LESSON 12:
SECONDARY MARKET & ITS OPERATIONS

The market for long term securities like bonds, equity stocks and preferred stocks is divided into primary market and secondary market. The primary market deals with the new issues of securities. Outstanding securities are traded in the secondary market, which is commonly known as stock market predominately deal in the equity shares. Debt instruments like bonds and debentures are also traded in the stock market. Well regulated and active stock market promotes capital formation. Growth of the primary market depends on the secondary market. The health of the economy is reflected by the growth of the stock market.

History of Stock Exchanges in India
The origin of the stock exchanges in India can be traced back to the later half of 19th century. After the American Civil War (1860-61) due to the share mania of the public, the number of brokers dealings in shares increased. The brokers organised an informal association in Mumbai named “The Natic Stock and Share Brokers Association” in 1875.

Increased activity in trade and commerce during the First World War and Second War resulted in an increase in the stock trading. Stock exchanges were established indifferent centres like Chennai, Delhi, Nagpur, Kanpur, Hyderabad and Bangalore. The growth of stock exchanges suffered a set back after the end of World War. Worldwide depression affected them. Most of the stock exchanges in the early stages had a speculative nature of working without technical strength. Securities and Contract Regulation Act, 1956 gave powers to the central government to regulate the stock exchanges. The stock exchanges in Mumbai, Calcutta, Chennai, Ahmedabad, Delhi, Hyderabad and Indore were recognised by the SCR Act. The Bangalore stock exchange was recognised only in 1963. At present we have 33 stock exchanges and 21 of them had hardware and software compliant to solve Y2K problem.

Till recent past, floor trading took place in all the stock exchanges. In the floor trading system, the trade takes place through open outcry system during the official trading hours. Trading posts are assigned for different securities where buy and sell activities of securities took place. This system needs a face to face contact among the traders and restricts the trading volume. The speed of the new information reflected on the prices was rather slow. The deals were also not transparent and the system favoured the brokers rather than the investors.

The setting up of NSE and OTCEI with the screen based trading facility resulted in more and more stock exchanges turning towards the computer based trading. Bombay stock exchange introduced the screen based trading system in 1995, which is known as BOLT (Bombay On-line Trading System). Madras stock exchange introduced Automated Network Trading System (MANTRA) on Oct 7th 1996. Apart from Bombay stock exchange, Vadodara, Delhi, Pune, Bangalore, Calcutta and Ahmedabad stock exchanges have introduced screen based trading. Other exchanges are also planning to shift to the screen based trading. The turnover and market share of the various stock exchanges are given in Table 4.1.

Functions of Stock Exchange

Maintains Active Trading
Shares are traded on the stock exchanges, enabling the investors to buy and sell securities. The prices may vary from transaction to transaction. A continuous trading increases the liquidity or marketability of the shares traded on the stock exchanges.

Fixation of Prices
Price is determined by the transactions that flow from investors’ demand and supplier’s preferences. Usually the traded prices are made known to the public. This helps the investors to make better decisions.

Ensures Safe and Fair Dealing
The rules, regulations and by-laws of the stock exchanges’ provide a measure of safety to the investors. Transactions are conducted under competitive conditions enabling the investors to get a fair deal.

Aids in Finacing the Industry
A continuous market for shares provides a favorable climate for raising capital. The negotiability and transferability of the securities helps the companies to raise long-term funds. When it is easy to trade the securities, investors are willing to subscribe to the initial public offerings. This stimulates the capital formation.

Dissemination of Information
Stock exchanges provide information through their various publications. The publish the share prices traded on daily basis along with the volume traded. Directory of Corporate information is useful for the investors’ assessment regarding the corporate. Handouts, handbooks and pamphlets provide information regarding the functioning of the stock exchanges.

Performance Inducer
The prices of stock reflect the performance of the traded companies. This makes the corporate more concerned with its public image and tries to maintain good performance.

