CHAPTER-II

Microstructure of the Select Sample and Global Financial Markets

2.1 INTRODUCTION

At the outset we desire to introduce in brief the effectiveness of policies, practices, and regulations of select sample countries that typically aim to protect the buyer of financial securities and ensure that transactions are carried out on a fair and competitive basis. These functions are generally discharged by regulatory bodies such as Securities and Exchange Commission (SEC) of United States, Securities and Exchange Board of India (SEBI) etc. Often we find multiple supervisory system exist in the countries which led to debate among academics like –'Is one watch dog better than more?' (Corbett 2007). Amongst our select sample countries India relies on the theory of 'more'. Singapore, Korea rely on 'single supervisor' system, Malaysia on dual and Indonesia, Thailand, Philippines, US on 'many'. Supervision, control and regulation is important to maintain investors' confidence and to encourage foreign investors who are with even less direct knowledge of potential abuses, and whose ability to judge the conditions affecting returns on securities may be very limited.

Most commonly controllers of capital market controls aim to restrict issuance of foreign securities in the national market thereby restricting the availability of foreign securities to domestic investors. Some countries restrict limit that a domestic investors can invest abroad or constrain the extent of foreign investment in national companies and some even prohibit the acquisition of foreign securities by private investors (Appendix 1). Institutional investors, however, face some unique type of problems that are more critical and mostly insurmountable. Indeed, there is almost no country where financial institutions, insurance companies, pension fund and similar fiduciaries are not subject to rules and regulations that make it difficult for them to diversify. Understanding of these factors will help foreign investors to diversify their funds skilfully to achieve the target of risk reduction.

2.2 DESCRIPTION OF THE COUNTRIES

UNITED STATES OF AMERICA

USA is the most powerful and prosperous countries in the world with a per capita GDP of $51704 in 2012. New York Stock Exchange [NYSE] is the largest stock exchange of the world by market capitalization of its listed companies at US$16.613 trillion as of 2012. It is the first country, which has complete capital account liberalization (CAL) in 1974. Most of the controls such as Interest equalization tax (1963), Voluntary guidelines limiting foreign lending and investment (1965) guidelines limiting foreign direct investment (1968) were eliminated from 1974 onwards after the break down of Breton wood system. Since then USA have been following a liberal capital regime with limited controls that mainly relates to security of nation (Bakker and Chappel, 2002 Abdallah, 2005). Recently after the crash of Enron in 2002, the SEC has adopted a new regulation called the 'Sarbanes - Oxley Act of 2002' which consists of various rules related to disclosure, auditors' independence, insider trading, and the use of non-financial measures by foreign firms listed in US. All these rules aim to offer highest level of investors protection, supply relevant information to investors to help them value the assets fairly Thus the country is following more or less 'open economic policy', there is continuous endeavour to improve functioning of the market and now it is truly a play maker in the globalization game. The US stock market is much disciplined, less volatile and stable one as compare to the other Asian markets(see market stats in chapter iv). The US is India's third largest trading partner and one of the prime export destinations (second largest in 2012). At present, it accounts for 12% of India's exports and around 6.26% of India's imports. However, India accounts for only about 1.06% of the USA's total exports and imports. Total trade between USA and India stood during 2011 at $ 60,496 million during 2012-2013.

UNITED KINGDOM

This country is the combination of four developed countries of Europe; England, Ireland, Scotland and Wales. FTSE 100 is considered one of the most important indices of not only UK but also whole world. The per capita GDP of the country is $39,161 (2012), and the country belongs to high income group. Since World War - II, UK followed a conservative policy that relied heavily on control of capital accounts and regulation of its domestic financial system [(i)]. Despite tight control UK witnessed frequent exchange rate crisis and discouraging economic performance and finally country decided to opt for market based solution. In 1979 particularly country initiated a series of policy reversal that include abolition of restriction on sterling lending, significant withdrawal of barrier on outward capital flows in the month of June, massive change in the policy of outward portfolio investment in July coupled with suspension of exchange control act of 1947 in October, removal of the traditional distinction between jobbers [dealers] and brokers, liberalization of commission, introduction of the Stock Exchange Automated Quotation System [SEAQ] and abolition of stamp duties [transaction tax] on foreign and large trades. The issuer of foreign share London Stock Exchange must prepare audit and disclose their financial information in accordance with UK or US. Generally Accepted Accounting Principles (GAAPs) or International Accounting Standard [IAS]. Foreign firms home GAAP may be accepted if it can satisfy UKLA [United Kingdom Listing Agreement].

Like other developed countries, UK also enjoys a high ranking [eighth] in institutional development index. Enlighten policy, strict regulation, robust institutional framework, increasing disclosure [reducing information asymmetry], low transaction cost [increasing liquidity] contributed to develop this international market with nearly 700 companies from 70 countries in its list [Leuz et. al 2003, Abdulla 2003]. It enjoys good trade relationship with India. The bilateral trade of UK with India crossed the $ 7436. 79 million mark in 2012.

