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Lopsided growth of industries spread across various sectors is one of the important aspects for the overall growth of GDP. Post 2003, worldwide capital markets have seen a big rise and sectors across the spectrum of industry found good amount of investments invested by Foreign Institutional Investors (FII’s) and Mutual Funds (M.F’s), Financial Institutions (F.I’s) besides domestic investors. The capital market as a whole has seen the infusion of USD 50 Billion by FII’s and equivalent amounts from various section of investors in the domestic side.

Various sectors like, Information Technology, Steel, Cement, Telecom, Real Estate, Infrastructure, Capital Goods and host of other sectors have absorbed good quantum of investments from the investors side.

Substantial academic literature and government strategies support the finance-led growth hypothesis, based on an observation first made almost a century ago by Joseph Schumpeter that financial markets significantly boost real economic growth and development.

Joseph Schumpeter asserted that finance had a positive impact on economic growth as a result of its effects on productivity growth and technological change. As early as 1991 the World Bank also endorsed the view that financial deepening matters for economic growth "by improving the productivity of investment". A number of case studies on Asia and Southern African countries show the positive nexus between development of financial instruments as a flow of funds in to various sectors of industry and economic growth.

Economic growth is also the result of the introduction of new products and services coupled with investments really taking place for the creation of production bases.

Indian corporate sector has experienced a paradigm shift over the last two decades with the initiation of certain measures of financial liberalization. Bombay stock Exchange (BSE) has the second largest number of domestic quoted companies in the world which is three times higher than China. Large Indian firms have also been permitted to directly raise capital in international capital markets through commercial borrowings and depository receipts. Various product innovations in the financial sector such as special purpose vehicles, financial derivatives, Global Depository Receipts (GDR), American Deposit Receipts (ADR), Foreign Currency Convertible Bonds (FCCBs), Foreign Currency Exchangeable Bonds (FCEBs), Private equity or venture capital have also facilitated Indian firms to raise resources under this new institutional framework. Now new players have also emerged with the entry of hedge funds and pension funds into the stock markets. Specialized credit funds and managers of collateralized debt obligations have emerged as providers of instruments.

This change is expected to have an impact on the resource mobilization of the private corporate sector in the Indian economy. According to Venture Intelligence Estimates, there are 350 PE firms exist in India. Most of them primarily focus on specific sectors such as infrastructure.
There is a strong relationship between investment and sectoral industry growth. Larger inflows of investments are needed for the country to achieve a sustainable high trajectory of economic growth. There are several irrefutable reasons for this.

For the economy to grow by 7 to 8 per cent a year there is a need to invest around 35 to 40 per cent of GDP. National savings fall far short of this by nearly 10 per cent. Foreign borrowing and foreign investments have to meet this investment-savings gap.

This is generally recognized and successive governments have attempted to provide various incentives to foreign investors. There are many conditions that have to be put in place to attract Investments into Industry and the various sectors forming part of Industry.

It is important to ensure an attractive investment climate. Consistent macroeconomic policies, good governance, economic stability, guarantee of property rights, rule of law and absence of corruption are among the conditions required to attract FDI. Consistency and predictability in economic policies and political stability are preconditions to attract Investments.

Since 2003 with the great investments flows that India has been attracting various sectors have really become like growth sectors. Various new avenues blossomed like Infrastructure Growth in the form of roads, ports, airports, power and telecom. Further some of the existing sectors continued to expand their capacities resulting into revenue growth.

More specifically investments flows into various sectors have been the growth engine for the Indian GDP growth rate on an average of above 8% to 9%.

History of Indian Capital Markets

The history of the Indian capital markets and the stock market, in particular can be traced back to 1861 when the American Civil War began. The opening of the Suez Canal during the 1860s led to a tremendous increase in exports to the United Kingdom and United States. Several companies were formed during this period and many banks came to the fore to handle the finances relating to these trades. With many of these registered under the British Companies Act, the Stock Exchange, Mumbai, came into existence in 1875. It was an unincorporated body of stockbrokers, which started doing business in the city under a banyan tree. Business was essentially confined to company owners and brokers, with very little interest evinced by the general public. There had been much fluctuation in the stock market on account of the American war and the battles in Europe. Sir Premchand Roychand remained a kingpin for many years.

Sir Phiroze Jeejeebhoy was another who dominated the stock market scene from 1946 to 1980. His word was law and he had a great deal of influence over both brokers and the government. He was a good regulator and many crises were averted due to his wisdom and practicality. The BSE building, icon of the Indian capital markets, is called P.J. Tower in his memory.
The planning process started in India in 1951, with importance being given to the formation of institutions and markets. The Securities Contract Regulation Act 1956 became the parent regulation after the Indian Contract Act 1872, a basic law to be followed by security markets in India. To regulate the issue of share prices, the Controller of Capital Issues Act (CCI) was passed in 1947.

The stock markets have had many turbulent times in the last 140 years of their existence. The imposition of wealth and expenditure tax in 1957 by Mr. T.T. Krishnamachari, the then finance minister, led to a huge fall in the markets. The dividend freeze and tax on bonus issues in 1958-59 also had a negative impact. War with China in 1962 was another memorably bad year, with the resultant shortages increasing prices all round. This led to a ban on forward trading in commodity markets in 1966, which was again a very bad period, together with the introduction of the Gold Control Act in 1963 and this led to a resurgence of interest in the capital markets, only to be punctured by the Harshad Mehta scam in 1992.

The mid-1990s saw a rise in leasing company shares, and hundreds of companies, mainly listed in Gujarat, and got listed in the BSE. The end-1990s saw the emergence of Ketan Parekh and the information; communication and entertainment companies came into the limelight. This period also coincided with the dotcom bubble in the US, with software companies being the most favored stocks. There was a meltdown in software stock in early 2000. Mr. P Chidambaram continued the liberalization and reform process, opening up of the companies, lifting taxes on long-term gains and introducing short-term turnover tax. The markets have recovered since then and we have witnessed a sustained rally that has taken the index over 13000.

Several systemic changes have taken place during the short history of modern capital markets. The setting up of the Securities and Exchange Board (SEBI) in 1992 was a landmark development. It got its act together, obtained the requisite powers and became effective in early 2000. The setting up of the National Stock Exchange in 1984, the introduction of online trading in 1995, the establishment of the depository in 1996, trade guarantee funds and derivatives trading in 2000, have made the markets safer. The introduction of the Fraudulent Trade Practices Act, Prevention of Insider Trading Act, Takeover Code and Corporate Governance Norms, are major developments in the capital markets over the last few years that has made the markets attractive to foreign institutional investors.

This history shows us that retail investors are yet to play a substantial role in the market as long-term investors. Retail participation in India is very limited considering the overall savings of households. Investors who hold shares in limited companies and mutual fund units are about 20-30 million. Those who participated in secondary markets are 2-3 million.

Capital markets will change completely if they grow beyond the cities and stock exchange centers reach the Indian villages. Both SEBI and retail participants should be active in spreading

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market wisdom and empowering investors in planning their finances and understanding the markets.

**India - Capital Markets**

Indian Capital market has witnessed a paradigm shift at par with the advanced markets of the world in the last 10 years or so. Business process, functionality, monitoring / regulating mechanisms, hardware, software etc., are all revamped to compete with the global leaders. The current stand of Indian capital market has a long history in its back. The history of the capital market in India dates back to the eighteenth century when East India Company securities were traded in the country. In 1850s, the trading was limited to a dozen brokers and their trading place was under a banyan tree in front of the Town Hall in Bombay. The location of trading changed many times, as the number of brokers constantly increased. The group eventually moved to Dalal Street in 1874 and in 1875 became an official organization known as 'The Native Share & Stock Brokers Association'. In 1895, this association acquired a premise in the Dalal Street and it was inaugurated in 1899. Thus, the Stock exchange at Bombay was consolidated. And, the orderly growth of the capital market in India began.