Self-regulating Organisation
The stock exchanges monitor the integrity of the members, brokers, listed companies and clients. Continuous internal audit safeguards the investors against unfair trade practices. It settles the disputes between member brokers, investors and brokers.

Regulatory Framework
A comprehensive legal framework was provided by the Securities Contract Regulation Act, 1956 and the Securities and Exchanges Board of India Act, 1992. A three tire regulatory structure comprising the Ministry of Finance, the Securities and Exchanges Board of India and the Governing Boards of the Stock Exchanges regulates the functioning of stock exchanges.
The names of the stock exchanges are given below

- Ahmedabad Stock Exchange
- Banglore Stock Exchange
- Bhubaneswar Stock Exchange
- Bombay Stock Exchange
- Calcutta Stock Exchange
- Cochin Stock Exchange
- Coimbatore Stock Exchange
- Delhi Stock Exchange
- Guwahati Stock Exchange
- Hyderabad Stock Exchange
- Indore Stock Exchange
- Jaipur Stock Exchange
- Kanpur Stock Exchange
- Ludhiana Stock Exchange
- Madras Stock Exchange
- Magadh Stock Exchange
- Managlore Stock Exchange
- Pune Stock Exchange
- Saurashtra Stock Exchange
- Vadodhara Stock Exchange
- N S E
- OTCEI
- Inter Connected Stock Exchange

Stock exchanges normally function between 10:00 a.m. and 3:45 p.m. on the working days. Badla sessions are held on Saturdays.

Member of the Stock Exchange

The Securities Contract Regulation Act of 1956 has provided uniform regulation for the admission of members in the stock exchanges. The qualifications for becoming a member of a recognised stock exchange are given below

The minimum age prescribed for the members is 21 years.

He/she should be an Indian Citizen.

He/she should not be a defaulter of any other stock exchange. He/she should not be engaged in any other business connected with the company.

The minimum required educational qualification is a pass in 12th examination.

The Mumbai and Calcutta stock exchanges have set up training institutes to enable the members to understand the complexities of the stock trading. In recent days highly qualified persons such as Company secretaries, Charted accountants and MBA’s are becoming members. Corporate membership is also permitted now. The members transacting business through their appointed members. The governing board has to approve the partnership and the appointed membership in other stock exchanges. If he applies before the completion of five years he has to relinquish the If membership of the present membership before accepting the other.

The Broker

A member/broker registered with the recognized stock exchange has to apply to the SEBI for registration. Likewise a
sub-broker even though he is registered with the stock exchange should apply to SEBI for registration. Usually the agreement between the broker and the sub broker is carried out on a non-judicial stamp paper of Rs 10. The agreement generally specifies the authority and responsibility of the broker and sub broker. The broker has to abide by the code of conduct laid down by the SEBI. The code of conduct prevents the malpractice, manipulation and gives other statutory requirements. If a broker is involved in manipulation or price rigging or gives false information, his registration is likely to be suspended. If the rules and regulations regarding insiders’ trading and take over codes are not adhered to, the registration may even be cancelled. The number of brokers in various exchanges is given in Table 4.2.

**Broker and the Investor**

1. The broker should provide adequate information regarding the stocks.
2. The broker should be capable of giving short term and long term investment suggestions to the investors.
3. The broker should be able to confirm the purchase and sale of the securities quickly.
4. He should be able to provide price quotes quickly, which is now possible with the computer network.
5. The broker should be noted for his integrity. He should have a good name in the society.
6. The broker should have adequate experience in the market to take correct decision.
7. The broker should have contact with other stock exchanges to execute the order profitably.
8. The broker should also offer incidental service like arranging for financing the clients’ transaction.

**Types of Orders**

Buy and sell orders are placed with the members of the stock exchanges by the investors. The orders are of different types.

**Limit Orders**

Orders are limited by a fixed price. ‘Buy Reliance Petroleum at Rs 50. Here, the order has clearly indicated the price at which it has to be bought and the investor is not willing to give more than Rs 50.