HONGKONG

There is a considerable continuity in Hong Kong's position in the international economy. It owes its origin as a commercial Centerport for China's regional global trade, and this is still a role it plays today. There was an amazing transformation of the country from a relatively unpopulated and backward territory at the beginning of the nineteenth century to one of the most attractive international financial centers of the world. Per capita GDP of $36,676 in 2012 clearly attests soundness of the economy and the country enjoys the status of high income group.

The Hong Kong Stock Exchange (HKSE) came into existence in Oct. 1986. During Oct. 1987 crash, trading in Hong Kong exchange was suspended for four days. In this instance, Hong Kong was mainly victim of global equity collapse, it costs the economy heavily but it also nakedly exposed few inadequacies of the institutional structure of the economy that escaped attention of the policy makers for long. Market authorities reacted promptly to reform functioning of the exchange and to strengthen the regulatory framework. In 1993 the semiautomatic system was combined with automatic order matching and execution system (AMS). There is no restriction on foreign investment and no limits exist on ownership of domestic companies by foreigners. Profits, dividends and interest can be fully and freely repatriated. Active derivative market is also an added source of its strength. All these liberal policies obviously are sources of encouragement for internationalization of the market. The Hong Kong market is highly volatile and the 'China Plot' has been a major factor influencing the market (Machiraju, 2000). The rate of volatility is much higher than that of US and UK and most of the other Asian countries (Chapter - iv). Simply between 2007 and 2008, market capitalization declined by nearly 50%, volume of share trading fall by nearly 24%, capital raised by new issue declined by 28%. Surprisingly the country that enjoys a rank of 12 in global competitiveness index suffers from the unruly behaviour of the market, the symptom is sufficient to fuel the debate 'does institution matter'. Highly skewed distribution (chapter - iv) of return suggests scope of earning abnormal gain through wise international diversification of fund.

This country is a strong trade partner of India, standing at the eighth position in the list of highest trade partners. The Bilateral trade of Hong Kong with India shots up to US$ 20356.89 million during the 2012-2013 financial year.

JAPAN

Japan is one of the worst victims of World War II but its astonishing turnaround in terms of technological advancement, economic prosperity, high standard of living, dynamism of capital market is an interesting agenda for discussion among development economist. Per capita GDP of the country, $46,707 (2012) symbolizes robustness of the economy. Presently it is a very important member of G8 nations. Nikkei 225 is internationally popular and widely observed stock index of the world. Since mid 60s Japan gradually started to liberalize its economy. From 1974 onwards the country initiated some major steps in quick succession such as abolition of voluntary restriction on banks' purchase of foreign securities, easing of restriction on foreign currency accounts, relaxing restriction on portfolio inflows and outflows, opening up of Japanese offshore market [JOM], introduction of new foreign trade control law etc. In case of institutional investors the limits on investment portfolio held abroad are (i) 30% of total assets for insurance companies purchasing foreign currency-denominated assets; and (ii) 20% of the reserve funds issued by non-residents for bond holdings by the Post Office Insurance Fund.

Japan enjoys eighth rank in global competitive index (World Economic Forum, 2008) and its relentless effort to build up favourable 'investment environment' deserves admiration. As an integral part of this on-going process, the country recently introduced 'Electronic Voting Platform' for foreign and institutional investors to improve the level of corporate governance.

India usually maintains steady trading relationships with Japan (presently 11th highest trade partners of India). The bilateral trade between these two countries stood at 10.2 billion us dollar in 2007. It is increased to US$18,613.19 million in 2012–13.

Due to prolonged stagnation market capitalization number of listed companies and foreign portfolio investment failed to increase to a satisfactory level during the last 15 years as compared to the other markets..

SOUTH KOREA

South Korea is one of the fastest growing economies of South East Asia. It has a very large and dynamic capital market too. However, the per capita GDP of this country is not very high; $22,589 (2012). During the late 80s this country started to adopt a policy of gradually liberalizing the domestic financial system and capital account, and this policy was fastened in 1993. In 1988, it introduced full convertibility for current account transactions. While the capital inflows were liberalized, capital outflows were restricted to help financing of current deficits. Later, due to substantial current account surplus, controls were re imposed on inflows and controls on outflows were eased. The country revised this policy in early 90's because of their strong domestic currency Won. It is evident that Korea's policy towards capital account transaction is completely guided by developments in the current account. Financial sector reform, including all efforts to improve regulation and supervision, were pursued concurrently. Korea was hit by Asian Financial crisis of 1997. Sharp rise in the short-term debt affected adversely the stability of financial sector, and produced a sustained pressure against WON. Following crisis it followed restructuring policies in financial sector, recovered fast and is currently showing robust growth rates. After liberalization in late 80s the country had to revert into restriction and then again moved towards liberalization. Thus economic policy of the country wanders from liberalization to restriction to cope up with the crisis emerging from internationalization of the economy. 'Experimentation, willingness to depart from orthodoxy and attention to local conditions' helped Korean Republic to withstand rough weather and to bolster its economy [Rodrik et al 2004]. The Standard Deviation of return during sample period is higher than that of all other countries under study except India (Table 4.1, Chapter-iv). Restrictive and frequently changing government policy coupled with excessive volatility resulted discouraging inflow of foreign portfolio investment. Interestingly growth of bank assets and market capitalization as a percentage of GDP shoot up remarkably in the last one decade in comparison with

other countries of the region and the country enjoys number one ranking in terms of stock index options contract traded in 2008 (Milo 2007). In response to change in economic policy, trade openness ratio of the country also varies.

