Chapter 1: INTRODUCTION

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Chapter 1: INTRODUCTION

01.01 Introduction

Presently the Indian Capital Market which is playing a pivotal role in the Global Capital Market is experiencing a great shove in the investment sector. This buoyant phase of the Capital Market may be attributed to various affluential factors, some of which are outlined below:

- Advent of MNCs & Private Banks
- Growing volume of Corporate & Personal Financing
- Increasing interest of Foreign Institutional Investors in Indian market
- Role of Government in Financial Policies.

Like any other sector the capital market is also not untouched by the rapid growth of the information & communication technology, one of the major turnaround in the history of Indian Capital Market was computerization of stock exchanges. Automated screen based trading introduced first at NSE and further to BSE. This brought a qualitative improvement in the market and its transparency and as a result transaction cost & time was also reduced. Further the expansion of stock exchanges by the help of trading terminals also gave an impetus to the capital market.
After all these efforts even, capital formation process was slow. With the expansion of broking firms and other financial firms there was a major upsurge in this segment still there is a difference in capital investments between those cities were stock exchanges exist and where they don’t. Some of the major factors that may be attributed to this disparity are:

- Lack of information at investors end
- Time delay for the execution of transaction
- Scarcity of professional advice regarding capital investment issues
- High cost of transaction
- Under utilization of market potential

On account of the above parameters it may be stated that with the help of electronic media the performance of Indian Capital Market may further be enhanced and untapped market may be catered to the growing capital requirements of the robust Indian economy.

Online share trading has replaced the off line trading process in almost every part of the world. In India also, the scenario is same. In India online share trading is becoming very popular among the investors. There are several stock exchanges in India and among these, The NSE and BSE are the most important one.
Share trading in India is a popular way of investment and this has made NSE, the third largest stock exchange of the world. As a growing economy, India is expected to do well in all the sectors of investment and that is exactly what the investment sector is doing now. Shares are the first choice of the investors because it can provide encouraging returns in a short period.

Following the global trends, India has also changed the process of trading. In India online share trading is providing the customers with the simple and comfortable way of share trading. The investors are enjoying a bunch of services which is making the trading process much more secured and profitable.

The online trading sites are providing free trading tools to the investor to provide them all the necessary information and suggestion regarding the investment options and strategies. There are several charts and graphs which allow the investors to interpret in the process. At the same time information about all the latest openings for investment are also provided to the investor. Many of the leading companies in India that provide online share trading services alongwith other small scale brokers which are further covered under the present work of research.
01.02 Online Investing Process

The process of buying and/or selling financial securities, currencies and commodities through the Internet is known as online trading. For this purpose of trading online, investors need to exercise patience as well as use the right proprietary software provided by several brokers.

Online trading is an internet based investment activity which does not involve any direct involvement of the broker. There are several leading online trading portals in India along with the online trading platforms of the biggest stock houses like the NSE and BSE. The total section of online share trading in India has been found to have grown from only 3 per cent of the total turnover in 2003-04 to 16 per cent in year 2006-07\(^1\).

01.02.01 Process

The investor needs to register with an online trading portal and get into an agreement with the firm to trade in different securities as per the terms and conditions listed down in the agreement. The order processing is done in correct timings since the servers of online trading portal are connected to the stock exchanges and designated banks all round the clock. Updates can be received on the trading and investors can check the current status of their orders either through e-mail or through the interface. Brokerages also provide research content on
websites, so that the clients can take their own decisions on the stocks before they invest.

Thus in online trading, orders are implemented through online trading platforms offered by various brokers. Investors place their orders directly on a broker's site. The broker then executes the orders on the stock exchange and also makes payments on behalf of the clients. Brokers also provide clients with information related to market data, news and charts through their online platforms. This is done to help them in making informed decisions. Brokers charge software usage fees and trading commissions for their services. An investor is able to trade in more than one product/market through the same account and software.

01.02.02 Benefits of Online Trading

- **Transparency**: Online trading provides transparency on all the information related to the time of order placement till the final settlement. Every step of online trading is subject to scrutiny, since this provides transparency to the trading process.
- **Best prices**: Investors, by way of online trading, can get the best quotes for securities because of high transparency in the system.
- **Added convenience and liquidity**: One can carry out online trading anytime during business hours. This also helps in providing liquidity to investors.
- **Low commissions**: Investors can make transactions frequently, without the need to worry about the burden of commissions; thus making day trading and short-term trading more feasible.