**Best Rate Order**

Here, the buyer or seller gives the freedom to the broker to execute the order at the best possible rate quoted on that particular date for buying. It may be the lowest rate for buying and the highest rate for selling.

**Discretionary Order**

The investor gives the range of price for purchase and sale. The broker can use his discretion to buy within the specified limit. Generally the approximate price is fixed. The order stands as this ‘Buy BRC 100 shares around Rs 40’.

**Stop Loss Order**

The orders are given to limit the loss due to unfavorable price movements in the market. A particular limit is given for waiting. If the price falls below the limit, the broker is authorised to sell the shares to prevent further loss. Ex. Sell BRC Ltd at Rs 25, stop loss at Rs 22.

**Buying and Selling Shares**

To buy and sell shares the investor has to locate a registered broker or sub broker who can render prompt and efficient service to him. Then orders to buy or sell the specified number of shares of a company of the investor’s choice are placed with the broker. The order may be of any of the above mentioned type. After receiving the order, the broker tries to execute the order in his computer terminal. Once matching order is found, the order is executed. The broker delivers the contract note to the investors. It gives details regarding: the name of the company, number of shares bought, price, brokerage, and date of delivery of shares. In the physical trading form, once the broker gets the share certificate through the clearing houses he delivers the share certificate along with transfer deed to the investor. The investor has to fill the transfer deed and stamp it. Stamp duty is one-half percentage of the purchase consideration, the investor should lodge the share certificate and transfer deed to the registrar or transfer agent of the company. If it is bought in the demat form, the broker has to give a matching instruction to his depository participant to transfer the share bought to the investors’ account. The investor should be an account holder in any of the depository participant. In the case of sale of shares on receiving payment from the purchasing broker, the broker effects the payment to the investor.

**Share Groups**

The listed shares are divided into three categories: Group A shares (specified shares) B1 shares and B shares. The last two groups are referred to cleared securities or no-specified shares. The shares that come under specified group can avail the carry forward transactions. In ‘A’ group, shares are selected on the basis of equity, market capitalisation and public holding. Further it should have a good track record and a dividend paying company. It should have good growth potential too. The trading volumes and the investors base are high in ‘A’ group share. Any company when it satisfies these criteria would be shifted from ‘B’ group to “A” group.

In the B1 group actively traded shares are included. Carry forward transactions are not allowed in this group. Settlement take place through the clearing house along with the “A” group shares. The settlement cycle and the procedure are identical to “A” group security. The rest of the company shares listed form the B group.

**Settlement Cycle**

A settlement cycle consists of five days trading period within which any transaction buy/ sell must be completed. There are two types of settlement: fixed and rolling. A fixed cycle starts on a particular day and ends after five days. For example, in the Mumbai stock exchange the settlement cycle starts on Monday and ends of Friday. In the NSE it starts on Wednesday of one week and ends on the Tuesday of the following week. A pay-in day and a pay-out day follow the settlement cycle. The pay-in day refers to all the buyer brokers depositing the money for the purchase of shares. The pay-out day refers to the exchange handing over the proceeds to the seller brokers.
A settlement cycle is important for the investors and brokers. If, an investor purchase 1000 shares of Asian Paints on Monday, to square up the position by the end of the settlement, the sale will have to take place before Friday, the same week. If the sale has not taken place, he has to pay the consideration for the broker at the end of the settlement period. The broker collects the payments from the clients and deposits it with the exchange on the pay-in day. The exchange allows four days, from the end of the settlement cycle to the pay-in day to enable the brokers to collect the payments from the clients. After found days, on the pay-out day the exchange hands over the proceeds to the seller broker.

The same trading/ settlement cycle and procedure of the specified group are followed in the “B1” non-specified group. But no carry forward (Badla) transaction is allowed for “B1” group shares. The pay-in for B1 group securities can be done with “A” group simultaneously under one balance sheet.

In the B group shares, clearing house handles the money and part of the transaction. Physical delivery of securities is done by the members. In the pay-in day the balance sheet is filed alongwith cheques/ drafts. Only on the payout day monetary are made by the clearinghouse.

