Chapter 1  Background and Perspective Framework of the Study

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1.1 Introduction

The capital market is one of the most vibrant sectors in the financial system, marking an important contribution to economic development. Two major reasons why Indian securities are now increasingly regarded as attractive to international investors are the relatively high returns compared with developed global markets as well as the low correlation with the world markets. Capital occupies a position so dominant to the economic theory of production and distribution that it is natural to assume that it should occupy at least an equally important place in the theory and practice of economic growth. It is usually implied that economic growth and capital accumulation with a high positive and significant correlation and additions to the stock of capital can provoke and facilitate faster rate of growth even under the circumstances which can be described as shortage of capital.

The aforesaid correlation between the process of economic growth and capital accumulation inspired the earlier theorists of economic development and even in the works of modern economists output is still assumed to be limited by capital whether there is abundant labour or not. A high rate of capital formation usually results in rapid growth in the production and income, but more capital formation by itself will not bring a corresponding acceleration in the growth of production. It also depends to a large extent on the manner in which the capital is utilized.

Capital market means the market for all the financial instruments, short term and long term as also commercial, industrial and government paper.
The capital market deals with capital. The capital market is a market where borrowing and lending of long term funds takes place. Capital markets deal in both debt and equity. The governments both central and state raise money in the capital market, through the issue of government securities. Capital markets refer to all the institutes and mechanisms of raising medium and long-term funds, through various instruments available like shares, debentures, bonds etc. 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 institutions also raise a lot of money from these markets. Examples of well-developed markets are – The Global depository and American depository. Moreover, the establishment of National Stock Exchange and Bombay Stock Exchange has been turning point in the working of capital markets.

"The volume of fresh capital raised on the primary market has declined significantly. The secondary market reforms have not really progressed because of the recalcitrance of the market operators’ and SEBI’s lack of will. The stock market is plagued by uncommonly high number of drawbacks, malpractices, weaknesses and so on. Both the primary and secondary market has remained depressed. The annual average growth rate of return of the stock market and other financial market has declined and other has not been much gain in terms of reduction of volatility of prices and return; infact, volatility has increased. The stock market has continued to be highly speculative."¹
1.2 Statement of Problems:

1. The complexities in the equity market have grown many folds. The market is moving on the basis of the behavior of the investors in the market.

2. The equity market is quite volatile due to the FII's entry and exit in the market and small investors are losing huge fund in short run if the volatility continues.

3. Derivative trading has been introduced in India capital market to protect the risk against the fluctuation of the prices, but it is not being used to hedge the fund rather for speculative activities which is making the investors in danger.

4. As and when the market is at boom, the companies come up with their IPOs. It is making the investors confused as they can get more prices for the same security during the boom time. Ultimately, it invites risk to the investment of investors as many times the IPO listed below the price of issue.

5. Asset prices are so high that they show all the signs of a stock bubble.

6. India was relatively untouched by the Asian financial crisis of 1997, but it is much more vulnerable to changes in external cash flows today.

7. India is very dependent on global cash flows. Unlike China, India runs a trade deficit and only showed a total capital account surplus in fiscal 2006 because of that US$12.5 billion from overseas investors in
stocks, foreign direct investment of $6 billion in 2006 and rising corporate borrowing on international capital market.

8. India's companies show above-average profitability. The average return on equity for Indian companies on the Mumbai stock exchange is 21%. It is significantly above the 18.7% average return on equity for the U.S. members of the Standard & Poor's 500 Index ($INX).

9. In addition, Indian companies are comparatively underleveraged, with an average debt-to-equity ratio of just 70% compared with a ratio of 123% for the S&P 500 companies. That means they've got plenty of room to add debt, which will in turn increase leverage, return on equity and profitability for investors.

10. The months of April, March and February have been quite volatile on the basis of degree of volatility as compare to the other months in India.

11. The impact of oil prices is directly affecting the Indian capital market.

12. The emergence of derivative segment is again creating problems for the equity delivery based market. Most of the investment in the market is speculative in nature and affecting the interest of the real investors.

13. 'Over the last decade of reforms, one of the things that we could not ignore about India has experienced dramatic development in the equity market. If nothing else, it has been a puzzle trying to figure out why our equity market appears to vacillate between suffering from scams and
market misconduct, and emerging one of the best developed markets in the world.\textsuperscript{3}

1.3 Emerging Issues

Indian capital market has gone with tremendous changes especially after the economic liberalization. No doubt, the market has achieved different milestones but simultaneously it has given many threats to the market which is making the apex authorities difficult to make the market in control. Some of the issues are mentioned below:

1. Recently, several large equity offerings, including those from reputable business houses, have struggled to hit their targets. India’s stock markets have been volatile, reacting to fears of a widening global credit crunch and fears of a U.S. recession.