The Bombay stock exchange got recognition in May 1927 under the Bombay Securities Contracts Control Act, 1925. The constitution of India came into being on 26th January, 1950. The constitution put the stock exchanges and the forward markets under the exclusive authority of the Government of India. In 1956, the BSE became the first stock exchange to be recognized by the Indian Government under the Securities Contracts (Regulation) Act. The 1980s witnessed an explosive growth of the securities market in India, with millions of investors suddenly discovering lucrative opportunities. Many investors jumped into the stock markets for the first time. The government's liberalization process initiated during the mid-1980s, spurred this growth. The Bombay Stock Exchange developed the BSE Sensex in 1986, giving the BSE a means to measure overall performance of the exchange.

The 1990s will go down as the most important decade in the history of the capital market of India. The Capital Issues (Control) Act, 1947 was repealed in May 1992. The decade was characterized by a new industrial policy, emergence of SEBI as a regulator of capital market, advent of foreign institutional investors, euro-issues, free pricing, new trading practices, new stock exchanges, entry of new players such as private sector mutual funds and private sector banks, and primary market boom and bust. The 1991-92 securities scam revealed the inadequacies of and inefficiencies in the financial system. It was the scam which prompted a reform of the equity market.

The Indian stock market witnessed a sea change in terms of technology and market prices. Technology brought radical changes in the trading mechanism. The Bombay Stock Exchange (BSE) was subject to nationwide competition by two new stock exchanges – the National Stock Exchange (NSE), set up in 1994, and Over the Counter Exchange of India (OTCEI), set up in 1992. The National Securities Clearing Corporation (NSCC) and National Securities Depository...
Limited (NSDL) were set up in April 1995 and November 1996 respectively form improved clearing and settlement and dematerialized trading. The Securities Contracts (Regulation) Act, 1956 was amended in 1995-96 for introduction of options trading. Moreover, rolling settlement was introduced in January 1998 for the dematerialized segment of all companies. With automation and geographical spread, stock market participation increased.

In 1996, the National Stock Exchange of India launched S&P CNX Nifty and CNX Junior Indices that make up 100 most liquid stocks in India. CNX Nifty is a diversified index of 50 stocks from 25 different economy sectors. The Indices are owned and managed by India Index Services and Products Ltd (IISL) that has a consulting and licensing agreement with Standard & Poor's. In 1998, the National Stock Exchange of India launched its web-site and was the first exchange in India that started trading stock on the Internet in 2000. The NSE has also proved its leadership in the Indian financial market by gaining many awards such as 'Best IT Usage Award' by Computer Society in India (in 1996 and 1997) and CHIP Web Award by CHIP magazine (1999).

In 2000 the BSE used the sensitive index, i.e., Sensex to open its derivatives market, trading Sensex futures contracts. The development of Sensex options along with equity derivatives followed in 2001 and 2002, expanding the BSE's trading platform. The introduction of rolling settlement system in all scrips and electronic fund transfer in 2003 reduced the settlement cycle to T+2.

Indian capital market in 2007-08, thus, features a developed regulatory environment, a modern market infrastructure, a steadily increasing market capitalization and liquidity, better allocation and mobilization of resources, a rapidly developing derivatives market, a robust mutual fund industry, and increased issuer transparency. However, in the last quarter of 2008 and up to the first quarter of 2009, the capital market went through a phase of downsizing due to the direct impact of global financial crisis that originated from the USA sub-prime mortgage market. Indian capital market has seen its worst time with the global financial crisis. The most popular stock index, i.e., Sensex declined to its levels attained in December 2005. Similar decline has also been noticed for S & P CNX Nifty index.

A. Market Size

The size of a capital market as measured by stock market capitalization is positively correlated with the ability to mobilize capital and diversify risk on an economy-wide basis. The size of the Indian capital market can be assessed by employing the stock market capitalization to GDP ratio. This size ratio of Indian capital market is shown in the Table given below. It is seen that the market size of Indian capital market is increasing over the years except in 2008-09. The decline in 2008-09 in market size is the effect of global financial crisis on Indian capital market. Thus, the overall indication is that in India the size of capital market is expanding which is the signal for strong potential of the market to mobilize capital for the economic development of the country.
B. Market Liquidity

Market Liquidity refers to the ability to buy and sell securities easily. Liquid capital market allows companies on the one hand, to have a permanent access to capital through equity issues and on the other hand, to allow investors to switch out of equity if they need to access funds or if they want to change the composition of their portfolios. The market liquidity is measured by the ratio of total value of shares traded to GDP. The liquidity ratio in Indian capital market on BSE ranges between 14.16% on the minimum and 33.42% at the maximum. Whereas on NSE it ranges between a mini-max of 27.87% and 72.72% respectively.

The overall performance of the range of percentages indicates that the Indian capital market is liquid and in particular the liquidity of NSE India is quite higher than that of Stock Exchange, Mumbai.

C. Market Turnover

The market turnover gives the total value of shares traded in relation to the size of the market. It is the most important indicator of market activity. It is calculated as the ratio of total value of shares traded to the market capitalization. The turnover ratio is also the indication of market liquidity. This ratio for Indian capital market on BSE touched a peak of 54.88% and also touched a bottom of 2.3% in 2008-09 during Global Financial Crisis. On NSE the peak rate ratio was 115.05% and low of 6.17% in 2008-09.

D. Market Efficiency

The term 'market efficiency' is used to explain the relationship between information and share prices in the capital market literature. An efficient capital market is commonly thought of as a market in which security prices fully reflect all relevant information that is available about the fundamental value of the securities. An efficient market is defined as a market in which prices always reflect the recent available information and states that three different levels of efficiency exist based on what is meant as 'available information' — the weak, semi-strong, and strong forms. Weak form efficiency exists when security prices reflect all the information contained in the history of past prices and returns. If capital markets are weak-form efficient, then investors can not earn super-normal profits (excess profits) from trading strategies based on past prices or returns. Therefore, stock returns are not predictable, and hence follow a random walk. Under semi-strong form efficiency, security prices reflect all publicly available information. Investors, who base all their decisions on the information that becomes public, cannot gain above-average returns. Under strong form efficiency, all information - even apparent company secrets — is incorporated in security prices and thus, no investor can earn excess profit by trading on public or non-public information.
Indian Capital Market – An Overview

There are 22 stock exchanges in India, the first being the Bombay Stock Exchange (BSE), which began formal trading in 1875, making it one of the oldest in Asia. Over the last few years, there has been a rapid change in the Indian securities market, especially in the secondary market. Advanced technology and online-based transactions have modernized the stock exchanges. In terms of the number of companies listed and total market capitalization, the Indian equity market is considered large relative to the country’s stage of economic development.

After a period of sustained growth, the Indian capital markets suffered a slowdown due to the global financial crisis. However, since early 2009, the markets have recovered. Indices have gained over 80 per cent, and market cap has more than doubled, making India one of the top performing markets.

Indian market confirms to best international practices and standards both in terms of structure and in terms of operating efficiency. Indian securities markets are mainly governed by:

a) The Company's Act 1956,

b) The Securities Contracts (Regulation) Act 1956 (SCRA Act) and


The Indian securities market consists of primary (new issues) as well as secondary (stock) market in both equity and debt. The primary market provides the channel for sale of new securities, while the secondary market deals in trading of securities previously issued.

The issuers of securities issue (create and sell) new securities in the primary market to raise funds for investment. They do so either through public issues or private placement. There are two major types of issuers who issue securities. The corporate entities issue mainly debt and equity instruments (shares, debentures, etc.), while the governments (central and state governments) issue debt securities (dated securities, treasury bills).

The secondary market enables participants who hold securities to adjust their holdings in response to changes in their assessment of risk and return. A variant of secondary market is the forward market, where securities are traded for future delivery and payment in the form of futures and options.

The futures and options can be on individual stocks or basket of stocks like index. Two exchanges, namely National Stock Exchange (NSE) and the Stock Exchange, Mumbai (BSE) provide trading of derivatives in single stock futures, index futures, single stock options and index options.
Foreign Institutional Investment in India

The liberalization and consequent reform measures have drawn the attention of foreign investors leading to a rise in portfolio investment in the Indian capital market. Over the recent years, India has emerged as a major recipient of portfolio investment among the emerging market economies. Apart from such large inflows, reflecting the confidence of cross-border investors on the prospects of Indian securities market, except for one year, India received positive portfolio inflows in each year. The stability of portfolio flows towards India is in contrast with large volatility of portfolio flows in most emerging market economies.