Rolling Settlement
SEBI introduced rolling settlement from Jan 10, 2000. Ten stocks are selected for rolling settlement. They are BFL Software, Citicorp Securities, Cybertech Securities, Hitech D rilling, Lupin Laboratories, Mars Software, More pen labs, Sri Adhikari Brothers, Tata Infotech and Visuals Soft. SEBI has announced a list of 156 stocks which would be included in rolling settlement made by the first fortnight of May 2000.

In a rolling settlement of a T+5 period trades are settled five days from the date of transaction. If an investor purchase of 3000 shares of Tata Infotech and sells 2000 shares on Monday he would be asked to settle the net outstanding that is 1000 shares on the following Monday, the fifth or sixth day. This means all open positions on a trading day are settled on the fifth working day after the trading day. Already rolling settlement is adopted by institutional trade.

Price Filters
A normal rise or fall in the prices of the securities destroys the investors’ confidence and such price fluctuations can lead to high transaction risk. Brokers create instability in prices to earn quick profits. Broker’s interest in the stock is initially triggered by market rumours such as takeover, bonus issue, good or bad financial performance and management problems. If the rumours are positive, there would be a scramble for the company’s shares. This is done in anticipation of the increase in demand once the information becomes public. Prices can be increased by the traders through circular trading.

Circular trading refers to the trading that takes place among the brokers to manipulate the prices for their personal gain. For example, if there is a rumour about the issue of bonus share by a company, the traders enter into matching deals among themselves (that is buy and sell order) at a price higher than the prevailing market price. Market psychology is that when the price increases investors think that it will go up further and enter into the market. At this juncture, the traders exit booking profits from the transactions. The investors are caught unaware of the real situation. To prevent these happenings price filters are introduced.

Intra day Price Bands
Here the price range is fixed to restrict the price movement of a scrip during a trading session. For example take the case of TVS Suzuki scrip. Suppose, the stock closed on Monday at Rs. 500 at the NSE, it would be allowed to trade on Tuesday only in a 10% percent variation of Monday’s close. It would be allowed to trade between Rs. 450 and Rs. 550.

The intra day price band is laid by all the exchanges depending upon the price and volatility of the stock. At NSE the Nifty and Junior Nifty stocks’ have 10 per cent and other stocks have five per cent intra day price bands. In August 1997, BSE reduced the filter limit from 10 per cent to 5 per cent in 32 stocks because of the uncertain market conditions.

Price filter ensures that the stock is traded only within the given range. Transaction beyond the band are rejected by the system. For example if thereis an order to buy TVS Suzuki scrip at Rs. 555, the system will not accept the trade.

Limitations
The intra day price band does not allow for the proper reaction in prices for the given information. Consider the situation of the Thai currency crisis, it affected exports to that nation and in turn the share prices of some companies might have a retreat. However, the price band places an artificial check on the reaction of the price. If the price band has to be released, the NSE has to get special permission from the SEBI.

Secondly, the intra day price band does not curb the automatic price movements within a day. For example, the TVS Suzuki scrip may open on Tuesday at Rs. 470 and rise immediately to an intra day high of Rs. 535 and may finally close at Rs. 485. The sudden increase of Rs. 65 would increase the investment risk due to the heavy transactions that take place on BSE and NSE.

To smoothen the price volatility Madras stock exchange has introduced graded price filters. In MSE, intra day price band prevents an order being executed at Rs. 530 after being opened at Rs. 470. An intermediate price filter is applied at Rs. 468.80 (that is 4 per cent of Rs. 470). If there is no matching orders at this price, the stock price is frozen at this level for the day. If the matching is order is found, it would be allowed to rise further by another intermediate price filter level, say 6 percent. Such graded price filters effectively prevent the knee-jerk price movements.

Inter Week Price Band
Here the weekly price movements are controlled by applying a weekly price band. The range would be fixed for the weekly price movement. This range is fixed in accordance with the price volatility. The inter week price band is 25 per cent of the previous week’s close on Nifty and Junior Nifty stocks.

Margins
Margins are additional filters applied by the stock exchanges to curb the price volatility. For every transaction undertaken by the broker he has to deposit a margin amount to the stock exchange. The margin amount paid is used as a tool to discourage the speculative and circular trading. It can be made simple with an example, if the MSE were to impose a margin of 20 per cent, traders would have to deposit Rs. 20 with the
Margins are of different types
- Gross Exposure margin
- Net Exposure margin
- Mark to Market margin
- Concentration margin
- Special margin

**Gross Exposure Margin**
This margin limits the risk exposure of the trader by putting an upper limit to his transaction. This would prevent him from trading beyond his means and the default risk. In the NSE the gross exposure is up to 7 times of the traders base capital, with Rs. 1 lakh he can trade up to Rs. 7 lakh. If it crosses that limit, he has to either switch over his terminal or should bring the gross exposure within the limits or he can deposit additional margin with the exchange to increase the limit.

The enhanced limit would exist for three months. At the end of the period the broker has the choice to continue the present level or revert to the older level. The outstanding exposures at the end of the settlement cycle i.e. Wednesday to Tuesday at NSE and Monday to Friday at BSE, would be added to the first trading day of the next settlement period.

**Net Exposure Margin**
Here, the trader has to deposit margins at a graded basis if the purchase is greater than sales in any day. This is imposed to curtail the risk involved in heavy purchase of shares without matching sales. For example, if a trader buys one lakh shares of Reliance at Rs 185 and sells only 30,000 for the net outstanding position of 70,000 shares poses as threat. Hence, the trader has to deposit a margin for the net exposure. Ten per cent margin is for net exposures exces of the total purchase.

**Mark to Market Margin**
The gross and net exposure margins try to stabilise the high transaction volume. The risk arises not only through the volume transacted but also through the price volatility. The trader may be able to find a matching order only at a lower price. For example, if Reliance stock price falls from Rs 185/- at the end of the trading session, the exposure risk would be high for the trader.

In the mark to market margin the trader has to deposit a sum that would be a fixed percentage of the product of the difference between the closing selling and purchasing price and the outstanding net position at the end of the day. This would be 5% of the price difference on the scrips, which fluctuate by 5% in a day or 10% over a settlement period. This margin is not imposed on share with market value of Rs 50 or less. In our example the Reliance share price closes at Rs 180, the broker has to deposit Rs. 1,75000 = .5(185-180×70,000). If, the trader buys two stocks and if, one of the stock closed at Rs 5 higher and other Rs 5 lower the exchange marks the trader to deposit the margin for the latter transaction not for the first transaction. This mark to market margin is refunded by the stock exchange to the concerned broker at the end of the settlement period.

**Concentration Ratio Margin**
This margin is levied to prevent the trader showing interest on a few stocks to manipulate their prices. Margin is computed on a graded basis, if 70 per cent of trader's total turn over in the previous quarter is derived from three or fewer stocks.

**Special Margin**
Special margins are imposed to arrest price rigging. If there is a high degree of volatility in a particular scrip's prices, even 100 per cent margin is imposed by the exchange. The 100 per cent margin curbs the high degree of price fluctuations.

**Recent Trends in the Margin**
In a move to curb excessive volatility in stock prices, the Securities and Exchange Board of India (SEBI) has reduced the daily price band from the current level of 10 per cent to 8 per cent. Replaced the existing weekly price band of 25 per cent by a graded margin system linked to price movements.

A security is considered to volatile if its price varies by plus or minus 16 per cent or more in a single trading cycle. For computing the price variation the closing price at the end of each day is compared with the closing price at the end of the previous settlement. If the price variation is 16 per cent or more, the margin rate is 5 per cent for 24 per cent or more variation 20 per cent, for 32 per cent or more variation 30 per cent and for 40 per cent or more the margin is 40 per cent.

Price variations because of calls, bonuses, rights, mergers, amalgamations and scheme of arrangements are excluded for determining volatile securities and adjustments in prices.

