquidity.

The listing of securities is of utmost importance for trade in the stock exchange. The stock market is an essential pillar of the private sector's corporate economy. According to V.K. Bhalla (2006), stock market discharges three primary functions in the process of capital formation and in raising resources for the corporate sectors:

1. It provides a marketplace for the purchase and sale of securities

2. It provides the linkage between the savings in the housing sector and the investment in the corporate economy, and

3. By providing a market quotation of prices of securities- a sort of collective judgment simultaneously reached by many buyers and sellers in the market. The stock exchange serves the role of a barometer, not only the state of health of individual companies but also of the nation's economy as a whole.

INVESTMENT DECISION MAKING

Kumar and Chandra (2000) concluded that individual small investors often invest in securities based on a rough rule of thumb, this means that they spend blindly without doing any research strictly in tune with market conditions. According to Kabra, Mishra, and Dash (2010), the growth and future of the capital market in any country is dependent upon the quality of investment decisions that the investors make. However, investment decision making is a difficult task, as all investments are risky.

In the research of Hong and Stein (2007), prices and returns are tightly correlated to movements in volume, and higher volume is more likely to accompany higher price levels. Investments in shares the assessment of prospective performance on invested amount, timing, and uncertainty are the ultimate object of analysis of the investors. This means that the prospective return on the invested amount is dependent on many factors. ‘Understanding investors' decision-making process implies understanding how they make an assessment and how they might change in response to inputs from the financial reports and other sources (Grewal, and Grewal, 1992).

Thus, according to Gupta, Gupta, and Jain (2001), the investment decisions are by the availability of resources and information about the economy, industry, company, and the share prices ruling and expectations of the market and the companies under consideration. In simple words, investment decision refers to deciding between the buying and selling of securities. There are two aspects involved: (i) What to buy and (ii) when to buy/to be sold later.

The first aspect is the subject matter of "Fundamental analysis," and the second one is the "Technical analysis”. Bharti (2006) and Baker and Wurgler (2007) argue the importance of investor sentiment, and volume can be a proxy for it. This means that investor's emotions are of utmost importance for generating a high volume of transactions in the stock market. Bettman, Sault, and Schultz (2008) propose an equity valuation model is integrating fundamental and technical analysis; they tend to recognize their potential as complements rather than as substitutes. This shows that the fundamental and technical analyses are complementary and not as a substitute.

The fundamental analysis approach, which is vital to the discussion because it suggests that every stock has an intrinsic value. By comparing it with the current market price of the stock, one can find out whether the market price is fair, underpriced, or overpriced, from the analysis, buy or sell decisions can arrive.

According to Bettman, Salut, and Schultz (2009), the fundamental analysis consists of the following three steps:

(i) Economic Analysis: It involves the examination of various economic factors. The analysis of the state of the economy at the macro level incorporates how the economy has performed in the past, how it is performing at present, and how it is expected to play in the future.

(ii) Industry Analysis: The investor has to find out what is the status of the industry, as he would like to pick up the company in a growth industry.

(iii) Company Analysis: It envisages analysis forecasting of Earning per Share (EPS), evaluation of the management of the company, and so on.

The Technical Analysis approach has the assumption that the price of a stock depends on supply and demand in the marketplace and has little relationship with its intrinsic value. All financial data and market information of a given security is having a reflection in the market price of the security. Therefore, an attempt is made to charts to identify price movement patterns which predict the future circulation of the security, thus anticipating the appropriate timing to buy or sell a security. The main tools used in the technical analysis are the Dow Theory, the Elliot Wave Principle, and the Modern Indicator Theory.

Indian Capital Market Systems			
Government Securities	Industrial Securities Market	Development Financial Institutions	Financial Intermediaries
	New Issue Market	IFCI	Merchant Banks
	Old Issue Market	ICICI	Mutual Funds
		SFCs	Leasing Companies
		IDBI	Venture Capital Companies
		IIBI	Others
		UTI	

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