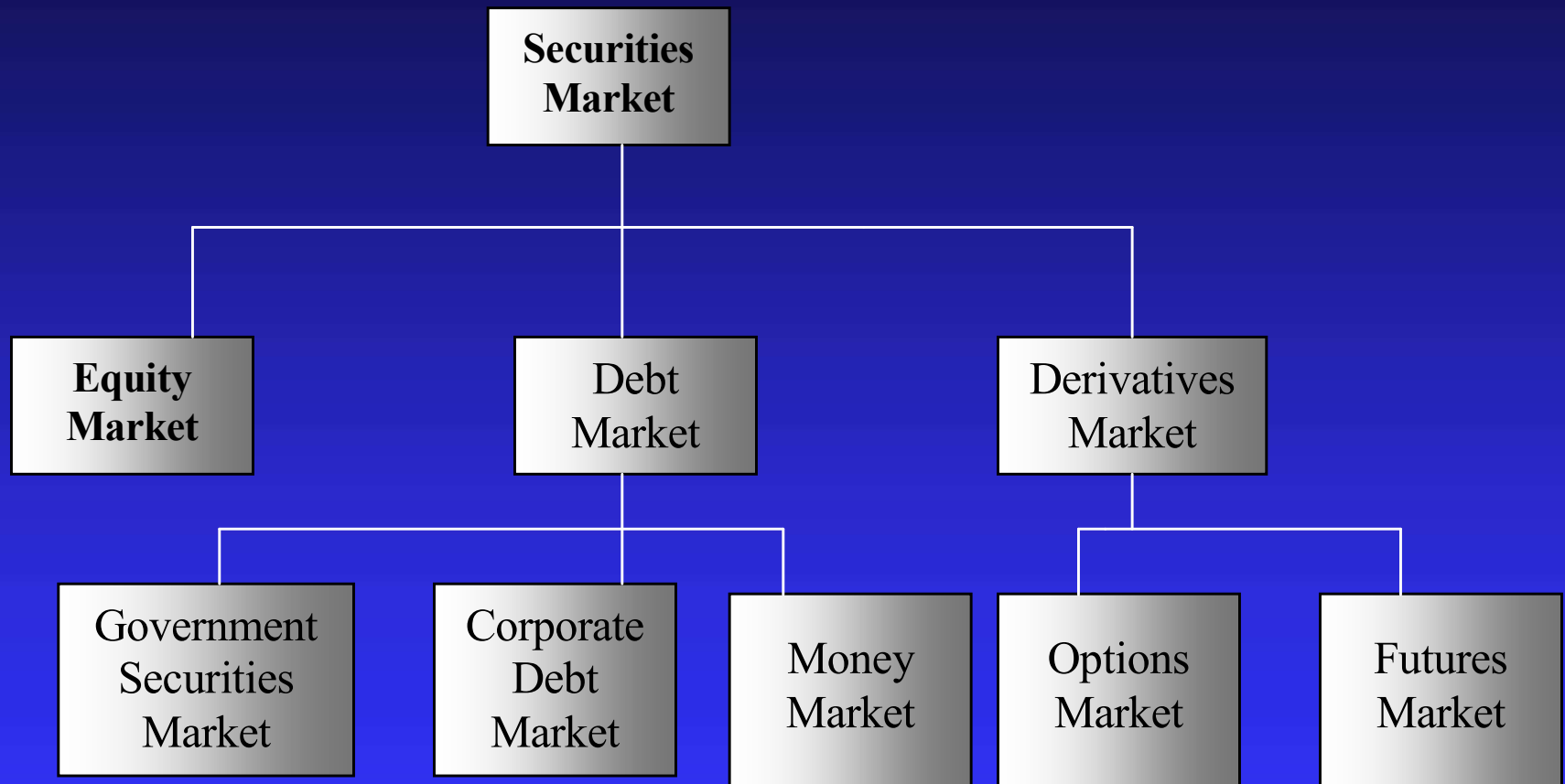


SECURITIES MARKET

The Battlefield

STRUCTURE OF THE SECURITIES MARKET



PARTICIPANTS IN THE SECURITIES MARKET

- **Regulators**
CLB, RBI, SEBI,
DEA, DCA
SEC, FRB
- **Stock Exchanges**
- **Listed Securities**
- **Depositories**
- **Brokers**
- **FII's**
- **Merchant Bankers or Investment Bankers**
- **Mutual Funds**
- **Custodians**
- **Registrars**
- **Underwriters**
- **Bankers to an issue**
- **Debenture trustees**
- **Venture capital funds.**
- **Credit rating agencies**