The additional volatility margins came into effect from the first trading period commencing on or after July 6, 1998. Simultaneously there restrictions on short sales are imposed and the 50 per cent margin for securities on no-delivery is removed. Once a security attracts the volatility margin, the margin will continue on the security at the margin rate as on the last day of the previous trading period for the first two trading days in the subsequent trading cycle also.

The additional volatility margin is applicable for the cash and carry forward markets. This margin would be applicable on the buy side when prices rise and on the sell side when the prices fall.

The margin would be payable on the outstanding buy or sell positions of the security at the end of each day. The margin would be in cash, bank guarantees or fixed deposits in banks by the brokers. The margins collected will be due for release along with other margins on completion of pay-in of securities.

The additional volatility margin would not be mandatory for securities whose price is less than Rs 40. However, it would be up to the exchanges to consider applying the additional volatility margin on the securities in case it is deemed necessary by the exchanges. If, the price of a security increases to Rs 40 or more, it will be eligible for consideration towards this margin. If the price goes down below Rs 40 in a trading period it will still be eligible for consideration during that trading period.

The additional volatility margin is levied, along with existing mark to market margin, daily carry forward margin, incremental carry forward margin, concentration margin and special margins. In the case of carry forward trade, the cumulative margin on a security on account of the above additional volatility margin.
and incremental carry forward margin is subject to an upper limit of 50 per cent.

In press release issued, SEBI stated, “Such a graded margin system would on the one hand contain volatility in securities, which on the other keep open and exit route for investors. It was felt that this graded margin system should be in addition to the existing margin system. This would provide additional market safety and also act as a deterrent to building up of excessive outstanding positions in the market”.

In May 2000 index linked margins for badla has been introduced. The new carry forward margin provides for the following:

- A 12.5 per cent margin if the BSE Sensitive index is below 4,500 points
- A 15.0 per cent margin if the BSE Sensitive index is between 4,500 and 5,250 points
- A 17.5 percent margin is the BSE Sensitive index is between 5,250 to 6,000 points
- A 20.0 per cent margin if the BSE Sensitive index is over 6,000 points

The additional carry forward margin has been linked to the gross outstanding position (GOP) of net outstanding position (NOP) arrived at after the carry forward sessions. The slabs prescribed are as follows:

If the GOP is over Rs 250 Cr or NOP is between Rs 150 and 200 Cr, the margin is 15 percent.

If the GOP is between Rs 150 Cr and Rs 200 Cr or NOP is between Rs 100 Cr and Rs 150 Cr, the margin is 10 percent.

If the GOP is between Rs 100 Cr and Rs 150 Cr and the NOP is between Rs 80 Cr and Rs 100 Cr, the margin is 5 percent.

Carry Forward Transactions

In the specified group, shares settlements can be done in three ways (a) delivery against payment (b) squaring up of the transaction (i.e. a purchase is offset by sales and vice-versa) (c) carrying over the settlement to next settlement period. The first two types are simple but the third one is complex. It can be explained by an example. An investor Mr. A buys 1000 shares on Monday at the price of Rs 50 but on the settlement day the settlement price is Rs 60. Now A has three options:

Paying Rs 50,000 and taking delivery of the shares.
Selling and booking a profit (Rs 60-50) × 1000 = Rs 10000
Carrying the transaction forward if he believes that the price may go up further.

In the third situation Mr A is postponing the payment as well as taking delivery of the shares. Either he can enter into a contract with the carry forward broker or with the badla financier. It depends upon the condition whether he has bought the shares straight from the carry forward broker or not. He has to get the difference between the consideration for which he has bought and the mark-up price on the settlement day. The mark-up price is determined by the stock exchange i.e. the rate (price) at which the settlement has to be carried over. The mark-up price resembles the closing market price of the previous day.