The Indian capital market was opened up for foreign institutional investors (FIIs) in 1992. The FIIs started investing in Indian markets in January 1993. The Indian corporate sector has been allowed to tap international capital markets through American Depository Receipts (ADRs), Global Depository Receipts (GDRs), Foreign Currency Convertible Bonds (FCCBs) and External Commercial Borrowings (ECBs). Similarly, non-resident Indians (NRIs) have been allowed to invest in Indian companies. FIIs have been permitted in all types of securities including Government securities and they enjoy full capital convertibility.

Mutual funds have been allowed to open offshore funds to investing equities abroad. FII investment in India started in 1993, as FIIs were allowed to invest in the Indian debt and equity market in line with the recommendations of the High-Level Committee on Balance of Payments. These investment inflows have since then been positive, with the exception of 1998-99, when capital flows to emerging market economies were affected by contagion from the East Asian crisis. These investments account for over 10 per cent of the total market capitalization of the Indian stock market.

Recent trends in the global capital markets:

Several current trends will continue to influence the world’s financial markets long after the present bout of turbulence ends.

Struggling credit markets, slumping stocks, and a sliding dollar generated anxiety among executives and policy makers in early 2008. Amid the turmoil, it’s easy to forget that long-term structural change in the world’s capital markets will probably prove more important than short-term fluctuations, as it did after the 1987 US stock market crash, the 1992 assault on the British pound, and the 1997 unraveling of Asia’s financial markets.

The following points highlight several trends that look set to continue during the years ahead, long after the present bout of market turbulence has ended:
CHAPTER-I: INTRODUCTION TO INDIAN CAPITAL MARKETS

- the continued growth and deepening of global capital markets as investors pour more money into equities, debt securities, bank deposits, and other assets around the world.

- the soaring growth of financial markets in emerging economies and the growing ties between financial markets in developed and developing countries.

- the shift of financial weight in Asia from Japan towards China and other fast-growing emerging markets.

- the growing financial clout of the euro zone countries and the significance of the euro.

- the burgeoning role of oil-rich Middle Eastern countries as suppliers of capital to the world, along with the rise of new financial hubs in the Middle East to complement the rapidly growing hubs in London and Asia.

While these trends reflect a shift in financial power from the United States toward other parts of the world, the sheer size and depth of the US market will give it a leading role on the international financial stage for years to come.

The continued growth of global financial assets

The full fallout from the credit market volatility of 2007 remains yet to be seen. But over the longer term, the volume of global financial assets (the value of all bank deposits, government debt securities, corporate debt securities, and equity securities) will continue to expand. Over the past 25 years, through stable and stormy times alike, financial assets have grown robustly. In 2006, their value rose to USD 167 trillion, from USD 142 trillion the year before—a 17 per cent increase, more than double the average annual growth rate (8 per cent) from 1995 through 2005.

For many years, as equity and bond markets thrived, bank deposits have accounted for a shrinking share of total financial assets. That trend continued in 2006, but the rate of decline slowed because the absolute value of bank deposits around the world jumped by USD 5.6 trillion—twice the average increase of the previous three years. The largest contributor to this rise was the United States, thanks largely to strong income growth and the housing boom, which enabled many households to tap their home equity for quick cash. This source of growth was shaky by 2007. Looking forward, the growth of deposits will depend to a large degree on China, where they are the primary savings vehicle.

Growing cross-border investment links financial markets

The rising level of foreign investment is making the world more financially inter-dependent than it was even a few years ago. By the end of 2006, the outstanding stock of cross-border investments reached the highest level, in real terms, in history—USD 74.5 trillion of assets. This sum includes the foreign investments of multinational corporations, purchases of foreign debt...
and equity securities by investors around the world, and foreign lending and deposits. Preliminary data indicate that the total grew to another record level in 2007, despite the disruptions in European and US credit markets during the second half of the year.

What's more, the source and direction of cross-border investment flows are shifting. In 1999, the United States was the dominant hub of the global financial system. By 2006, it remained the largest single foreign investor and a major hub in global capital markets—but the euro zone countries together had as many financial links with other parts of the world, including emerging markets.

The United Kingdom too has become a more significant global financial hub, and Middle Eastern countries are now major investors in global financial markets, thanks to the windfall generated by rising oil prices. In 2006, for the first time since the 1970s, the oil-exporting countries joined those of East Asia as the world's largest net suppliers of capital.

The Indian financial system has undergone structural transformation over the past decade. The financial sector has acquired strength, efficiency and stability by the combined effect of competition, regulatory measures, and policy environment.

While competition, consolidation and convergence have been recognized as the key drivers of the banking sector in the coming years, consolidation of the domestic banking system in both public and private sectors is being combined with gradual enhancement of the presence of foreign banks in a calibrated manner.

There has been improvement in banks' capital position and asset quality as reflected in the overall increase in their capital adequacy ratio and declining NPLs, respectively. Significant improvement in various parameters of efficiency, especially intermediation costs, suggests that competition in the banking industry has intensified. The efficiency of various segments of the financial system also increased.

The major challenges facing the banking sector are the judicious deployment of funds and the management of revenues and costs. Concurrently, the issues of corporate governance and appropriate disclosures for enhancing market discipline have received increased attention for ensuring transparency and greater accountability.

Financial sector supervision is increasingly becoming risk based with the emphasis on quality of risk management and adequacy of risk containment. Consolidation, competition and risk management are no doubt critical to the future of Indian banking, but governance and financial inclusion have also emerged as the key issues for the Indian financial system.

The capital market in India has become efficient and modern over the years. It has also become much safer. However, some of the issues would need to be addressed. Corporate governance needs to be strengthened.

Retail investors continue to remain away from the market. The private corporate debt market continues to lag behind the equity segment.
Foreign Institutional Investors

India, which is the second fastest growing economy after China, has lately been a major recipient of foreign institutional investor (FII) funds driven by the strong fundamentals and growth opportunities.

According to analysts, the late revival of monsoon, upward revision of economic growth from 5.8 per cent to 6.1 per cent, better-than-expected performance of companies in the quarter ended-June 30, the new direct taxes code, leading to savings in the tax payer’s money, and the trade policy with an ambitious target of US$ 200 billion exports for 2010-11 have all revived the confidence of FII's investing in India.

Both consumption and investment-led industries linked to domestic demand, such as auto, banking, capital goods, infrastructure and retail, are likely to continue attracting FII funds.

FIIs have made net investments of US$ 10 billion in the first six months (April to September) of 2009-10. Major portion of these investments have come through the primary market, more than through buying via secondary markets.

Earlier, FIIs' net investments in Indian equities crossed the US$ 8 billion-mark in calendar 2009, the first time in this year, with foreigners buying stocks worth US$ 274 million on August 28, 2009. With FIIs holding 16 per cent of India's biggest 500 companies and increasing growth of the economy, the FII sentiment is expected to remain positive towards India. At the end of July 2009, net inflows from FIIs stood at US$ 7.3 billion.

Along with construction, the market cap of FII investment in infrastructure and heavy engineering has also risen, largely due to higher government spending and leveraged investment by companies in these sectors. In heavy engineering, FII market cap has gone up 202 per cent and in steel, it was up 274 per cent in the past six months.

In the previous April-June quarter, initial signs of recovery in world economies, a stable government in New Delhi and the positive impact of its stimulus packages substantially improved the sentiments of FIIs.

Real estate, banking and finance, engineering and oil and gas—garnered almost three-fourths of the money invested by FIIs. These four sectors accounted for over 71 per cent of the total FII investment at US$ 4.55 billion during the quarter.

Researcher: CVSL Kameswari
Government Initiatives

India’s foreign investment policies allow foreign direct investment up to 26 per cent and foreign institutional investments of (an additional) 23 per cent in stock exchanges. Under the regulation, FIIIs have been allowed to acquire shares of unlisted stock exchanges through transactions outside a recognized stock exchange provided it is not an initial allotment of shares.

The Reserve Bank of India (RBI) and the Securities and Exchange Board of India (SEBI) have jointly unveiled norms enabling exchange-traded interest rate futures (IRF). Foreign portfolio investors have been allowed to trade in IRFs, but limits have been put in place to keep their influence under check.