### 01.02.03 Demerits of Online Trading

- **Technology problems**: Delays in transactions may be caused due to Internet connection outages or power failures.
- **A mentor's absence**: As there is no guidance from professionals, online trading may involve formulation of improper trading strategies which in turn would lead to huge losses.
- **Overtrading**: Online traders usually have a long term strategy before investing. However, the attraction of capitalizing on short term movements might make them buy and sell more often. Since the commission levels in online trading are low, investors are lured into day trading. This takes them away from their well-researched and long term trading strategy, causing great losses in the long run.

### 01.02.04 Considerations

- Set limit orders on trading of stocks.
- Avoid overtrading.
- Do not form decisions based on daily ups and downs.
- Observe long term trends.
- Stay away from trading based on rumors.
Online trading is an excellent tool to earn a living and to supplement regular income. However, before venturing into online trading, an investor must carefully research on the risks associated with online trading and must be prepared for the same before investing.
**01.03 Review of Literature:**

For obtaining a comprehensive view of the past and present online investment practices across various capital markets around the globe including that of India, an extensive study of available literature comprising of previous researches done in this regard has been summarized as under.

**Barber and Odean (2001, 2002)** studied the impact that the Internet is having on investors and financial markets. Their first study (2001) examined how the Internet, with its abundance of information, is affecting online investors’ decisions because of an illusion of knowledge and an illusion of control. They further studied this phenomenon in a second study (2002) and they concluded that after deciding to trade via the Internet, investors make more frequent trades, more risky trades and make less profit than they did prior to switching to online trading.

An article by **Hurley (2000)** discussed how online stock trading created an urge to trade and a desire for the investor to have more control over what they are investing in capital market.

**Opiela (2000)** looked at whether online investing is an opportunity or a hindrance from the viewpoint of financial planners. In a second article, **Opiela (1999)** once again touched on the pros and
cons of Internet trading from the viewpoint of professionals in the finance field. She stated that although the Internet may provide speed and convenience, it fails to provide the same advice as a professional for long term planning and diversification.

Fan, Stallaert, and Whinston (2000)\textsuperscript{7} studied two issues that are important to the efficiency of financial markets: order routing and order execution. They looked at how the Internet is affecting where orders for stocks are routed. They also discussed where the orders will be executed if they are originally placed on the Internet.

Vakil and Lu (2005)\textsuperscript{8} evaluated how the Internet has affected the capacity and volatility of the stock market. According to their research, since online trading has started, new investors have emerged that trade more aggressively and in higher volume and this in turn has led to an increase in stock trading and volatility in the market.

Bhasin (2005)\textsuperscript{9} examined e-broking and how e-brokerage firms can market financial services. He discussed the benefits of the lower transaction costs and the convenience of online trading for the investor.

In a separate article by Phelan (2001)\textsuperscript{10}, the difference between full service brokers and online brokers is presented and a discussion about the need for good online security is examined.
Another study by Globerman, Roehl, and Standifird (2001)\textsuperscript{11} assessed how e-commerce has added to the retail brokerage business. Brokers are now online and thus can provide lower costs to their customers along with a larger variety of investment information.

Yap and Lin (2001)\textsuperscript{12} examined how online trading systems are changing. They opine that future online discount brokerage firms will evolve from systems that provide basic services like low transaction costs, speed, and boundary spanning to systems that will eventually be able to provide the one-on-one personal advice that online brokerage firms are now missing.

Lewison and Bernstein (1996)\textsuperscript{13} wrote an article when online investing was still in its infancy. They discussed how to match the investors’ needs with the right online brokerage firm, how to avoid sales pitches, and how to think about security needs before one begins to invest.

Hong (2000)\textsuperscript{14} studied the information-processing costs that may arise from online trading. He discussed how many online traders are new to the investing world and are therefore naïve about how to go about investing.
Konana, Menon and Abramowitz (1999) explored the observable and unobservable costs associated with online electronic brokerages. A second article by these authors in 2000 looked at verifiable versus unverifiable costs. Verifiable and observable costs are the direct costs associated with online trading, like commissions. Unverifiable and unobservable costs are indirect costs that result from ways that electronic brokerages choose to complete their transactions and how the different locations could indirectly affect the investor. Since online investing is not a phenomenon affecting only the United States but the world as well, articles discussing Internet trading in different countries were analyzed.

Cocca (2002) studied the characteristics of online investors in Switzerland and the implications that online trading had on the Swiss market.

Teo, Tan, and Peck (2004) evaluated the attitudes of people who trade stocks online as well as the attitudes of those who do not trade online in the Singapore market.

M.T. Raja and Varsha Marathe (2002) conducted study on transaction cost for equity shares in India. The main objectives of the study was to analyse the cost of equity shares transaction in physical mode and demat mode. He found that the average cost for the FII in India is lower than stock market like Singapore, china, and Thailand. Due to
dematerialization the transaction cost of FII have comedown by 60 % and for mutual funds by 75%.