2. India, among the European investors, is believed to be a good investment despite political uncertainty, bureaucratic hassles, shortages of power and infrastructural deficiencies. India presents a vast potential for overseas investment and is actively encouraging the entrance of foreign players into the market. No companies, of any size, aspiring to be a global player can, for long ignore this country which is expected to become one of the top three emerging economies.

3. India is the fourth largest economy in the world (ranking above France, Italy, the United Kingdom, and Russia)\textsuperscript{4} and has the third largest GDP in the entire continent of Asia. It is also the second largest among emerging nations. (These indicators are based on purchasing power parity.) India is also one of the few markets in the world which offers
high prospects for growth and earning potential in practically all areas of business. Yet, despite the practically unlimited possibilities in India for overseas businesses, the world’s most populous democracy has, until fairly recently, failed to get the kind of enthusiastic attention generated by other emerging economies such as China.

4. The reason being, after independence from Britain 50 years ago, India developed a highly protected, semi-socialist autarkic economy. Structural and bureaucratic impediments were vigorously fostered, along with a distrust of foreign business. Even as today the climate in India has seen a sea change, smashing barriers and actively seeking foreign investment, many companies still see it as a difficult market. India is rightfully quoted to be an incomparable country and is both frustrating and challenging at the same time. Foreign investors should be prepared to take India as it is with all of its difficulties, contradictions and challenges.

5. Success in India will depend on the correct estimation of the country’s potential, underestimation of its complexity or overestimation of its possibilities can lead to failure. While calculating, due consideration should be given to the factor of the inherent difficulties and uncertainties of functioning in the Indian system. Entering India’s marketplace requires a well-designed plan backed by serious thought and careful research. For those who take the time and look to India as an opportunity for long-term growth, not short-term profit- the trip will be well worth the effort.
6. Developing a basic understanding or potential of the Indian market, envisaging and developing a Market Entry Strategy and implementing these strategies when actually entering the market are three basic steps to make a successful entry into India. Developing a basic understanding or potential of the Indian market The Indian middle class is large and growing; wages are low; many workers are well educated and speak English; investors are optimistic and local stocks are up; despite political turmoil, the country presses on with economic reforms. But there is still cause for worries-

7. The rapid economic growth of the last few years has put heavy stress on India's infrastructural facilities. The projections of further expansion in key areas could snap the already strained lines of transportation unless massive programs of expansion and modernization are put in place. Problems include power demand shortfall, port traffic capacity mismatch, poor road conditions (only half of the country's roads are surfaced), low telephone penetration (1.4% of population).

8. Although the Indian government is well aware of the need for reform and is pushing ahead in this area, business still has to deal with an inefficient and sometimes still slow-moving bureaucracy.

1.4 Review of the Literature

The subject matter of Capital Market in its multifacism spheres has been the thought provoking subject of topical interest. In the following paragraphs, the researcher has made a comprehensive review of literature on the wide-
ranging studies on the variegated aspects of Indian capital market. The notable among them are:


Three types of informational efficiency (weak, semi-strong and strong) have been well identified by researchers in the field of capital markets throughout the world. Weak efficiency states that current prices fully reflect all the information contained in the history of past prices and denies the utility of charting and technical analysis. This issue has been researched in India over a long period and the overwhelming preponderance of evidence, for example, Barua (1980, 1987); Sharma (1983); Ramachandran (1985); Sharma and Kennedy (1977); Gupta (1985) is in favor of weak form efficiency. There have been only a few studies (Kulkarni (1978) and Chaudhury (1991a,b,c)) which did not support the weak efficiency hypothesis.
In the light of the above evidence, the results of Bhat and Pandey (1987) appear paradoxical. On the basis of a questionnaire survey, they conclude that the users and preparers of accounting information in India do not believe that the market is efficient in any of its three forms.

Semi strong form of efficiency deals with the speed with which publicly available information is assimilated by the market and incorporated in market prices. The evidence on this issue is mixed. Subramaniam (1989) found that in the case of political events, the market appeared to respond more efficiently to events whose impact on share values was characterized by low complexity and high clarity. The market seemed to have difficulty with ambiguous and complex events. Ramachandran (1985) and Srinivasan (1988) found that the market was by and large efficient in responding to the information content of bonus issues and rights issues respectively.

The third form of market efficiency (strong form) asserts that even inside information which is not publicly available is reflected in market prices very rapidly. This hypothesis is usually tested by evaluating the performance of mutual funds whose managers can be expected to have some degree of inside information. The research in this field is discussed in a separate section of this review.

In a unique work of its kind, L.C. Gupta (1980, 1981) examines the characteristics of the rates of return on equities in the Indian capital market for a fairly large sample of 276 companies over a sixteen year period from 1961-76. He concludes that the rates of return provided by equities are unsatisfactory because: a) about 20% of returns for various holding periods
are negative, b) the returns provide only a partial hedge against inflation, c) the fluctuations in returns even within a year are large enough to conclude that timing of transactions decisions have significant bearing on realized returns, d) the risk is considerable even when investment is made in a portfolio of securities and for long periods of time. While the study is an important milestone in research in Indian capital market, given the equity cult that started after forced dilution by MNCs because of FERA in the late seventies and the rise in the equity returns since the second half of eighties, the conclusions of the study are unlikely to be valid now for the Indian market. A comprehensive study of that kind for the more recent period is called for.

Srinivasan (1993) studied the efficiency of the market in assimilating the information content of rights issues and concluded that the market was by and large efficient. Rao and Bole (1990) have examined the real rates of return on equities in the Indian market for the period 1953-87. They conclude that equities provide only a partial hedge against inflation. While the long term real rates of return are positive, during periods of extraordinarily high inflation, the real rates of return are negative. The study would have been more useful had the returns provided by bullion also analyzed for the same period. It would also have been useful to break up the long period into sub-periods to determine whether the behaviour of returns was different for different sub-periods and whether reasons could be ascribed for any observed differences. As observed earlier in the paper, as the Indian stock market has been booming in recent years, the conclusions for a more recent period could be quite different from the conclusions reached in the study.
Several studies, for example, Sahni (1985), Kothari (1986), Raju (1988), Lal (1990), Chandra (1990b), Francis (1991a), Ramesh Gupta (1991a,c, 1992a), Raghunathan (1991), Varma (1992a), L.C. Gupta (1992) and Sinha (1993) comment upon the Indian capital market in general and trading systems in the stock exchanges in particular and suggest that the systems therein are rather antiquated and inefficient, and suffer from major weaknesses and malpractices. According to most of these studies, significant reforms are required if the stock exchanges are to be geared up to the envisaged growth in the Indian capital market.

The issue of inflation hedge has also been researched in the context of stocks. Verma (1991) compares the BSE National Index (Natex) which comprises 100 scrips with the Sensitive Index (Sensex) comprising 30 scrips and concludes that the Natex is a sluggish index that responds too slowly to market conditions. Changes which are reflected in the Sensex on any day are completely reflected in the Natex only by the next day. He finds that Sensex is more volatile than Natex. He concludes for this and other reasons that those who follow the Natex because of its greater comprehensiveness and theoretical appeal may be mistaken. The Sensex needs to be taken more seriously as a sound market index.

Venkateshwar (1991) explores the relationships of the Indian stock markets as reflected by the Bombay Stock Exchange Index, vis-a-vis other prominent international stock markets. 23 international Stock indices are used over the period 1983-87. He concludes that there is practically no meaningful relationship between the BSE index and other international stock market
indices, though the British and South Korean indices are inversely related to BSE.

Raghunathan and Varma (1992a) pointed out that any comparison of the Indian stock market with that elsewhere must be carried out on a common currency base. They find that in dollar terms, the SENSEX return over the 1960-92 period is only about 0.5%, while during the same period the returns in the U.S. (based on the S & P Index) and the Japanese (based on the NIKEI index) are 6.1% and 11.4% per year respectively. Over the twelve-year period 1980-92, the dollar returns for SENSEX, S & P and NIKEI indices turn out to be 6.5%, 10.65% and 13.6% respectively. For a shorter span of seven years, namely 1985-92, the returns for the three indices turn out to be quite comparable at 15%, 13% and 14% respectively.

Ignatius (1992) has done an interesting study comparing the returns in the BSE with those in the NYSE. He finds a mildly significant weekend effect in the returns on equities in India as well as seasonality in return, with the month of December providing significantly higher monthly return. Overall, the return patterns in the BSE and the NYSE appear to be similar. A more rigorous study of this kind involving other markets would be very useful at the present juncture when the Indian market has been thrown open to investment by foreigners, since such a study can assess whether there could be gains from portfolio diversification through investment in the Indian capital markets.

Pandya (1992) observes that as a regulatory and development body, SEBI's efforts in the direction of investor protection are varied and unlimited. The measures brought in by SEBI broadly cover measures for allocative
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efficiency in the primary market with fair degree of transparency, reforms in the secondary market for visible and mutual funds, regulation of various market intermediaries and above all for the protection of the investing public.

In his book, L.C. Gupta (1992) concludes that, a) Indian stock market is highly speculative; b) Indian investors are dissatisfied with the service provided to them by the brokers; c) margins levied by the stock exchanges are inadequate and d) liquidity in a large number of stocks in the Indian markets is very low. While evidently a painstaking work, the conclusions except 'c' above seem to be built on wrong or questionable arguments.

Ajeet Prasad [October 1996] in their article titled "Stock Exchanges: New Market Mechanism", highlights that the number of major changes have taken place after liberalization of the capital market in India like establishment of OTC for small and medium sized companies, market making, rolling settlement, online depository etc has improved the market.

Ashok Rambhia and Roshni Rao [November 1996] in their article titled "Global Stock Exchanges", highlights that the temporary setback of the equity on the Indian Stock Markets does not mean that one can write them off. An improvement in trading infrastructure and investor's protection mechanism is required. If an investor is made to feel secure with superior trading, clearing and settlement, transfer and regulatory mechanism, Indian exchanges will not only gain but surpass their past glory.

Rajiv Tayal [1999] in his dissertation titled "Impact of Buy Back of Shares on Indian Corporates" emphasized that the companies do the buy back of shares as a matter of strategy. If it is advantageous for the company
then it may go for it. If the expected prices of the concerned companies are likely to go high and it has been forecasted and predicted strongly then companies may go for it. Sometimes to manage the capital structure also it is undertaken.

Aqeel-ur-Rehman [1999] in his dissertation titled “The role of SEBI’s in Indian Capital Market” highlights that the SEBI is responsible for the entire development in the capital market. It has introduced lot of new thing which are being experienced in the developed capital market.

Md. Faiz Alam [2000] in his dissertation titled “SEBI and Management of Indian Capital Market” highlights that the SEBI is responsible for the entire major changes in the capital market of India. The main emphasis has been given on the protection of the fund of the investors and to check the frauds and unfair activities.

Aftab Ahmad Khan [2000] in his dissertation titled “Prospects of Future in India” said that the new instruments have been introduced in the market during 1999-2000 for the hedging of the investment. Its objective is to hedge the risk associated with the fluctuation of the prices. If it is properly used then only its benefits may bless otherwise it has been in use for speculative purposes in most of the developed countries.

Shakyendu [2000] in his dissertation titled “Look back Option and their Applicability in India” highlights that the introduction of the derivatives trading is highly recommended to ensure the protection of the interest of the investors. It has always been in want to protect the investment of the investors
in the Indian capital market against the unwanted fluctuation of the share prices.

Khan Farhat [2001] in his dissertation titled “SEBI's guidelines and Protection of Small Investors in India”, highlights that the number of steps taken by the SEBI to protect the interest of the investors has given the confidence to investors in the Indian capital market and day by day their investment is ballooning in the market.

Khan Safiuddin [2002] in his dissertation titled “Development of Equity Research in India”, highlights that the number of specialized firms have been established since 1991 in India to provide the investment information to different investors on the basis of research of the company’s information. It is leading to professionalism in the India capital market.

Khan Rashid Ali [2002] in his dissertation titled “Recent Changes in the Mechanism of Stock Exchanges in India” stressed that in recent years especially after the liberalization of the capital market, the entire mechanism of the working of the capital market has gone metamorphosis from old, conventional and outdated to modern one.

Asif Abbas Abdi [2003] in his dissertation titled “Role of Depository System in Indian Capital Market: A case study of NSDL” highlights that the SEBI is responsible for the entire development in the capital market. The main reason of the making the Indian capital market at par with the global standard is due to the establishment of NSDL as the first depository to provide trading and custody of securities in electronic form. Since then, the number of investors in the market has increased many folds.
Mehta Balraj [January 2003] in his commentary on “Indian Share Market in for Big Bang Expansion” reveals that Sebi’s role, establishment of NSE etc. have been of great help in making the India Capital market at par with the global standard. Again this study could not touch the role of Depository Institutions in bringing the capital market at par with the global standard.

Mehta Balraj [July 2003] in his article titled “Is India’s Primary Market is Reviving?” highlights that the different companies are coming with the IPOs due to the good response of the investors. Companies are giving huge benefits to the investors and as a result of that they are also buying stocks from the primary market. It is leading to the growth of the Indian Capital Market. Most of the IPOs have shown premium price on the very first day of its listing. This study does not take in to consideration that how the market matured to the global standard.

Khan, Amanor Rehman [2003] in his dissertation titled “The Securities Exchange Board of India- An evaluation of performance” highlights that with the starting of the functioning of the SEBI, lot of changes in the form of reforms have been done in the primary as well as secondary market. His study concludes that the present condition of the capital market is the result of the positive actions of the SEBI.

Ahmad Rafai [2003] in his dissertation titled “Organisation and working of Securities Exchange Board of India in recent year” stressed that the capital market is in the global picture. It has been doing quite well due to the efforts
made by the SEBI in last few years like introduction of depository system has really changed the pattern and way of working.

Keneth M. Kletzer [July 2004] in his paper "Liberalizing Capital Flows in India: Financial Repression, Macroeconomic Policy and Gradual Reforms" highlighted Capital account liberalization in financially repressed economies often leads to a period of rapid capital inflows followed by financial crisis. This paper considers the vulnerability of the Indian economy to financial crises with international financial integration and the policy agenda for further liberalization of capital flows. The legacy of financial repression on fiscal and financial policies poses the primary challenge to stable integration of the domestic financial markets of India with international capital markets. Brief overviews of the theory and experience of liberalization elsewhere and of the recent liberalization by India frame the discussion of the risks of liberalization and sequencing of policy reforms.

Mehta Balraj [August 2004] in his article "Share Market Stage Rally Following Cut In Turnover Tax Rates" finds that the stock market of India is showing new peak due to the performance of some of the companies like Infosys, Satyam, Reliance, SBI, Tata steel, Digital Global, HPCL, SAIL, Canara Bank etc. These companies have shown tremendous performance due to the favorable policies of the Government and of course interest of the investors.

Mehta Balraj [November 2004] in his article titled "Is the Share Market Rally warranted", highlights that the mid cap is really performing well and slowly and gradually the Indian capital market is maturing. Now investors are
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showing interest in the capital market. The P/E ratio of madcap is higher than that of large cap companies.

Raju M.T. [Oct.-Dec. 2004] in his article “Capital market reforms in India: An Evaluation” published in India Journal of Commerce, reveals that the various steps taken to make the capital market reforms in India. These factors are Disclosure standards in Primary market, introduction of number of innovative instruments, Better price discovery through Book-building process, Professionalism, Screen-based trading with transparency, introduction of rolling settlement, Dematerialization, reduction of implicit and explicit cost, safety measure to protect the interest of investors, introduction of derivative trading, Inviting FIIIs etc.

Mehta Balraj [January 2005] in his article titled "Surge in Trade in Stock Market" highlights that the stock market of India is on surge due to the speculative activities by FIIIs. As long as the market is bullish, FIIIs will show the interest. The Indian stock market is yet to perform well. So the FIIIs will continue to push the stock market.

Mehta Balraj [February 2005] in his article titled "Sensex and Nifty Touch New Peak Levels on Frantic Buying" highlights that the Sensex and Nifty is going on the new peak due to the hectic buying by the FIIIs and other investors. They are buying from the Indian Capital market as it has tremendous potential to grow. Numbers of initial Public Offerings have also gone up. But his study does not show the causes of this boom in the Indian Capital market.
Md. Wamiq [2005] in his dissertation titled "Techniques of hedging risk in Stock Market", highlights that the number of new hedging tools like future contracts, option contract and swaps etc. have given the protection cover to the investors but it is not being use for protection of investment against risk rather these are used for speculative activities.

Imam Ashraf [2005] in his dissertation titled "Reforms in Trading Pattern of Stock Market of India" highlights that the pattern of stock trading has tremendously changed from the conventional one to the modern one. It has lead to make the Indian capital market more efficient. These changes are introduction of Internet based trading, establishment of depositories etc.

Khan Mohd. Arif Raza [2005] in his dissertation titled "Performance of new equity issues in India" highlights that the new issues in India have done well due to the great response by the FII's, Mutual fund, individual and other investors. It has become possible due to the reforms measures taken by the SEBI since its establishment and taking over the charge of an apex body to regulate and control the Indian capital market.

Mohd. Suhaib [2005] in his dissertation titled "Behavior of Share Prices in India" highlights that during recent years the prices of stocks are moving as per the action of FII's. As and when there is buying pressure from them the prices are likely to go northward and if there is selling pressure from them the prices are going down.

Raju M.T. [2005] in his article titled "Capital Market Reforms in India: An Evaluation" said that the SEBI has been framing, regulations, guidance and also changing them from time to time to make Indian Capital Market a
modern, safe, fair and efficient one. He also made an attempt to list some of the major policy reforms initiated by SEBI and to measure their impact on capital market in general and on investors in particular.

Harvinder Kaur [2005] in her article titled “Stock Market Volatility in India” highlights that how Indian stock market is experiencing the volatility in share prices. He found in her study that April has been the most volatile followed by March and February. This could probably be due to the occurrence of the most significant economic event in the year namely Union Budget.

Gulcharan Singh [2005] in his article titled “Illiquidity in Stock Exchanges: Some Issues” highlights that how Indian stock market is also facing the problem of illiquidity for certain shares of the companies. It is happening due to the poor working results of the companies, reduction in the percentage of public offers, classification into Z category, low capital base of listed companies, introduction of the rolling settlement, free pricing of shares, introduction of book building, merger of unlisted companies, and lack of incentives for the market makers.

Shrawan Kumar Singh [2005] in his article titled “Foreign Portfolio Investment in India”, said that the nature of FIIs differ on the basis of their country of origin. It has been observed on the basis of his study that the market has been quite volatile on the basis of inflow and outflow of the fund by FIIs in the Indian capital market. Whatever is done by FIIs in the market, it is copied by the Mutual Fund, individual and other investors.
Kedarnath Mukhari and R.K. Mishra [2005] in their article titled, “Stock Market Inter linkages: A Study of Indian and World Equity Markets”, highlights that the Indian stock market is not co-integrated with other international markets in the long run and there is no cause and effect relationship among those markets except Indonesia, Malaysia, Thailand, Korea, Philippines and Greece. In short run there is some possibility so there is a greater chance for international diversification to enhance their potential benefits.

Mahboob Fazal [2006] in his dissertation titled “Role of IPOs in Globalised India” highlights that due to the congenial and sophisticated environment provided by the SEBI, new and new IPOs are striking in the market. The large numbers of companies are in queue for IPOs as the market indexes are going up so companies are likely to get better prices for their securities.

Arif Ali [2006] in his dissertation titled “A study of SEBI’s role in Development of Capital Market” highlights that the SEBI is responsible for the entire development in the capital market. Since the SEBI has been assigned the task of an apex institution to regulate the market, the Indian capital market has gone metamorphosis.

Mehta Balraj [March 2006] in his article on “ Booming Stock Market and Sinking Indian Rupees “reveals that the Indian capital market is booming but simultaneously the rupee is loosing its value. This study is not saying any thing about what prompting the Indian Capital market to boom.

Mehta Balraj [April 2006] in his article on “Sharpe Upsurge in Equities on Frantic Buying” reveals that the Boom in the Indian capital market is due to
the hectic buying of stocks from the market by different investors. Since GDP rate is going up that is why the stock market is also at boom and nothing else. His analysis does not throw light on the factors to make the buyers to buy from the market.

Mehta Balraj [July 2006] in his article on "Indian Share Market hit by the Volatility in The Global Stock Exchanges" reveals that the Indian capital market is bullish due to the tremendous potential of growth and due to the favorable global business environment. His work is unable to say anything on the main reason to make the Indian capital market at par with the global standard.

Mehta Balraj [October 2006] reveals in his article on "Sensex outdoes Global Market" that the Index of stock market of India is growing at a faster rate of 8.9% than that of the Indonesia's Jakarta at 5.9%, Russia's RTSI at 4.9%, Mexico's Mexbol at 4.7% and Korea's Kospi at 4.2%. But his study is unable to throw light on the various factors responsible to make the Indian Capital Market in the Global picture.

Subha M.V. [March 2006] in her article titled "Indian Capital market: A Road Ahead" published in Indian Journal of Marketing, threw light on the current issues in the Indian Capital Market. The individual investors are averse of investing in the capital market. The FII's and mutual fund companies do most of the investment. But the Indian Capital Market is emerging.

Satish D. and Vaddepalli Surender [March 2006] in his article titled "Real Estate- Private Equity to Fuel Growth" published in The Analyst enquires that the India Stock Market is witnessing handsome growth in the
recent times, every reputed investment firm is looking to capitalize on the opportunities real estate has to offer. The Indian capital market is at boom due to one of the key attractions for private equity players is the ability to invest relatively large amounts of capital and earns returns in excess of 25%.

Satish D. [June 2006] In his article titled "Private Equity- Hub of Activity" published in The Analyst enquires that the India Stock Market is witnessing significant activities in the private equity space with a number of overseas and domestic private equity firms eyeing for opportunity. Various sectors like real estate, information technology etc are at boom that is why the FIIs and other investors have done a lot of investment.

Satish D. and Bharti Y Bala [July 2006] In his article titled "Indian Stock Market- The Tightening Bear Grip" published in The Analyst enquires that the India Stock Market have continued their downward Journey for sometime now, confirming the strengthening position of the bears. When the US interest rates increase {or expected to increase), the FIIs invest more in the fixed income securities over there, which reduces the portfolio weights of the emerging markets stocks.

Ghosh S.N. [December 2006] In his article titled "Large Shareholder activism, Economic Reforms and Corporate Governance- Indian Landscape" published in Chartered Secretaries enquires into the contribution of large shareholders on notions of performance monitoring to ensure corporate governance and particularly on the role of internal and external forces that govern a company’s behavior.
Raul R.K. [2006] in his article on “Stock Market Boom, Bubble or Burst?” Reveals the stock market success in India is based on the structural rather than cyclical boom. His work, however, does not cover the various factors responsible to make the India Capital market in the global picture. In his work he only pointed out dematerialization, introduction of derivatives scrap of badla trading in stock index future etc are the factor to support the Indian Capital Market.

Biswa Joydeep [2006] in his article “Development of Indian Capital Market: Role of Foreign Portfolio Investments” reveals that Foreign Portfolio Investment (FPI) inflows in India has taken three routes- American Depository Receipts (ADRs), Global Depository Receipts (GDRs), AND Foreign Currency Convertible Bonds (FCCB). FPI is the factor responsible to change the entire scenario of Indian Capital Market. But his study is unable to explain why FPI are making India as investment destination in the Capital market.

Saifi Mohd. Waseem [2006] in his dissertation titled “FIIs in the India Equity Market: An Appraisal”, highlights that the number of FIIs and their volume of investment is increasing in the Indian capital market and as a result of that the indexes of the stock exchanges are going up.

Kumar Pradeep [2006] in his dissertation titled “Impact of Liberalization on Financial Sector in India” highlights that the policy of liberalization has made the Indian capital market so efficient. The privatization and entry of FIIs in the market has compelled the Government of India to make improvement.

Ansari Valeed K., Mahmood Fizza [June 2007] in their article on “Stock Market efficiency in India: An empirical scrutiny of the Price earning anomaly”
reveals that P/E ratio anomaly is nonexistent in India. Further, no relationship was found between beta and return. It shows that CAPM may not hold in Indian context.

Mehta Balraj [June 2007] in his article titled "Stock Market Euphoria", highlights that the euphoria in India and abroad, methodically whipped up, over the operation of global stock market and its increasing forceful and close linkages with stock market in India is remarkable.

Parameshwaran R., Thanihaivel M., [June 2007] in his article titled "Sensex- A simplified Representation of Reality", highlights that the sensex is the barometer of the economy and in whatever manner the sensex is moving, is the copy of the movement of the Indian economy.

Vijayakumar N., Rao K. Chandra Sekhara [July 2007] in his article titled "Volatility Smiles in India Option Market; A study", highlights that the relationship of implied volatility against different exercise prices, often results into a phenomenon, popularly pronounced as 'Volatility Smiles'.

Mehta Balraj [July 2007] in his article titled "Super Share Market in The Making", highlights that there should be the possibility of a marriage between BSE and NSE to gain ground at a time when global stock exchanges like NYSE and Euro next to create a single entity.

Mehta Balraj [August 2007] in his article titled "Share market move in A 7-year cycle of bull and boom; say market pundit", highlights that the ups and downs in the market is only cyclical, which is likely to happen in 7 years. The
current boom is likely to end in 2012. The last time this happened was in 1997 when the Asian market hit the peak and there was a capital flight out of Asia.

1.5 Research Gap

A review of similar studies in the context of Capital Market of India reveals that with the exception of a few studies and scanty articles written in newspapers and magazines, very little work has been done in respect of this. After going through the various articles, projects and research works of different researchers related to the capital market which is divided into primary and secondary market, Researcher concludes that there are number of issues related to primary and secondary markets of the Indian capital market. These are related with the operating efficiency, weak, semi strong and strong form of the market, problems and prospects of gilt and other debts based securities, story of IPO, role of different types of investors in the capital market like FIIIs, mutual funds, NRIs, corporate and individuals etc. a lot of work has been done on the government securities market, efficiency of the market, capital market reforms including primary and secondary market. Since the composition, dominance and importance of stock market is more and is of vital importance so the work done by me related and touching some burning issues of the equity market of India. With the literature review done, I came to know that FIIIs and their impact on the stock index of the Indian equity market, the impact of liberalization policy in regard to the liquidity, marketability, profitability, volatility and on the overall institutional efficiency of the market is still untouched. That is why the proposed research work is to check the impact of liberalization policy on these aspects of Indian equity market.
1.6 Scope and Objectives of the study

The overriding objective of the study is to assess the relationship between the liberalization policy and its effectiveness and impact on the Indian capital market. However, the proposed work has been undertaken to achieve the following specific objectives as well:

1. To examine the role of capital market in promoting the economic development.
2. To examine the various major environmental changes affecting the Indian capital market.
3. To study the role of Foreign Institutional Investors (FIIs) in Indian capital market.
4. To analyse the various changes in India Capital market after liberalization.
5. To make a comparative study of Indian capital market with global capital market.
6. To check the liquidity and operating efficiency in the equity market as a result of the liberalization policy.
7. To measure the volatility of the capital market after liberalization.
8. To find various measures to overcome the problems of Indian capital market and to make suggestive strategies to get maximum benefits from the globalised capital market.
9. To make various measure to make the Indian Capital market at par with the global standard.
1.7 Hypotheses of the study

The following hypotheses are formulated to test and to substantiate the objectives of the study:

**H₀-1** The liquidity and marketability in the Indian capital market have not improved in the post liberalization regime which is measured in terms of the following three parameters:

a. Total turnover in the Indian capital market has not improved in post liberalization era.

b. Turnover in relation to percent of GDP has not improved in post – liberalized era.

c. Market capitalization in terms of % of GDP of Indian capital market has not increased in post liberalization era.

**H₀-2** The profitability of the Indian capital market has not improved in post liberalized era as the market was unexplored and immature in pre-liberalized era. The profitability has been measured on the basis of P/E ratio and stock index (Sensex – the barometer) which reflects economic progress of the economy in the post liberalization era.

**H₀-3** The Indian capital market has not become more volatile in post liberalization period.

**H₀-4** There is no positive relationship between the investment of Foreign Institutional Investors (FIIs) and market index.

**H₀-5** The market has not become global and in liberalized era. It means the Indian capital market has not got more economic
significance at global level and has not created positive impact in post – liberalized era.

1.8 Methodology of the Study

With a view to achieving the objectives of the present study, the primary and secondary sources of information have been utilized.

1. The history, genesis, components, growth, performances of the capital market have been examined on the basis of secondary data like periodicals, text books, journals, reports, office records of various organizations like SEBI, RBI and ministry of finance, and different websites containing information of Indian capital market. Thus, the research work is heavily banked on the secondary source of information.

2. The actual performance and effectiveness of the Indian capital market has been examined in the light of the perception of investors and various functionaries involved in the system in regard to volatility, operating efficiency, transaction cost. For this purpose, discussions and interviews were conducted with a large number of officials and experts who are associated with the Indian capital market operation like investors and brokers.

1.9 Significance and Need of the Study

The present study aims at analyzing the overall impact of the liberalization policy of the Government on the capital market of India. Since the capital market is a very broad market and on the basis of the research gap a confined area has been studied. The study will help the researchers,
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academicians, corporations, investors, institutions and other entities which are involved directly or indirectly with the capital market operation to understand the following thing which have emerged as a matter of this research:

1. The behavioral pattern of the Foreign Institutional Investors (FIIs) who are dominating and controlling the capital market has been analysed.

2. This will help the different investors in formulating their strategies to make the best use of their capital in the market.

3. The volatility as a result of global aspects has also been analysed to help the investors to understand the global impact on the Indian capital market.

4. This study will help in knowing the profitability, liquidity, marketability and global competitiveness of the Indian capital market.

5. The study will also help the various authorities of capital market to bring further improvement in the market in regard to protect the larger interest of the small investors.

1.10 Use of Statistical Tools

The present research work is to check the impact of liberalization policy on the Indian capital market. The parameters of the Indian Capital Market like liquidity, profitability and volatility are tested by the use of t-test as the data was classified in to pre-liberalization and post-liberalization and numbers of variables were less than 30. The impact of Foreign Institutional Investments on the Sensex is tested by using the Karl Pearson's Coefficient of Correlation. Again to test the global impact, t- test is used by comparing the mean return of Indian capital market with the mean returns of other emerging Capital Markets of the world.
1.11 Scheme of Chapters

The present research work has been divided into six chapters. The first chapter deals with the introductory part and the framework of the study which includes introduction, literature review, research gap, objective, scope, methodology, hypotheses, importance of the study.

The second chapter deals with the conceptual framework of Indian Capital market including historical background, developments of the capital market in pre and post liberalized era, components, structure, mechanism and legal framework of Indian Capital Market.

The third chapter deals with the assessment of the performance of Indian Capital market in pre and post liberalization period. The numbers of important aspects of the capital market have been assessed in regard to liquidity, profitability, FII and Mutual Fund investment and their impact on the capital market. The growth and development quantitatively as well as qualitatively of the Indian capital market has also been analyzed in post liberalized era.

The fourth chapter deals with the comparison of the Indian Capital market with some other developed as well as emerging Capital Markets of the world. The various aspects like liquidity, profitability, investor’s protection index of different Capital Markets have also been studied. This chapter also covers the comparative analysis of Indian and Chinese Capital Market. The Separate analyses of some of the selected African Capital Markets have also been touched upon.
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The fifth chapters deal with the analyses and interpretation of the hypotheses of the study. The hypotheses have been tested by using suitable statistical tools and interpretations have also been made on the basis of results obtained.

The sixth chapter deals with the conclusion, findings and recommendations on the basis of the study.

1.12 Conclusion

This chapter deals with the background and Perspective Framework of the Study which includes Statement of Problems, Emerging Issues, Review of the literature, Research Gap, Scope and Objectives of the study, Hypotheses of the study, Methodology of the Study, Significance and Need of the Study, Use of Statistical Tools, Scheme of Chapters and References. After going through background and Perspective Framework of the Study, it is necessary to touch upon the conceptual Framework of the Capital Market before its assessment. The Conceptual Framework of the Capital Market is highlighted in the next chapter.
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