FIIIs and the non-resident Indians (NRIs) are allowed to invest in Indian Depository Receipts (IDRs), according to the operational guidelines issued by the RBI on July 22, 2009.

Importance of Capital Markets

Capital market plays an important role in mobilising resources, and diverting them in productive channels. In this way, it facilitates and promotes the process of economic growth in the country.

Various functions and significance of capital market are discussed below:

1. Link between Savers and Investors

The capital market functions as a link between savers and investors. It plays an important role in mobilising the savings and diverting them in productive investment. In this way, capital market plays a vital role in transferring the financial resources from surplus and wasteful areas to deficit and productive areas, thus increasing the productivity and prosperity of the country.

2. Encouragement to Saving

With the development of capital, market, the banking and non-banking institutions provide facilities, which encourage people to save more. In the less-developed countries, in the absence of a capital market, there are very little savings and those who save often invest their savings in unproductive and wasteful directions, i.e., in real estate (like land, gold, and jewellery) and conspicuous consumption.

3. Encouragement to Investment

The capital market facilitates lending to the businessmen and the government and thus encourages investment. It provides facilities through banks and nonbank financial institutions. Various financial assets, e.g., shares, securities, bonds, etc., induce savers to lend to the government or invest in industry. With the development of financial institutions, capital becomes more mobile, interest rate falls and investment increases.
CHAPTER-I: INTRODUCTION TO INDIAN CAPITAL MARKETS

4. Promotes Economic Growth
The capital market not only reflects the general condition of the economy, but also smoothens and accelerates the process of economic growth. Various institutions of the capital market, like nonbank financial intermediaries, allocate the resources rationally in accordance with the development needs of the country. The proper allocation of resources results in the expansion of trade and industry in both public and private sectors, thus promoting balanced economic growth in the country.

5. Stability in Security Prices
The capital market tends to stabilise the values of stocks and securities and reduce the fluctuations in the prices to the minimum. The process of stabilisation is facilitated by providing capital to the borrowers at a lower interest rate and reducing the speculative and unproductive activities.

6. Benefits to Investors
The credit market helps the investors, i.e., those who have funds to invest in long-term financial assets, in many ways:

a) It brings together the buyers and sellers of securities and thus ensures the marketability of investments,

b) By advertising security prices, the Stock Exchange enables the investors to keep track of their investments and channelize them into most profitable lines,

c) It safeguards the interests of the investors by compensating them from the Stock Exchange Compensating Fund in the event of fraud and default.

The role of capital markets in an economy

- Provides an important alternative source of long-term finance for long-term productive investments. This helps in diffusing stresses on the banking system by matching long-term investments with long-term capital.

- Provides equity capital and infrastructure development capital that has strong socio-economic benefits - roads, water and sewer systems, housing, energy, telecommunications, public transport, etc. - ideal for financing through capital markets via long dated bonds and asset backed securities.

- Provides avenues for investment opportunities that encourage a thrift culture critical in increasing domestic savings and investment ratios that are essential for rapid industrialization. The Savings and investment ratios are too low, below 10% of GDP.
CHAPTER-I: INTRODUCTION TO INDIAN CAPITAL MARKETS

- Encourages broader ownership of productive assets by small savers to enable them benefit from India’s economic growth and wealth distribution. Equitable distribution of wealth is a key indicator of poverty reduction.

- Promotes public-private sector partnerships to encourage participation of private sector in productive investments. Pursuit of economic efficiency shifting driving force of economic development from public to private sector to enhance economic productivity has become inevitable as resources continue to diminish.

- Assists the Government to close resource gap, and complement its effort in financing essential socio-economic development, through raising long-term project based capital.

- Improves the efficiency of capital allocation through competitive pricing mechanism for better utilization of scarce resources for increased economic growth.

- Provides a gateway to India for global and foreign portfolio investors, which is critical in supplementing the low domestic saving ratio.

Problems faced by various sectors in the Industry

The constraints or problems for balanced sectoral growth in the Industry Development in India are numerous to say, but some of the major issues can be outlined as mentioned here under:-

They are:-

1. Lack of Entrepreneurship
2. Inadequate Infrastructure
3. Paucity of Financial Resources

The above constraints can be elucidated in detail

Lack of Entrepreneurship

Presence of ample entrepreneurial ability is a sine-qua-non of industrial progress. Whereas finance mobilizes the industrial resources of any area of the centre of production, entrepreneurship acts as the drive of the vehicle of industrial development. Without entrepreneurship all the constituents of industrialization will remain inactive because they cannot be assembled together for actual manufacture.

Development of entrepreneurship may be a practical approach. Barriers to entrepreneurship and its diffusion can be overcome through institutional innovations and programming so that existing potentials are translated into reality.
Inadequate Infrastructure
The social and economic overheads are one of the basic factors which determine the pace of sectoral growth and industrialization. The cost of industrial projects includes the social and economic costs also.

The social and economic overheads for an industrial project are determined on the basis of infrastructure developed to facilitate the development of the project. The infrastructure includes the road and transport facilities, provision for gas, water and electricity, availability of insurance, banking and other commercial services, etc.

These facilities reduce the cost of establishing an industrial project and these costs are termed as social costs. For any balanced sectoral industrial growth these facilities are very much essential.

Paucity of Financial Resources
Private capital in India has remained extremely shy for centuries and only a limited number of entrepreneurs have come forward with their capital for the development of Industry. Growth results from a high rate of capital formation.

For net addition to capital stock, savings from capital income is a central factor. This means not only a high saving ratio, in various sectors appropriate growth but massive capital is also required for long term growth of each sector forming part of Industry.

Indian Economy
India economy, the third largest economy in the world, in terms of purchasing power, is going to touch new heights in coming years.

As predicted by Goldman Sachs, the Global Investment Bank, by 2035 India would be the third largest economy of the world just after US and China. It will grow to 60% of size of the US economy.

This booming economy of today has to pass through many phases before it can achieve the current milestone of 9% GDP.

The history of Indian economy can be broadly divided into three phases: Pre- Colonial, Colonial and Post Colonial.

Pre Colonial: The economic history of India since Indus Valley Civilization to 1700 AD can be categorized under this phase. During Indus Valley Civilization Indian economy was very well developed. It had very good trade relations with other parts of world, which is evident from the coins of various civilizations found at the site of Indus valley.
Before the advent of East India Company, each village in India was a self sufficient entity. Each village was economically independent as all the economic needs were fulfilled with in the village.

Then came the phase of Colonization. The arrival of East India Company in India ruined the Indian economy. There was a two-way depletion of resources. British used to buy raw materials from India at cheaper rates and finished goods were sold at higher than normal price in Indian markets. During this phase India's share of world income declined from 22.3% in 1700 AD to 3.8% in 1952.

After India got independence from this colonial rule in 1947, the process of rebuilding the economy started. For this various policies and schemes were formulated. First five year plan for the development of Indian economy came into implementation in 1952. These Five Year Plans, started by Indian government, focused on the needs of Indian economy.

If on one hand agriculture received the immediate attention on the other side industrial sector was developed at a fast pace to provide employment opportunities to the growing population and to keep pace with the developments in the world. Since then Indian economy has come a long way. The Gross Domestic Product (GDP) at factor cost, which was 2.3 % in 1951-52, reached 9% in financial year 2005-06.

Trade liberalization, financial liberalization, tax reforms and opening up to foreign investments were some of the important steps, which helped Indian economy to gain momentum. The Economic Liberalization introduced by Man Mohan Singh in 1991, then Finance Minister in the government of P V Narsimha Rao, proved to be the stepping-stone for Indian economic reform movements.

To maintain its current status and to achieve the target GDP of 10% for financial year 2006-07, Indian economy has to overcome many challenges.

Challenges before Indian economy

Population explosion
This monster is eating up into the success of India. According to 2001 census of India, population of India in 2001 was 1,028,610,328, growing at a rate of 2.11% approx. Such a vast population puts lots of stress on economic infrastructure of the nation. Thus India has to control its burgeoning population.

Poverty
As per records of National Planning Commission, 36% of the Indian population was living Below Poverty Line in 1993-94. Though this figure has decreased in recent times but some major steps are needed to be taken to eliminate poverty from India.
Unemployment

The increasing population is pressing hard on economic resources as well as job opportunities. Indian government has started various schemes such as Jawahar Rozgar Yojna and Self Employment Scheme for Educated Unemployed Youth (SEEUY). But these are proving to be a drop in an ocean.

Rural urban divide

It is said that India lies in villages, even today when there is lots of talk going about migration to cities, 70% of the Indian population still lives in villages. There is a very stark difference in pace of rural and urban growth. Unless there isn't a balanced development Indian economy cannot grow.

These challenges can be overcome by the sustained and planned economic reforms. These include:

- Maintaining fiscal discipline
- Orientation of public expenditure towards sectors in which India is faring badly such as health and education.
- Introduction of reforms in labor laws to generate more employment opportunities for the growing population of India.
- Reorganization of agricultural sector, introduction of new technology, reducing agriculture's dependence on monsoon by developing means of irrigation.
- Introduction of financial reforms including privatization of some public sector banks.

GDP Growth – Actual & Projected

<table>
<thead>
<tr>
<th></th>
<th>2000</th>
<th>2001</th>
<th>2002</th>
<th>2003</th>
<th>2004</th>
<th>2005</th>
</tr>
</thead>
<tbody>
<tr>
<td>Growth</td>
<td>4.4%</td>
<td>3.9%</td>
<td>4.6%</td>
<td>6.9%</td>
<td>8.1%</td>
<td>9.2%</td>
</tr>
</tbody>
</table>

Table 1: GDP Growth rate - Actual

India GDP growth rate spiraled up from 2003 onwards. An Analysis of GDP Component's was presented from 2005-06 to 2010-11 on Actual basis and 2011-12 on projected basis.
### CHAPTER-I: INTRODUCTION TO INDIAN CAPITAL MARKETS

#### ANNUAL RATES

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<th></th>
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</tr>
</thead>
<tbody>
<tr>
<td><strong>Agriculture &amp; allied activities</strong></td>
<td>5.1</td>
<td>4.2</td>
<td>5.8</td>
<td>-0.1</td>
<td>0.4</td>
<td>6.6</td>
<td>3.0</td>
</tr>
<tr>
<td><strong>Mining &amp; Quarrying</strong></td>
<td>1.3</td>
<td>7.5</td>
<td>3.7</td>
<td>1.3</td>
<td>6.9</td>
<td>5.8</td>
<td>6.0</td>
</tr>
<tr>
<td><strong>Manufacturing</strong></td>
<td>10.1</td>
<td>14.3</td>
<td>10.3</td>
<td>4.2</td>
<td>8.8</td>
<td>8.3</td>
<td>7.0</td>
</tr>
<tr>
<td><strong>Electricity, Gas &amp; Water Supply</strong></td>
<td>7.1</td>
<td>9.3</td>
<td>8.3</td>
<td>4.9</td>
<td>6.4</td>
<td>5.7</td>
<td>7.0</td>
</tr>
<tr>
<td><strong>Construction</strong></td>
<td>12.8</td>
<td>10.3</td>
<td>10.7</td>
<td>5.4</td>
<td>7.0</td>
<td>8.1</td>
<td>7.5</td>
</tr>
<tr>
<td><strong>Trade, Hotels, Transport, Storage &amp; Communication</strong></td>
<td>12.2</td>
<td>11.6</td>
<td>11</td>
<td>7.5</td>
<td>9.7</td>
<td>10.3</td>
<td>10.8</td>
</tr>
<tr>
<td><strong>Finance, insurance, real estate &amp; business services</strong></td>
<td>12.7</td>
<td>14</td>
<td>11.9</td>
<td>12.5</td>
<td>9.2</td>
<td>9.9</td>
<td>9.8</td>
</tr>
<tr>
<td><strong>Community &amp; Personal Services</strong></td>
<td>7.0</td>
<td>2.9</td>
<td>6.9</td>
<td>12.7</td>
<td>11.8</td>
<td>7.0</td>
<td>8.5</td>
</tr>
<tr>
<td><strong>Gross Domestic Product (factor Cost)</strong></td>
<td><strong>9.5</strong></td>
<td><strong>9.6</strong></td>
<td><strong>9.3</strong></td>
<td><strong>6.8</strong></td>
<td><strong>8</strong></td>
<td><strong>8.5</strong></td>
<td><strong>8.2</strong></td>
</tr>
<tr>
<td><strong>Industry (2+3+4+5)</strong></td>
<td>9.7</td>
<td>12.2</td>
<td>9.7</td>
<td>4.4</td>
<td>8</td>
<td>7.9</td>
<td>7.1</td>
</tr>
<tr>
<td><strong>Services (6+7+8)</strong></td>
<td>11</td>
<td>10.1</td>
<td>10.3</td>
<td>10.1</td>
<td>10.1</td>
<td>9.4</td>
<td>10</td>
</tr>
<tr>
<td><strong>Non- agriculture (9-1)</strong></td>
<td>10.5</td>
<td>10.8</td>
<td>10.1</td>
<td>8.2</td>
<td>9.4</td>
<td>8.9</td>
<td>9.0</td>
</tr>
<tr>
<td><strong>GDP (factor cost) per capita</strong></td>
<td><strong>7.8</strong></td>
<td><strong>7.8</strong></td>
<td><strong>7.6</strong></td>
<td><strong>5.0</strong></td>
<td><strong>6.2</strong></td>
<td><strong>6.8</strong></td>
<td><strong>6.4</strong></td>
</tr>
</tbody>
</table>

#### Some Magnitudes

- GDP at factor cost-2004/05 Prices in Rs Lakh crore(or Trillion): 32.5, 35.7, 39.0, 41.6, 44.9, 48.8, 52.8
- GDP market & current prices in Rs lakh Crore (or Trillion): 36.9, 42.9, 49.9, 55.8, 65.5, 78.8, 89.8

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Researcher: CVSL Kameswari
Table 2: YEAR-ON-YEAR RATES OF GROWTH IN %

<table>
<thead>
<tr>
<th>ANNUAL RATES</th>
<th>YEAR-ON-YEAR RATES OF GROWTH IN PER CENT</th>
</tr>
</thead>
<tbody>
<tr>
<td>GDP market &amp; Current prices</td>
<td>834 949 1241 1223 1385 1732 1994</td>
</tr>
<tr>
<td>Population in Million</td>
<td>1108 1126 1145 1164 1183 1202 1222</td>
</tr>
<tr>
<td>GDP market Prices per Capita current prices</td>
<td>33317 38117 43554 47975 55384 65517 73460</td>
</tr>
<tr>
<td>GDP market prices per capita in current US$</td>
<td>753 842 1084 1051 1171 1441 1632</td>
</tr>
</tbody>
</table>

When we take a look at the GDP numbers that Government of India released, the highlights of the same reveals the fact that Capital Formation as the Key for the Growth.

**Important highlights of Economic Outlook 2010-11**

**Agriculture** grew at 6.6% in 2010-11.

**Industry** grew at 7.9% in 2010-11.

**Services** grew at 9.4% in 2009-10.

**Investment rate** projected at 36.4% in 2010-11 and 36.7% in 2011-12

**Domestic savings rate** as ratio of GDP projected at 33.8% in 2010-11 & 34.0% in 2011-12

**Current Account deficit** is $44.3 billion (2.6% of GDP) in 2010-11 and projected at $54.0 billion (2.7% of GDP) in 2011-12

**Merchandise trade deficit** is $130.5 billion or 7.59% of the GDP in 2010-11 and projected at $154.0 billion or 7.7% of GDP in 2011-12

**Invisibles trade surplus** is $86.2 billion or 5.0% of the GDP in 2010-11 and projected at $100.0 billion or 5.0% in 2011-12

**Capital flows** at $61.9 billion in 2010-11 and projected at $72.0 billion in 2011-12

**FDI inflows** projected at $35 billion in 2011/12 against the level of $23.4 billion in 2010-11

**FII inflows** projected to be $14 billion which is less than half that of the last year i.e. $30.3 billion
Accretion to reserves was $15.2 billion in 2010-11. Projected at $18.0 billion in 2011-12.

Inflation rate would continue to be at 9 per cent in the month of July-October 2011. There will be some relief starting from November and will decline to 6.5% in March 2012.

The most important aspects of the Highlights is Capital flows standing at USD 61.9 billion in 2010-11, where as FDI inflows at USD 23.4 Billion and FII Inflows at USD 30.3 Billion and Accretion to Reserves to the tune of USD 15.2 Billion for the same year, when the domestic savings rate as a ratio of GDP stands at approximately 36.4%.

Also significant to note from the GDP numbers is the fact that the major economic growth components of India are Industry and Services Sector, almost contributing to the extent of 75% of our economy on annualized basis.
An Overview of Theoretical and Empirical Literature Survey

Literature review provides, no evidence of any similar study done on, "India Capital Markets – Sectoral Growth Led by Investments".

However to make the research direction more definite and specific and to serve a stimulus to the advance of the researcher's own thoughts and ideas, Literature review has been conducted extensively and the findings of the literature review are mentioned as below:

In the year 1994 Research on the Indian Capital Market: A Review was conducted by Samir K. Barua, V. Raghunathan, Jayanth R. Varma at Indian Institute of Management-Ahmedabad, In this paper a review of research done in the field of Indian capital markets during the fifteen years from 1977 to 1992.

The research works included in the survey were identified by two search procedures. Firstly, 118 Indian university departments and research institutions, requesting information on the works done in this field in their department/institution. After three reminders, the researches obtained responses from 53 institutions.

Simultaneously, they also searched through various Indian journals in library, located books listed in the library catalogue and traced through the list of references provided in various research works.

A Research Paper was published in 1996 in Economic and Political Weekly with a title of India's Capital Market Growth by R.Nagaraj. The study documented India's capital market boom and its proximate causes.

What does it mean for the economy and private corporate sector? It is largely disintermediation, household sector substituted 'shares and debentures' for bank deposits, and corporate sector securitized debt. The study covered the period up to 1995 by leaving many questions? Some which are targeted towards creation of liquidity and governance.

Role of FIs in Indian Capital Market, P.K. Mishra, Institute of Technical Education and Research (ITER) in the year 2009, as a part of his research study observed that Until the 1980s, there was a general disinclination towards foreign investment or private commercial flows as India's development strategy was focused on self-reliance and import substitution and current account deficits were financed largely through debt flows and official development assistance.

After the launch of the reforms, Foreign Institutional Investors (FIIs) have been allowed to invest in all securities traded on the primary and secondary markets, including shares, debentures and warrants issued by companies which were listed or were to be listed on the Stock Exchanges in India and in schemes floated by domestic mutual funds.

Researcher: CVSL Kameswari
From September 14, 1992, with suitable restrictions, FIs were permitted to invest in financial instruments. Since then foreign portfolio inflows through FIs, in India, have been important from the policy perspective, especially when the country has emerged as one of the most attractive investment destinations in Asia.

Although the FIs have been blamed for large and concerted withdrawals of capital from the country at the time of recent financial crisis, they have emerged as important players in the Indian capital market. As on June 4, 2009, the net equity investment by FIs in India is Rs. 2, 52,233.10 crore with the registration of 1662 foreign institutional investors.

Thus, in this paper an effort has been made to examine the performance of the Indian capital market by empirically studying the impact of net equity investment by FIs on stock returns. The study using monthly data on Sensex based stock return and net FII flows over a period of 17 years spanning from Jan 1993 to May 2009, provides the evidence of positive correlation between FII net flows into India and stock market return. And, the analysis finds that the movements in the Indian capital market are fairly explained by the FII net inflows.

In 2010, Capital Market Efficiency and Economic Growth: The Case of India, P K Mishra, Uma Sankar Mishra, Biswo Ranjan Mishra, Pallavi Mishra of Siksha ‘O’ Anusandhan University, Bhubaneswar, India observed as a part of their research, examined the impact of capital market efficiency on economic growth in India using the time series data on market capitalization, total market turnover and stock price index over the period spanning from the first quarter of 1991 to the first quarter of 2010.

The application of multiple regression model shows that the capital market in India has the potential of contributing to the economic growth of the country. This is as a result of high market capitalization and relatively high market liquidity.

Thus, the market organizations and regulations should be such that large number of domestic as well as foreign investors enters the market with huge listings, investments, and trading so that the very objective of optimal allocation of economic resources for the sustainable growth of the country can be ensured.

In 2010, ASSOCHAM and Price Water House Coopers jointly have come out with a study on The Indian Capital Market – Growth with Governance, broadly this study also covered the need for Governance for Growth but could not go in-depth into Sectoral Growth Trends.

In 2011, REDESIGNING THE CLEARANCE AND SETTLEMENT PROCESS IN THE INDIAN CAPITAL MARKETS, Research conducted by Preeti Goyal Visiting Faculty, Management Development Institute Gurgaon, India Raj S. Dhankar Professor of Finance, Faculty of Management Studies, University of Delhi, South Campus, New Delhi, India Visiting Professor, Faculty of Business Administration, Lakehead University, Thunder Bay, Ontario, Canada. As a part of their study, they have taken up, Clearance and settlement process is at the core of the securities market infrastructure.
The paper presents the importance of the process, describes the pre-redesign state of the Indian capital markets which was riddled with ineffective processes and regulations that led to a loss of investor confidence in the capital markets. In India the clearance and settlement process has been redesigned substantially due to various reasons including the integration of Indian capital markets with the global markets, growing trading volumes, various scams, and the need to boost investor confidence in the capital markets.

Financial liberalization thesis brought out by McKinnon (1973), Shaw (1973) and Cho (1986) emphasize an important role in resource allocation.

Modigliani and Miller (1958) argued that real investment decisions are independent of financial decisions. Capital structure of the firms or sources of financing has no bearing on their financial decisions. Contrary to the neoclassical models developed since 1950s, there are theoretical and empirical studies that stressed on the relationship between finance and investment (Minsky 1975; Fazarri and Variato 1994).

The financial system facilitates intermediation between savers (public) and investors (firms) and helps translate savings into investments. The system can be credit (bank) based and securities (capital market) based (Stiglitz 1994). Stiglitz (1994) further argued that market for corporate control provides the ultimate discipline in the stock market-dominated economies. Myres (1984) and Myres and Majluf (1984) opened up the way to the so-called pecking order theorem.

Pecking order theorem predicts a negative relationship between profitability (as a measure of internal funds) and debt financing. Debt and equity are not merely alternative modes of finance, but are also alternative modes of governance (Williamson 2002). Corporate governance is meant to create some rules and regulations which would ensure that external investors and creditors in a firm can get their money back and would not simply be expropriated by those who are managing the firm (Shleifer and Vishny 1997).

Berle and Means (1932) argued that the separation of ownership and control may lead managers to pursue their own objectives at the expense of owners. However, it is also argued that the diffuse equity ownership can also make managers run the firm to their own benefits at the expense of investors (Bolton and Schartstein 1998, p.100).

Cornelli, Portes, and Schaffer (1998) observed that the price of outstanding shares usually drops when a firm announces a new equity issue. An increase in debt has also a similar but less strong effect on share price. This could be the reason why managers prefer internal financing, turn to debt if the former option is not available and use equity issue only as a last resort.

The rationale for the relevance of the internal finance could be defended from two theoretical perspectives: The managerial approach emphasizes agency costs arising out of the separation of ownership from control and the role of internal finance in facilitating managerial discretion. However, in the context of developing countries, including India, the primary agency problem has
been between majority and minority owners (not between owners and managers) (refer La Porta et.al (1999) as cited by Reed Darryl p.15, 2004).

The second approach i.e. the information-theoretic approach emphasizes asymmetries of information between insiders (managers) and outsiders (suppliers of capital) leading to credit shortage faced by firms. Mishkin (1996) noted that adverse selection3 and moral hazard4 problems arising from asymmetric information in investor-firm relationship necessarily create disruptions in financial markets, leading to inefficient allocation of investible funds.

Asymmetric information framework relates information failures to the failures of intermediaries and stock markets and thus argues for government intervention. Stiglitz and Weiss 1981 & 1994 criticize the financial liberalization thesis on the grounds that financial markets are prone to market failures. Singh (1997) further argued that less developed countries should promote a bank based system and prevent a market for corporate control.

Singh (2003) argued that emerging countries with reasonably well-developed banking system and equity markets would follow pecking order pattern of finance, not only because of the informational asymmetries argued by Myres and Majuf for advanced countries,5 but also due to the institutional specificities of emerging markets in particular, (the desire to maintain family ownership and control of corporations).

The study by Mayer (1990) observed that two-thirds on the average of investment financing in developed countries like the US, UK, Japan, Germany, France, Italy, Canada and Finland are mobilized through internal financing. In contrast to the experience of the developed countries, Singh and Hamid (1992) observed very different trends in certain developing countries.

The contribution of external sources to the financing of net fixed capital formation in the 1980s was around 50 per cent with a significant share coming from the stock market. Government regulations that directly discourage the use of debt by imposing specified limits to debt ratios of firms could explain to some extent the preference of developing countries’ corporations for equity rather than debt financing.


Between the periods 1972-80 to 1988-966 which supports the findings of other studies, findings were observed by Rajakumar (2001), Sarkar and Sarkar (2004), Joshi (2005) and Bhole (2005). Various studies such as Singh and Hamid (1992), Nagaraj (1996), Singh (1995 & 1997), and Samuel (1996) argued that the capital market boom in developing countries is not associated with improved corporate profitability and therefore, may not help in achieving quicker industrialization and faster long-term economic growth.
A recent study by RBI (2005-06) has observed that the Indian corporate sector has mobilized a large share of resources from internal sources which accounts for 60.7 per cent during 2000-01 to 2004-05. Capital market has been considered as a last resort which contributed merely 9.9 per cent.

The debt-equity ratio has also declined over the years as the corporate sector has been able to mobilize resources internally. This kind of pattern of financing conforms to the so-called “pecking order” theory as applied in the developed countries (Singh, 2003). However, the study does not reveal the contribution of depreciation on large scale as a source of internal finance which is also an important aspect to be explored.

There are few empirical studies specifically on the investment pattern of the Indian corporate sector. Bhole (2005) argued that the gross or net savings rates of the private corporate sector remained low during 1966-67 to 2000-01. Moreover, this sector has not kept pace with its capital formation.

However, there is an increasing trend of capital formation in the private corporate sector since 2002-03. According to Mazumdar (2008), the annual rate of growth of gross fixed capital formation at constant prices was quite high during 1990-91 to 1996-97 which accounts for 19.5 per cent. And the growth in capital formation during the 1990s was relatively higher than the growth registered in the 1980s (Nair 2005).

Similar observations were made by another study based on ASI data (Nagaraj 2002). But this rate has sharply declined to the level of negative growth rate during 1996-97 to 2002-03 and again increased significantly to the level of 28.51 per cent during 2002-03 to 2007-08 (Mazumdar 2008).

The latest study (Robertson, 2010) also observed that India’s investment rate has increased from 25 per cent to 35 per cent of GDP in the present decade and argues that it may not get fully utilized in the long run.

Notably, Indian economy has also experienced a large number of mergers and acquisitions (M&A) during the liberalization period (Beena, P.L. 2008). One-third of the M&A deals that occurred in India during 1978-2007 were cross-border deals (Beena, S. 2010). Another recent study (Rao and Dhar 2010) observed that almost two-fifth of the foreign equity inflows was nothing but an acquisition of existing shares during 2005-06 & 2006-07.

Services sector was exposed to large share of Private Equity (PE) or Venture Capital (VC) investments as compared to the manufacturing sector7. There have also been several studies on Indian firms' acquisitions (Nayyar 2007; Pradhan 2007; Nagaraj 2006).

However no attempt has been made to understand the financing sources of each of the sectors under the umbrella of Industry. Therefore this study intends to fill this gap, based on a sample of companies chosen under each sector which are listed on BSE & NSE.
CHAPTER-I: INTRODUCTION TO INDIAN CAPITAL MARKETS

Given this background, an attempt has been made in this Research Thesis to analyze the sources of financing of Indian corporate sector and the role of such investments led sectoral growth trend, during 2003-2011.

SIGNIFICANCE OF THE STUDY

The present study is significant because development of INDUSTRY, which comprises of various sectors primarily needs investments and sources of such investments and rise and fall of investment patterns in to the various sectors is most crucial for decision makers and policy makers for encouraging and creating policy frame work for creating sustainable investments in the long run for the overall growth of each sectors forming part of the Industry.

LIMITATIONS OF THE STUDY

1. The study concentrates only on the select BSE and NSE listed companies from each of the sectors and SENSEX and NIFTY Companies, to draw the trends of growth.
2. The study is both qualitative and quantitative.
3. Though all the sectors are covered under the study of listed companies in BSE and NSE, for data analysis purpose only companies which have significant Market Capitalization of Rs.100 crores and above have been chosen as Market Capitalization is the basic criteria for institutional investments.
4. As the study is based on subjective perception based on the statistical data analyzed with the help of simple statistical tools, it may not be totally free from errors.
5. The study is focused on investments through capital markets as the capital markets both primary and secondary markets are the forums available for investments.

Researcher: CVSL Kameswari
OBJECTIVES, SCOPE AND RESEARCH METHODOLOGY:

MAIN OBJECTIVE

The main objective of the study is to find out, "How the capital markets in India have helped the various industrial sectors in India in terms of fresh capital addition contributing to the revenue growth".

Assess the role of Foreign Institutional Investors, Financial Institutions, Mutual Funds and Domestic Retail Investors.

SUB-OBJECTIVES

In achieving the main objective, the following sub-objectives are being framed:


II. Examine the investments that each of the above mentioned sectors have attracted.

III. Examine the Growth Pattern of the companies under sector wise segmentation.

IV. Examine the increase in capital in the respective companies under each sector as a function of increase in sales, profitability, asset addition and share price appreciation.

V. Examine the sector wise and company wise yearly returns that the respective sectors and companies have given to investors as investors at the end of the day, who are interested in return on investment.

VI. Identify problems, if any, faced by each of the sectors, in carrying out their revenue growth strategies with the help of new investments and to suggest remedial measures.

HYPOTHESIS

"Sectoral Growth in the Industry is led by Investment Flows through Capital Markets in India".

Having generated hypothesis, the process of hypothesis testing becomes important. In order to test whether, hypothesis is true or not, the current research study has been carried out.

In order to back up the hypothesis, the need to compare the results against the opposite situation: This is null hypothesis – the assertion that the things under testing (i.e. sectoral growth trends and investments) are not related and results are the product of random chance events.

More accurately, define the two hypotheses, the null and the Alternative.
CHAPTER-I: INTRODUCTION TO INDIAN CAPITAL MARKETS

NULL & ALTERNATIVE HYPOTHESIS

Null Hypothesis (H0): “Sectoral Growth in the Industry is Not Lead by the Investment Flows through Capital Markets in India”.

Alternate Hypothesis (H1): “Sectoral Growth in the Industry is led by Investment Flows through Capital Markets in India”.

For testing, Researcher analyzed and compared results against the null hypothesis.

PERIOD OF THE STUDY

The study covers the investment flows pattern between 2003 and 2011 in to various sectors in the Industry, based on availability of comparable data and information the period of study of many of the aspects falls within this range.

The rationale for broadly reviewing the topic since 2003 is based on two considerations. First, Investors worldwide have started investing in the India Capital Markets since 2003 after the bear run between 2001-2002. Second, a period between 2003-11 spanning over 9 years will provide the trend in the investments made by different kind of investors in various sectors in their growth perspective. Wherever authentic published data for comparable purpose is not available there the data is limited to the period of availability only.

SOURCES OF DATA & TECHNIQUES OF ANALYSIS

The present study is both descriptive and analytical. To suit its analytical requirements “Random Sampling Design” has been adopted. The companies forming part of the sectors have been chosen from a wide array of companies which have risen capital through Indian Capital Markets and listed on BSE & or NSE.