PRIMARY EQUITY MARKET

- PUBLIC ISSUE
- RIGHTS ISSUE
- PRIVATE PLACEMENT
- PREFERENTIAL ALLOTMENT

PUBLIC ISSUE IN INDIA

- Approval of the board of directors
- Approval of shareholders
- Appointment of the lead manager
- Due diligence by the lead manager
- Appointment of other intermediaries like co-managers, advisors, underwriters, bankers, brokers, and registrars
- Preparation of the draft prospectus
- Filing of the draft prospectus with SEBI
- Application for listing in stock exchanges
- Filing of the prospectus (after any modifications suggested by SEBI) with the Registrar of Companies
- Promotion of the issue
- Printing and distribution of applications
- Statutory announcement
- Collection of applications
- Processing of applications
- Determination of the liability of underwriters
- Finalisation of allotment
- Giving of demat credit (or dispatch of share certificates) and refund orders
- Listing of the issue

PUBLIC ISSUES IN THE U.S

In the U.S., public offerings of both stocks and bonds are typically marketed by investment bankers who perform the role of underwriters. Generally, the lead investment banker forms an underwriting syndicate with other investment bankers to share the responsibility of the issue.

BOOK BUILDING

Book building is a method of offering shares to investors in which the issue price is not fixed in advance (as is done in a fixed price offer) but is determined through a bidding process.

STOCK MARKET IN INDIA

- **As of January 2005 there were 23 stock exchanges recognised by the central government.**
- **The most important development in the Indian stock market was the establishment of the National Stock Exchange (NSE) in 1994.**
- **Within a short period it emerged as the largest stock exchange surging ahead of the Bombay Stock Exchange (BSE)**

NATIONAL STOCK EXCHANGE (NSE)

- **The NSE is a ringless, national, computerised exchange.**
- **The NSE has two segments: The Capital Market Segment and the Wholesale Debt Market Segment.**
- **Trading members in the Capital Market Segment are through VSATs. The trading members in the Wholesale Debt Market are linked through leased lines.**
- **The NSE has opted for an order-driven system.**
- **All trades on NSE are guaranteed by the National Securities Clearing Corporation.**

BOMBAY STOCK EXCHANGE (BSE)

- **The BSE switched from the open outcry system to the screen-based system in 1995.**
- **Jobbers play an important role on the BSE. A jobber is a broker who offers a two-way quote or a bid-ask quote.**
- **Since both jobbers and brokers feed their orders, the BSE has adopted a ‘quote-driven’ system and an ‘order-driven’ system.**

SCREEN BASED SYSTEM

The kind of screen based system adopted in India is referred to as the open electronic order (ELOB) market system.

ELOB

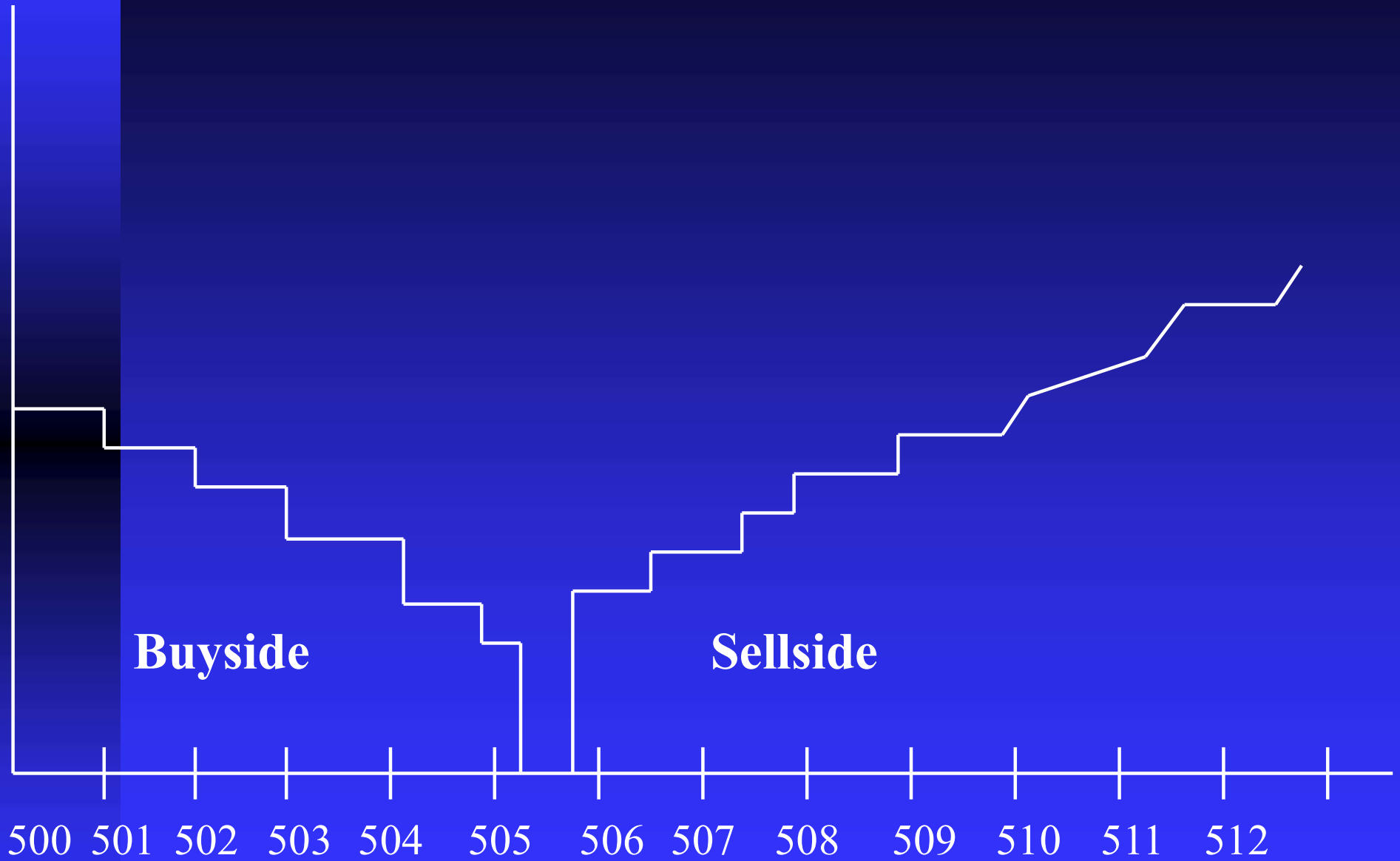
- Buyers and sellers place their orders on the computer

Limit order ... Market order

- Computer instantly tries to match mutually compatible orders on a price-time priority
- The limit order book, the list of unmatched limit orders is displayed on the screen

LIMIT ORDER BOOK

Shares



Buyside

Sellside

Limit Price

SETTLEMENT

- **Security transactions are settled through electronic delivery facilitated by depositories**
- **Presently, the settlement of all trades is a rolling settlement on a T+2 basis**

TRANSACTION COSTS

Thanks to the introduction of screen-based trading and electronic delivery transaction costs have fallen sharply in India.

	<i>MID - 1993</i>	<i>TODAY</i>
TRADING	3.75%	0.40%
BROKERAGE COST	3.00%	0.25%
MARKET IMPACT COST	0.75%	0.15%
CLEARING		
COUNTERPARTY RISK	PRESENT	ABSENT
SETTLEMENT	1.25%	0.10%
PAPERWORK COST	0.75%	0.10%
BADPAPER RISK	0.50%	0.00%
TOTAL	5.00% (+RISK)	0.50%

BUYING AND SELLING OF SHARES

- **Locating a Broker**
- **Placement of Order**
- **Execution of Order**
- **Internet Trading**

TYPES OF ORDER

- **Limit Order**

Those who place limit order

supply liquidity

- **Market Order**

Those who place market order

demand liquidity

INDIVIDUAL STOCK QUOTATIONS

Co., (Prev.Cl.), Open, High, Low, Close [Vol., Val. Rs'000s, Trades]	P/E	M Cap.	52-Wk H/L
Bajaj Auto (932.65), 937, 948, 931, 932.85 [46436, 43591.29, 1384]	12.7	(9438.6)	1200/692
(932.80), 940, 949, 931, 933.20 [138630, 130216.84, 4404]	12.7	(9438.6)	1200/692

STOCK MARKET INDICES

	INITIAL PRICE	FINAL PRICE	SHARES (MLN)	INITIAL VALUE OF OUTSTANDING STOCK	FINAL VALUE OF OUTSTANDING STOCK	PRICE RELATIVE
A	RS.25	RS.30	20	RS.500 M	RS.600 M	120
B	RS.100	90	1	RS.100 M	RS.90 M	90
	RS.125	RS.120		RS.600 M	RS.690 M	210

$$\text{PRICE WEIGHTED INDEX} = \text{RS.120} / \text{RS.125} \times 100 = 96$$

$$\text{VALUE WEIGHTED INDEX} = 690 / 600 \times 100 = 115$$

$$\text{EQUAL WEIGHTED INDEX} = 210 / 200 \times 100 = 105$$

SENSEX

The Bombay Stock Exchange Sensitive Index, popularly called the Sensex reflects the movement of 30 sensitive shares from specified and non-specified groups. The index for any trading day reflects the aggregate market value of the sample of 30 shares on that day in relation to the average market value of these shares in the base year 1978-79. This means that this is a value-weighted index. The base value is 100.

From September 1, 2003, Sensex is being constructed on the basis of free float market cap rather than full market cap.

NIFTY

The S&P CNX Nifty, popularly called Nifty, is arguably the most rigorously constructed stock market index in India. The Nifty reflects the price movement of 50 stocks selected on the basis of market cap and liquidity (impact cost). The base period for Nifty is the close of price on November 3, 1995. The base value of the index has been set at 1000. It is a value-weighted index. It is market-cap weighted

STOCK MARKET INDICES

AROUND THE WORLD

- **Dow Jones**
- **S & P 500**
- **Nikkei 225**
- **FTSE 100**

i – BEX

i – SEC BOND INDEX (i – BEX) is the most popular bond market index in India. There are two versions of i-BEX.

- **Total return index This tracks the total returns. It captures interest payment (accrued and actual) and capital gains/losses**
- **Principal return index This index reflects movements of net prices in the market, that is prices quoted in the market exclusive of accrued interest**

THRUST OF SEBI's REGULATION OF EQUITY MARKET

PRIMARY MARKET

ACCESS	: RESTRICTED
INSTRUMENTS	: MULTIPLIED
PRICING	: RELAXED
DISCLOSURE NORMS	: TIGHTENED
RESPONSIBILITY OF MERCHANT BANKERS	: ENHANCED
FOCUS INVESTORS	: SHIFTED ... INST'NAL
METHOD	: BOOK BUILDING

SECONDARY MARKET

TRADING	: COMPUTERISED
TRADING COSTS	: LOWERED
TRANSPARENCY	: ENHANCED
MARKETS	: INTEGRATED
GLOBALISATION	: ENCOURAGED
MANAGEMENT	: STRENGTHENED
SPECULATION	: HEIGHTENED
SETTLEMENT	: SHIFTED TO ELECTRONIC MODE

NEW YORK STOCK EXCHANGE

- **Trading through a system of brokers and specialists**
- **Brokers ... link ... investors ... market**
- **Specialists ... dual role**
 - a. Match buy and sell orders when the prevailing prices permit them to do so**
 - b. Buy and sell on their own account when they cannot match customer orders.**

NASDAQ

- **Unlike the NYSE, Nasdaq does not have a specific location.**
- **It is a fully computerized market consisting of many market makers competing on an electronic network of terminals rather than on the floor of the exchange**
- **Each Nasdaq company has a number of competing market makers, or dealers, who make a market in the stock.**
- **Dealers post their bid and ask prices on the Nasdaq system.**
Brokers choose among market makers to handle their trades

INTERNATIONAL STOCK EXCHANGE

- **Big bang 1986 ... amalgamation of all exchange in UK & Ireland**
- **Emergence of a single electronic market national market in UK and Ireland and the closure of regional exchanges**
- **Stock Exchange Automatic Quotation (SEAQ) System, a 'quote-driven' system**
- **Stock Exchange Automatic Execution Facility (SEAF) System, an 'order-driven' system**

TOKYO STOCK EXCHANGE

- The TSE divides stocks into two sections: First Section: 1200 most actively traded stocks. Second section: 400 less actively traded stocks.
- Trading in the larger stock of the First Section ... on the floor of the exchange
- Remaining stocks in the First Section and the Second Section are traded electronically
- The TSE relies on saitories who match orders but do not trade on their own
- A saitori maintains a public limit order book, matches market and limit orders, and slows down price movements when simple matching of orders would result in price changes greater than what is prescribed by the exchange.

SHOULD TRADING BE REGULATED?

KEYNES - TOBIN - BUFFETT

KEYNES ... 'INDUSTRY' ... 'FINANCE'

TOBIN ... TAX ON FINANCIAL TRANSACTIONS

BUFFETT .. A CARD

NOT PRACTICAL

1. RESTR'N OF FREEDOM
2. ADMINISTRATIVELY IMPRACTICAL
3. IMPAIRS .. PRICE DISCOVERY
4. SPECUL'N ... LIQUIDITY

SPECUL'N

LIQUID'Y

LOWER
COC

HIGHER
INVEST

GROWTH



GOVERNMENT SECURITIES MARKET

- **INTRODUCTION OF AUCTION-BASED PRICE DETERMINATION.**
- **DEVELOPMENT OF THE RBI'S YIELD CURVE FOR MARKING TO MARKET THE G-SECS PORTFOLIOS OF THE BANKS.**
- **INTRODUCTION OF THE SYSTEM OF PRIMARY DEALERS.**
- **CREATION OF WHOLESALE DEBT MARKET SEGMENT ON THE NATIONAL STOCK EXCHANGE, THE FIRST FORMAL MECHANISM FOR THE TRADING OF G-SECS.**
- **INTRODUCTION OF DVP (DELIVERY VERSUS PAYMENT) FOR SETTLEMENT.**
- **INCREASE IN THE NUMBER OF PLAYERS IN THE G-SECS MARKET WITH THE FACILITY FOR NON-COMPETITIVE BIDDING IN AUCTIONS.**
- **ESTABLISHMENTS OF GILT-ORIENTED MUTUAL FUNDS.**
- **RE-EMERGENCE OF REPOS AS AN INSTRUMENT OF SHORT-TERM LIQUIDITY MANAGEMENT.**
- **PHENOMENAL GROWTH IN THE VOLUME OF SECONDARY MARKET TRANSACTIONS IN G-SECS.**
- **EMERGENCE OF SELF-REGULATING BODIES SUCH AS THE PRIMARY DEALERS ASSOCIATION OF INDIA (PDAI) AND FIXED INCOME AND MONEY MARKET DEALERS ASSOCIATION (FIMMDA).**

PRIMARY MARKET FOR GOVERNMENT SECURITIES (G-SECS)

- The issue of G-secs or Treasury securities is done by the Reserve Bank of India (RBI) which serves as the merchant banker to the central and state governments.
- The RBI announces the auction of G-secs through a press notification and invites bids from prospective investors.
- Two systems of treasury auctions are widely used all over the world: (a) French auction. (b) Dutch auction
- In a French auction (or discriminatory price auction), successful bidders pay the actual price (yield) they bid for
- In a Dutch auction successful bidders pay a uniform price which is usually the cut off price (yield)

PATICIPANTS IN THE G-SECS MARKET

- **Banks are the largest holders of G-secs. Other investors are insurance companies, provident funds, mutual funds, trusts, primary and satellite dealers.**
- **The RBI provides the facility of Subsidiary General Ledger (SGL) account to large banks and financial institutions so that they can hold their investment in G-secs and treasury bills in the electronic book entry form. These institutions can settle their trades in securities through DVP (delivery versus payment) mechanism.**
- **Primary dealers are important intermediaries in the G-secs market. They serve as underwriters in the primary market, act as market makers in the secondary market, and enable investors to access the SGL account.**

SECONDARY MARKET FOR G-SECS

- **As soon as they are issued G-secs are deemed to be listed and eligible for trading.**
- **The NSE has a wholesale Debt Market (WDM) for high value debt transactions.**
- **Two kinds of trades occur on the WDM : Repo trades and Non-repos trades.**
- **Despite the WDM, the wholesale market in G-secs is by and large a telephone market. After a deal is done, it is reported on the Negotiated Dealing System (NDS) of NSE**

CORPORATE DEBT MARKET PRIMARY MARKET

THE PROCESS OF ISSUE OF CORPORATE SECURITIES ISSUANCE INVOLVES THE FOLLOWING STEPS :

- **BOARD MEETING AND APPROVAL FOR ISSUE AT THE AGM**
- **CREDIT RATING OF THE ISSUE**
- **CREATION OF SECURITY FOR THE SAID BONDS/DEBENTURES THROUGH APPOINTMENT OF DEBENTURE TRUSTEES**
- **APPOINTMENT OF ADVISORS AND INVESTMENT BANKERS FOR ISSUE MANAGEMENT**
- **FINALISATION OF THE INITIAL TERMS OF ISSUE**
- **PREPARATION OF THE OFFER DOCUMENT (FOR PUBLIC ISSUE) AND INFORMATION MEMORANDUM (FOR PRIVATE PLACEMENT)**
- **SEBI APPROVAL OF OFFER DOCUMENT FOR PUBLIC ISSUE**
- **LISTING AGREEMENT WITH STOCK EXCHANGES**
- **OFFER THE ISSUE TO PROSPECTIVE INVESTORS AND/OR BOOK BUILDING**
- **ACCEPTANCE OF APPLICATION MONEY/ADVANCE DEPOSITS FOR THE ISSUE**
- **ALLOTMENT OF THE ISSUE**
- **ISSUE OF LETTERS OF ALLOTMENT AND CERTIFICATES/DEPOSITORY CONFIRMATION**
- **COLLECT FINAL AMOUNTS FROM INVESTORS**
- **REFUND EXCESS APPLICATION MONEY/INTEREST ON APPLICATION MONEY**

PRIVATE PLACEMENT

- **PRESENTLY CORPORATE DEBENTURES IN INDIA ... MOSTLY PLACED PRIVATELY**
- **MANAGED BY A LEAD ARRANGER WHO IS ALSO THE ADVISOR & INVESTMENT BANKER TO THE ISSUE**
- **BOOK BUILDING MECHANISM IS COMMONLY EMPLOYED**

MONEY MARKET

Money market is the market for short-term debt funds. It comprises of the call and notice money market, repo market, and the market for debt instruments such as treasury bills that have an original maturity of less than one year.

The money market does not exist in a specific physical location or follow a single set of rules or post a single set of prices. Rather, it represents a web of borrowers and lenders, linked by telephones and computers, dealing with short-term debt funds.

REPO MARKET

In a repo transaction two parties exchange securities and cash with a simultaneous agreement to reverse the transaction after a given period. Thus a repo represents a collateralised short-term lending transaction. The party which lends securities (or borrows cash) is said to be doing the repo and the party which lends cash (or borrows securities) is said to be doing a reverse repo.

TREASURY BILL MARKET

- **Treasury bills are short-term debt instruments of the central government.**
- **Treasury bills are sold through an auction process according to a calendar announced by RBI.**
- **Treasury bills are issued at a discount and redeemed at par.**
- **Most buyers of treasury bills hold them till maturity and hence the secondary market activity is limited**

SUMMING UP

- **The securities market is the market for equity, debt, and derivatives.**
- **Equity market has two segments, viz., the primary market and the secondary market.**
- **There are four ways in which a company may raise equity capital in the primary market: public issue, rights issue, private placement, and preferential allotment.**
- **The secondary market consists of the organised stock exchanges. The principal stock exchanges in India are the National Stock Exchange and the Bombay Stock Exchange.**
- **The key features of stock market transaction in India are screen-based trading, electronic delivery, and rolling settlement.**
- **The major stock exchanges around the world are the New York Stock Exchange, NASDAQ, International Stock Exchange, and Tokyo Stock Exchange.**
- **The general market movement is measured by stock market indices. Sensex and Nifty are the two most popular stock market indices in India.**

- **G-secs market is the largest segment of the debt market.**
- **G-secs are issued through an auction mechanism.**
- **Transactions in G-secs are settled through the delivery versus payment mode.**
- **The wholesale secondary market in G-secs is by and large a telephone market.**
- **Presently, corporate bonds (debentures) in India are mostly privately placed.**
- **The secondary market for corporate debt has been historically rather dull.**
- **The money market is the market for short-term funds. It comprises of the call and notice money market, repo market, and the market for debt instruments such as treasury bills that have an original maturity of less than one year.**