Forward seller or the badla financier executes a resale contract with Mr. A for a subsequent settlement at the new rate i.e. Rs 60/- plus badla charges (the interest factor) for the remaining amount to be settled (Rs 50,000). Now, on the next settlement date if there is a further rise in the price of the scrip, Mr. A again has the options either to close the transaction or carry forward the settlement to the next cycle. The same procedure mentioned above will take place again. This transaction may be carried forward up to 90 days.

If, an investor sells shares and wants to carry forward, he gets profit when the share price falls and lose when it gains. To carry forward his short position he has to pay a back wardation charge or undha badla charge for borrowing the share certificate. He has to enter into a contract to resell the shares to the lender at the next settlement period and pay interest rate.

Now it is clear from the above example that four parties are involved in the carry forward system the investor, the broker, the badla financier and the stock exchange.

Investor

There is no compulsion for the investor to specify the nature of trade, which he is going to have, he has to option to inform the broker whether the trade is for delivery or for carry forward. If it is not specified, the stock exchange will treat it as a carry forward trade. It can be settled within the settlement period or it can be carried forward to the next period. If the trade is informed for delivery, the trader has to play lower margins. The margin for the carry forward trade is 15 per cent, whereas that for delivery is 7.5 per cent. The lower margin is applied both for buying and selling. An investor can avoid paying the margin provided the stock are deposited with the clearing house within 48 hrs of the transaction. Once the investor has opted for delivery, he cannot reverse the situation i.e. an investor cannot buy and sell or vie cersa in the same settlement period.

If the investor has declared to carry the trade or remained silent, he has the only disadvantage of paying higher margins but he can liquidate his trade or carry it forward. The investor has to bring in additional funds whenever there is a loss in the carry forward transactions. These losses are computed on weekly basis by marking the position to market at the prevailing price. The profits earned under carry forward transactions are forzen till the positions are squared.

Brokers

The brokers are categorized into: (1) not interested in carry forward business (2) interested in vyaj badla i.e. money or scrip lenders (3) interested in carry forward business. Members can switch from one category to another. The broker has to give two reports: a daily report and another at the end of the carry forward system. There are two additional sessions, held along with the regular trading sessions. Ayaj badla members can lend shares or money in these sessions.

The reports give the details of sales for delivery, sales for carry forward, purchases for delivery, purchases for carry forward, vyaj badla and share badla. The limits are imposed for each member, each scrip and the total trades. If the limits are crossed they have to inform the stock exchange. This daily reporting is exempted for the first few days of each settlement.

Badla Financier

Badla financing is carried out by two ways either by lending money or sby lending shares for the sort position. The badla money financier enters into contract on the badla finacing day.
The badla financier cannot use his position to earn higher badla charges in the next settlement period. The shares received from the seller have to be deposited in the clearing house till the arrangement for the borrowed fund is complete. If the original buyer carries forward the position for four settlements the financier get the principal only at the end of the fourth settlement.

The Stock Exchanges
The stock exchange has to arrange for separate trading sessions for the carry forward transactions. In an extraordinary situation it has to levy special margins for the various types of transactions and limit the total trades. The exchange has to monitor the margins deposited by the members with the clearing house under different transactions, the limits prescribed for each member against individual scrips, the over all limit for each member and the over all limit for the scrip under carry forward system. The exchange provides one exclusive carry forward transaction day (on Saturday following the last day of settlement between 9.30 a.m. and 1.30 p.m.) followed by at least two carry forward sessions along with normal screen based trading session. The exchange also provides several screen based trading features for the carry forward sessions. A quote driven automated trading facility with the order book functioning as an auxiliary jobber is provided. The trading system is fair to the jobbers who give two way quotes by giving them the priority to match orders when theirs and other operator’s rates match.

Badla Track Record
Introduction of badla and ban on badla is not new to the market players. If one reviews the history, badla was banned several times.