The study is based on both primary and secondary data, which constitutes the information, which have been culled out from the company specific records in terms of annual reports, news flows and announcements made on exchanges by the companies for their capital rising. The primary data are the data collected by the researcher on her own interaction with the companies concerned officials by way of emails, telephone interviews, and and one to one meetings. The secondary data constitute beside annual reports and other records of the concerned companies, the other published reports namely, industry reports, sector reports, periodicals and reference books, internet & websites.

Compiled data on the sources of financing in the Indian corporate manufacturing sector as a whole as well as in selected industries from the data- base on ‘corporate sector’ published annually by CMIE. The similar information at the firm level is collected from the PROWESS data- base published by CMIE.

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Also data was sourced from SEBI, RBI, IMF, World Bank Reports, NCEAR, Ministry of Corporate Affairs, Capital Ole databases relating to Indian Companies.

ANALYSIS OF DATA

The Data collected from various sources both primary and secondary are analyzed by applying appropriate statistical tools like percentages, weighted averages, Financial Ratio analysis and financial formulas as applicable and judgmental forecasting. To do cross comparison of sectoral returns to investor's benchmark P/E ratios have been used. To indicate the sectoral growth during the study period Graphical Charts and Trend Diagrams as suitable have been applied.

Advanced Statistical tools like Correlation techniques have been applied to find out the impact of correlation between investment flows and sectoral growth on one side and sectoral growth and GDP growth on the other side during the study period.

As the Study is meant for finding out the Sectoral Growth Trends Led by Investments, the proposition for Statistical Analysis of the data to find out the dependence and relationship between the variables relating to Sectors and Investments. Hence the most appropriate tool to find out the Statistical Relationship and Dependence of Sectoral Growth on Investments is through Correlation Coefficient.

About the Statistical Tool, Correlation Coefficient

In statistics, dependence refers to any statistical relationship between two random variables or two sets of data. Correlation refers to any of a broad class of statistical relationships involving dependence.

Formally, dependence refers to any situation in which random variables technically refers to any of several more specialized types of relationship between mean values. There are several correlation coefficients, often denoted $\rho$ or $r$, measuring the degree of correlation. The most common of these is the Pearson correlation coefficient, which is sensitive only to a linear relationship between two variables (which may exist even if one is a nonlinear function of the other).

"Pearson's correlation." It is obtained by dividing the covariance of the two variables by the product of their standard deviations. Karl Pearson developed the coefficient from a similar but slightly different idea by Francis Galton.

The population correlation coefficient $\rho_{X,Y}$ between two random variables $X$ and $Y$ with expected values $\mu_X$ and $\mu_Y$ and standard deviations $\sigma_X$ and $\sigma_Y$ is defined as:

$$\rho_{X,Y} = \text{corr}(X,Y) = \frac{\text{cov}(X,Y)}{\sigma_X \sigma_Y} = \frac{E[(X - \mu_X)(Y - \mu_Y)]}{\sigma_X \sigma_Y}.$$
Where $E$ is the expected value operator, cov means covariance and, corr a widely used alternative notation for Pearson’s correlation.

The Pearson correlation is defined only if both of the standard deviations are finite and both of them are nonzero. It is a corollary of the Cauchy–Schwarz inequality that the correlation cannot exceed 1 in absolute value. The correlation coefficient is symmetric: $\text{corr}(X,Y) = \text{corr}(Y,X)$.

The Pearson correlation is +1 in the case of a perfect positive (increasing) linear relationship (correlation), −1 in the case of a perfect decreasing (negative) linear relationship (anticorrelation), and some value between −1 and 1 in all other cases, indicating the degree of linear dependence between the variables. As it approaches zero there is less of a relationship (closer to uncorrelated). The closer the coefficient is to either −1 or 1, the stronger the correlation between the variables.

If the variables are independent, Pearson’s correlation coefficient is 0, but the converse is not true because the correlation coefficient detects only linear dependencies between two variables. For example, suppose the random variable $X$ is symmetrically distributed about zero, and $Y = X^2$. Then $Y$ is completely determined by $X$, so that $X$ and $Y$ are perfectly dependent, but their correlation is zero; they are uncorrelated. However, in the special case when $X$ and $Y$ are jointly normal, uncorrelatedness is equivalent to independence.

If we have a series of $n$ measurements of $X$ and $Y$ written as $x_i$ and $y_i$ where $i = 1, 2, ..., n$, then the sample correlation coefficient can be used to estimate the population Pearson correlation $r$ between $X$ and $Y$. The sample correlation coefficient is written

$$r_{xy} = \frac{\sum_{i=1}^{n} (x_i - \bar{x})(y_i - \bar{y})}{(n-1)s_x s_y} = \frac{\sum_{i=1}^{n} (x_i - \bar{x})(y_i - \bar{y})}{\sqrt{\sum_{i=1}^{n} (x_i - \bar{x})^2} \sqrt{\sum_{i=1}^{n} (y_i - \bar{y})^2}},$$

Where $x$ and $y$ are the sample means of $X$ and $Y$, and $s_x$ and $s_y$ are the sample standard deviations of $X$ and $Y$.

This can also be written as:

$$r_{xy} = \frac{\sum x_i y_i - n \bar{x} \bar{y}}{(n-1)s_x s_y} = \frac{n \sum x_i y_i - \sum x_i \sum y_i}{\sqrt{n \sum x_i^2 - (\sum x_i)^2} \sqrt{n \sum y_i^2 - (\sum y_i)^2}}.$$

If $x$ and $y$ are results of measurements that contain measurement error, the realistic limits on the correlation coefficient are not −1 to +1 but a smaller range.

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Positive value of 'r' indicates positive correlation between two variables (i.e., Changes in both variables take place in the statement direction). Whereas negative values of 'r' indicates negative correlation i.e., changes in two variables taking place in the opposite direction. A zero value of 'r' indicates that there is no association between the two variables. The value of 'r' nearer to +1 or -1 indicates high degree of correlation between the two variables.

COVERAGE OF THE STUDY

To suit both a descriptive and analytical study, the various aspects of Government Initiatives, SEBI's Policy and Regulation, Reports of Various Researchers, Committees, Legal Professionals, Reports of Various Investment Banks and Statistics of Various Publications and Government Reports have been pursued.

The study finally narrows down to examine quantitatively, "Sectoral Growth in the Industry, Led by Investment Flows through Capital Markets in India"

PLAN OF THE STUDY

The contents of the study evolved into 10 (Ten) Chapters.

Chapter – I, is introductory in nature and reviews the concept, rational, History and Overview of Capital Markets. Besides these aspects, the Chapter consists of objectives, scope and methodology which have been adopted for the Research.

Chapter – II: "Types of Indian Stock Markets – Primary and Secondary Markets – Regulatory Frame Work & Development Initiatives", it deals with the regulatory frame work relating to the Primary and Secondary Markets.

Chapter – III: Indian Debt Markets – Primary and Secondary Markets. Though focus is on investments from equity perspective, but briefly touches the Kind of Debt Markets in India.

Chapter – IV: Modes of Issuing Fresh Capital in Indian Markets, traces the various modes being used for rising capital and also touch base the various instruments through which fresh capital can be raised by companies.

Chapter V: Investment Inflows in to Various Sectors.

Quantitative Assessment of Foreign Institutional Investors, Mutual Funds, Financial Institutions / Banks, Insurance Companies and Domestic Corporate and Individual Investors investments in various selected Sectors for the Study for the period of 2003 and 2011 and depiction of the trend through Trend Diagrams.

Chapter VI: analyses the "Investments and Sectoral Growth Perspective". Statistical Analysis of Correlation between Investments and Sales, Profitability, Assets and Investor

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Market Capitalization and Net worth Multiplication in terms of Market Capitalization to assess the benefit for the investors through their investments.

Chapter VII: Provides an "Analysis of BSE SENSEX and NSE NIFTY Companies" and investment trends in these companies and growth correlation between investments and company’s growth in aggregates.

Chapter VIII: presents a "Comparative Analysis of Indian Stock Markets with International Markets and also studies the impact of Sub Prime Crisis on Capital Rising in India".

CHAPTER-IX: Deals with India Investments – The way forward with constructive suggestions” from researcher.

CHAPTER-X: Presents the Summary, Findings, Suggestions and Conclusion of the study.