**Malabika deo(1999)** conducted a study on depository ordinance: a new dimension of capital market reform. The objective of the study deals with operations, functions and benefits of depository system. She concluded that introduction of depository system would take away of the ailments facing the present style, making the trading in scrip’s fool proof, would serve as a panacea and will ultimately pave the way for emergence of highly efficient capital market. However improved banking system, adequate infrastructure and fast information technology are all going to play a crucial role in the success of depository system in India.

**Chikodikar(2000)** studies undertaking dematerialization and the objectives framed was demat process and have detailed discussion on demat system-its meaning advantages, demat charges (price) depository and depository participants. He found that the electronic trading and trading of securities is a step in the right direction, paperless trading will prove to be boon to the stock market in the years to come.

Finally, **Goswami (2003)** examined the needs of investors that are trading online in India. He compared the needs of the investors to what online investing websites are offering and then tried to bridge the gap
between the existing disparities amongst investors requirements and service rendering by online broking firms.

In consonance with inferred observations from the above stated reviewed research literature, the derived objectives and hypotheses for current research study of online investing scenario in Indian Capital Market have been outlined.
01.04 Scope of Research

The present research focusses onto exploring the extent of usage of online services with respect to ongoing investment practices in Indian Capital Market. This being such a vast area of study, the scope of present study is limited to two major bourses of Indian Capital Market i.e., Bombay Stock Exchange and National Stock Exchange through which majority investors do online investing or online trading through various financial intermediaries. The technology being used in these exchanges is known as BOLT(BSE) and NEAT(NSE). Since the number of online investors is so enormous it would be difficult to formulate a justified sample with investors to explore the efficacy of online investments. For the same purpose the sample has been taken from the population of corporate and proprietary broking firms along with a sample of adopters and non-adopters of online trading system. The study being an individual research and not a group research is conducted with five different cities as the base(Mumbai, Delhi, Kanpur, Lucknow and Allahabad). A detailed structure of sample stratification is provided in later chapters.
01.05 Objectives of Research Study:

The present research work on “Efficacy of Online Investment Practices in India” is an exploratory research which focuses on identifying the current investment trends in the Indian Capital Market and to identify the efficacy of online investment process. Internet stock trading in India is a new phenomenon. Indian Stock Markets' Regulator, the Securities and Exchange Board of India (SEBI), approved the Internet trading on January 25, 2000 (AFP, 2000). Though still in its nascent stage, internet trading has grown steadily due to positive attitude of retail investors, reduction in the cost of a personal computer, availability of reliable Internet connectivity, and sophistication of Internet trading products. As of November 2009, there are as many as 345 Internet-based trading members in the Indian capital market having 23,78,456 registered clients for Web based access. The growth of Internet trading in India is, however, restricted by the low diffusion of technology, limited technology-based investors, insufficient banking interface, and the high cost of infrastructure (Australian Securities and Investment Commission, 2001).

While some investors are early technology adopters, others are slow in technology adoption. It is worth mentioning here that, in a recent study, adopters prefer using Internet to conventional means of trading (Teo et al., 2000). Hence, there is need to bring out the factors accountable for inter-group differences.
The main objectives of the present research study are outlined as under:

- **To analyze current state of online investment practices**
- **To study the role & efficacy of online trading terminals, broking firms & other private firms involved in this process.**
- **To investigate whether demographics such as age, income, occupation, trading experience influence the adoption of Internet trading by the investors;**
- **To examine whether attitude factors affect the adoption of Internet trading by the investors.**
- **To identify the major problems in online investment practices.**
01.06 Research Hypotheses:

On the basis of identified research objectives, fundamental hypotheses for the research study are outlined as follows:

H$_{01}$: There exists a uniformity in investment patterns amongst different strata of investors.

H$_{02}$: Demographic factors namely age, education level, occupation, income level and trading experience of the investors discriminates significantly between adopters and non-adopters of Internet stock trading.

H$_{03}$: Convenience, transparency, variety and safety of the system discriminates significantly between adopters and non-adopters of internet stock trading.

H$_{04}$: Awareness discriminates significantly between adopters and non-adopters of Internet stock trading.

H$_{05}$: Financial intermediaries (broking firms) are able to educate the investors for increasing the awareness and adoption of online trading in Indian Capital Market.
01.06 Conclusion

In consonance with the research objectives and designed hypotheses the study further aims at identifying the options available and hurdles being faced by an online investor in Indian Capital Market in the current scenario and thereby providing viable solutions for improvising and promoting investment through the technology enabled route of “Online Trading”.

List of References:


