

Capital Market: Structure and Emerging Trends

Part-3

Topic: Stock Exchange in India

1.6 Concept of Stock Exchange

A stock exchange is a place where securities, shares, bonds and other financial instruments are listed and bought and sold by traders or brokers. To be able to trade on a stock exchange, securities must be listed on it. Stock exchanges help companies to raise funds. Therefore the company needs to list themselves in the stock exchange.

The Securities Contracts (Regulation) Act, 1956, has defined Stock Exchange as an "association, organization or body of individuals, whether incorporated or not, established for the purpose of assisting, regulating and controlling business of buying, selling and dealing in Securities". The securities include:

- (i) Shares, scrip, stocks, bonds, debentures stock or other marketable securities of a like nature in or of any incorporated company or other body corporate;
- (ii) Government securities; and
- (iii) Rights or interest in securities.

Thus, Stock exchange as an organized security market provides marketability and price continuity for shares and helps in a fair evaluation of securities in terms of their intrinsic worth. It also helps orderly flow and distribution of savings between different types of investments. This institution performs an important part in the economic life of a country, acting as a free market for securities where prices are determined by the forces of supply and demand. Apart from the above basic function, it too assists in mobilizing funds for the Government and the Industry and to supply a channel for the investment of savings in the performance of its functions.

The Stock Exchanges in India as elsewhere have a vital role to play in the development of the country in general and industrial growth of companies in the private sector in particular and helps the Government to raise internal resources for the implementation of various development programmes in the public sector. As a segment of the capital market, it performs an important function in mobilizing and channelizing resources which remain otherwise scattered. Thus, the Stock Exchanges tap the new resources and stimulate a broad based investment in the capital structure of industries.

A well developed and healthy stock exchange can be and should be an important institution in building up a property base along with a socialist in India with broader distribution of wealth and income. Thus, Stock Exchange is a vital organ in a modern society. Without a stock exchange a modern democratic economy cannot exist. The system of joint stock companies financed through the public investment as emerged has put the vast means of finances almost to entrepreneurs' needs.

1.7 Functions of Stock Exchange

Some of the significant objectives or functions of the Stock Exchange are listed below:

1. **Economic Barometer:** A stock exchange is a solid barometer to gauge the economic circumstance of a country. A stock exchange is also known as a pulse of the economy or economic mirror which reflects the economic conditions of a country.
2. **Pricing of Securities:** The stock market helps to assess the securities on the basis of demand and supply factors. The securities of effective and growth-oriented organisations are estimated higher as there is more demand for such securities.
3. **Safety of Transactions:** In the stock market only the indexed securities are traded and stock exchange authorities include the corporations named in the trade list only after verifying the soundness of the organisation. The organisations which are listed also have to function within the stringent rules and regulations. This guarantees the security of dealing through the stock exchange.
4. **Contributes to Economic Growth:** In stock exchange securities of various organisations are traded. This method of disinvestment and reinvestment helps to invest in the most productive investment proposal and this leads to capital structure and economic growth.
5. **Spreading of Equity Cult:** Stock exchange urges people to invest in ownership securities by managing new issues, better trading practices and by educating the people about investment.
6. **Providing Scope for Speculation:** To assure liquidity and demand of supply of securities the stock exchange allows healthy consideration of securities.
7. **Liquidity:** The principal purpose of the stock market is to present a ready market for sale and purchase of securities. The presence of the stock exchange market gives certainty to investors that their investment can be transformed into cash whenever they want.

8. **Better Allocation of Capital:** The shares of profit-making organisations are valued at higher prices and are actively traded so such organisations can efficiently raise capital from the stock market.
9. **Promotes the Habits of Savings and Investment:** The stock market gives attractive chances for investment in different securities. These attractive opportunities inspire people to save more and invest in securities of the corporate sector rather than investing in unfruitful assets such as gold, silver, etc.,

1.8 Features of Stock Exchange:

- **A market for securities-** It is a wholesome market where securities of government, corporate companies, semi-government companies are bought and sold.
- **Second-hand securities-** It associates with bonds, shares that have already been announced by the company once previously.
- **Regulate trade in securities-** The exchange does not sell and buy bonds and shares on its own account. The broker or exchange members do the trade on the company's behalf.
- **Dealings only in registered securities-** Only listed securities recorded in the exchange office can be traded.
- **Transaction-** Only through authorised brokers and members the transaction for securities can be made.
- **Recognition-** It requires to be recognized by the central government.
- **Measuring device-** It develops and indicates the growth and security of a business in the index of a stock exchange.
- **Operates as per rules–** All the security dealings at the stock exchange are controlled by exchange rules and regulations and SEBI guidelines.

1.9 POWERS THAT MAY BE EXERCISED BY THE STOCK EXCHANGE

As per SCRA Act any recognized stock exchange may, subject to the previous approval of the Securities and Exchange Board of India (SEBI) make bye-laws for the regulation and control of contracts. The bye-laws can provide for the exercise of following powers by the stock exchange:

- a. The opening and closing of markets and the regulation of the hours of trade;
- b. Set up a clearing house for the periodical settlement of contracts and differences there under, the delivery of and payment for securities, the

- passing on of delivery orders and the regulation and maintenance of such clearing house;
- c. The fixing, altering or postponing of days for settlements;
 - d. The determination and declaration of market rates, including the opening, closing, highest and lowest rates for securities;
 - e. The terms, conditions and incidents of contracts, including the prescription of margin requirements, if any, and conditions relating there to, and the forms of contracts in writing;
 - f. The regulation of the entering into, making, performance, rescission and termination, of contracts, including contracts between members or between a member and his constituent or between a member and a person who is not a member, and the consequences of default or insolvency on the part of a seller or buyer or intermediary, the consequences of a breach or omission by a seller or buyer, and the responsibility of members who are not parties to such contracts;
 - g. The listing of securities on the stock exchange, the inclusion of any security for the purpose of dealings and the suspension or withdrawal of any such securities, and the suspension or prohibition of trading in any specified securities;
 - h. The method and procedure for the settlement of claims or disputes, including settlement by arbitration;
 - i. The levy and recovery of fees, fines and penalties.
 - j. The regulation of the course of business between parties to contracts in any capacity;

1.10 REGULATION OF BUSINESS IN THE STOCK EXCHANGES

Under the SEBI Act, 1992, the SEBI has been empowered to conduct inspection of stock exchanges. The SEBI has been inspecting the stock exchanges once every year since 1995-96. During these inspections, a review of the market operations, organizational structure and administrative control of the exchange is made to ascertain whether:

- The exchange provides a fair, equitable and growing market to investors,
- The exchange's organization, systems and practices are in accordance with the Securities Contracts (Regulation) Act (SC(R) Act), 1956 and rules framed there under,
- The exchange has implemented the directions, guidelines and instructions issued by the SEBI from time to time,

- The exchange has complied with the conditions, if any, imposed on it at the time of renewal/grant of its recognition under section 4 of the SC(R) Act, 1956.

From time to time inspection of stock exchanges was carried out with a special focus on the measures taken by the stock exchanges for investor's protection. Stock exchanges were, through inspection reports, advised to effectively follow-up and redress the investors' complaints against members/listed companies. The stock exchanges were also advised to expedite the disposal of arbitration cases within four months from the date of filing.