Upto 1969 : Badla system was in vogue
June 1969 : Government of India prohibits all transactions other than for ash/delivery
1970 : Lifting of the ban on forward trading was suggested by Prof. J.J. Anjaria Committee but ban continued.
1972 : Mumbai, Ahmedabad, Delhi and Calcutta Stock exchanges evolve a pattern of trading similar to the earlier system.
1983 : Forward trading was permitted for the specified group shares for a period of 90 days. The settlement cycle was 14 days.
Only Mumbai, Ahmedabad, and Calcutta stock Exchanges were permitted to adopt the system.
Dec 1993: Badla was prohibited by SEBI. Six weeks grace period was given to settle the open positions.
Jan 1994 : SEBI bans Badla
March 1994 : Stock exchanges suggested modified proposal for Carry forward and SEBI rejected the proposal.
Feb 1995 : SEBI appoints three-member committee Comprising Mr. G.S. Patel, Mr.Deepak Parek, Mr. M.R. Mayya to review the carry forward system.
March 1995 : G.S. Patel Committee submits its report.
Jan 1997 : BSE asks for a review of the revised system.
March 1997 : SEBI appoints J.S. Varma Committee to review the revised badla system.
July 1997 : J.S. Varma Committee report has been submitted.

Questions
1. What are the functions of stock exchanges? How are the managed?
2. Specify the conditions for a person to become a member of a stock exchange.
3. How are trades settled in the stock markets?
4. What are the measures taken to contain the price volatility?
5. What is carry forward transaction? Explain.
6. What is meant by stock exchange? What are the functions of a stock exchange?

7. How do stock exchanges function? Discuss the recent changes that have taken place in the trading?

8. How are stock exchanges controlled by the regulatory authority?

9. What are the requirements to become member of the stock exchange? Explain the role of brokers in the trading of stock.

10. Enumerate the various types of orders.

11. How are listed shares classified? Explain the settlement cycle of the Mumbai stock Exchange.

12. "Price filters reduce the price volatility" - Discuss

13. How do price filters control circular trading?

14. What is meant by margin? Explain the different types of margin imposed on the trading of stocks.

15. How are the fluctuations in the stock prices controlled?

16. Discuss the functioning of the carry forward transaction.

17. Explain the parties involved in carry forward transaction.

18. What are the margins imposed on the carry forward transaction?

19. "Price filters and margins imposed on the carry forward transaction?"

20. Discuss the present position of secondary market in India.

**Multiple Choice Questions**

1. Stock exchange
   a. Helps in the fixation stock prices
   b. Ensures safe and fair dealing
   c. Induces good performance by the company
   d. All the above  
   [Ans d]

2. In the governing body of the stock exchange, certain percentage of the elected members retire at annual general meeting. That is
   a. 33%
   b. 40%
   c. 50%
   d. 25%  
   [Ans a]

3. The President and Vice President of the stock exchange can offer themselves for re-election after a gap of
   a. One year
   b. Two year
   c. Three years
   d. Six years  
   [Ans a]

4. "Sell Reliance Petro shares at Rs 60". This order is a
   a. Best rate order
   b. Limit order
   c. Discretionary order
   d. Stop loss order  
   [Ans b]

5. In BSE shares are divided into
   a. Two categories
   b. Three categories
   c. Four categories
   d. Five categories  
   [Ans b]

6. The settlement cycle in BSE and NSE are
   a. 10 days
   b. 8 days
   c. 7 days
   d. 15 days  
   [Ans c]

7. The rolling settlement period introduced in the stock exchanges is
   a. T + 5
   b. T + 7
   c. T + 10
   d. T + 15  
   [Ans a]

8. Carry forward transactions are permitted for a period of
   a. 70 days
   b. 75 days
   c. 80 days
   d. 90 days  
   [Ans d]

9. In May 2000 the badla transaction’s compulsory margin is linked with
   a. BSE Sensex
   b. BSE-100
   c. BSE-200
   d. trading of the broker  
   [Ans a]

10. The broker has bought 10,000 ABC share at Rs 200 and sold 8,000 shares at Rs 190 on the same day the margin he has to pay is
   a. Gross exposure margin
   b. Special margin
   c. Mark to market margin
   d. Concentration ratio margin  
   [Ans c]