However, India is a good trade partner of Korea (14th in the highest trading partners' list). Recently both the countries have entered into an agreement called Comprehensive Economic Partnership Agreement (CEPA). In last 3 years, the bilateral trade between both countries has grown by the average of 27 per cent and has reached to US$ 17,662.73 million in 2012.

INDONESIA

Indonesia was one of the worst sufferers of 1997 crisis. It has a weak financial structure in comparison with other economies of Asia-Pacific region. Jakarta stock exchange is considered to be one of the important stock exchanges of this region. Presently the per capita GDP of the country is $3,594 (2012) which is considered to be very low as compare to the other Asian countries under study except India. The economy was officially liberalized on September 1989. The Bank Act of 1992, (enacted Oct. 30 1992) allowed foreigners to invest up to 49% of listed shares of national banks. Minister of finance allows foreigners to purchase up to 49% of all companies listed in the domestic exchanges, excluding financial firms (Kim and Signal, 2000). To heal the devastating impact of Asian financial crisis on the economy, the country's public finance was tuned aggressively ignoring the rule of free economy. Government debt and spending on subsidies increased dramatically, while development spending fell sharply. The stock market was not opened enough till mid-nineties thus restricting the flow of foreign fund. Presently; Indonesia had liberalized its capital account, but still maintained its fixed exchange rate system. This fixed exchange rate system gave companies the perception that the risk of foreign currency-denominated debt was small. During the past decade, Indonesia has made an impressive recovery, thanks to prudent fiscal management, declining debt service, as well as increased tax and export revenues.

In line with its burgeoning economy, India's economic ties with its maritime neighbour Indonesia have also strengthened with high-growth trajectory in recent years. Our bilateral trade with Indonesia was increased by 36.6 per cent in 2007 as compared to 2006. Government of both the countries has signed strategic partnership agreement in the year of 2005. Presently Indonesia is the ninth highest trading partner of India. Total bilateral trade between those countries stood at $ 20,105 million in 2012-2013.

MALAYSIA

Malaysia is an important economy in this Asia Pacific region with a per capita GDP of $ 10,345 in 2012. Kualalampur Stock Exchange (now naming Bursa Malaysia) is a very active market of this very part of the world that is gradually transforming itself from emerging to developed market. 'Price regulation, licenses and quotas' were the salient features of Industrial Coordination Act [ICA] (1971-1975) of Malaysia. However, the recession obliged Malaysia to relax the strict controls of the New Economic Policy [NEP (1971-1975)]. The policies that previously had deterred foreign capitals- like ethnic quotas in equity ownership were relaxed. Most of the direct foreign investment was oriented to the dynamic electronic and electric machinery industry. Malaysian market was considerably liberalized during late nineties following series of measures taken by government and central bank to encourage existing portfolio investors to take a longer view of their investment in Malaysia, attract new funds into the country, while at the same time discouraging destabilizing short-term flows and penalizing early withdrawals. In addition, they were designed to allow smoother outflow of funds, rather than a sudden and massive outflow upon the expiry of the one year holding period. All these policies resulted into increase in the Foreign Portfolio Investment, infused vigor in market activities during the last 15 years.

The country has also a strong bilateral trade relation with India. Total bilateral trade of Malaysia with India amounted to $12032.38 million during 2012-2013 financial year.

SINGAPORE

Another important economic centre of South East Asia is Singapore with a per capita GDP of $60,799 (2012). Yearly growth rate of 3.42% sufficiently indicate the economic soundness of the country. Singapore-India bilateral trade has grown to a record level since the signing of the Comprehensive Economic Cooperation Agreement (CECA) 2007. The country is firmly committed to rely on free market economy thus the operation of the capital market is sufficiently liberalized. No foreign exchange control, no capital gains tax on the trading of securities by non-residents, negligible restrictions on the acquisition of securities by foreign investors, no limitations on the repatriation of dividend income and capital gains, no restriction to buy foreign securities by residents-all these enlightened policy allowed the country to enjoy the benefits of internationalization of the market while the countries commitment to develop 'quality' institutions helped to sustain economic growth [Miles et. al 2006].

Following rules and regulations regarding the capital market are worth mentioning-

1) Non-residents may issue equity shares without converting the Singapore Dollar proceeds of public offering in local currency.
2) Non-residents may issue bonds in same terms like the previous one. All rated and unrated foreign entities are allowed to issue Singapore Dollar bonds.
3) Financial institutions in Singapore may not extend Singapore Dollar credit facilities exceeding $5 million to any non-resident financial entity for speculative activities in foreign exchange market.

It is one of the very few Asia Pacific markets, which were completely out of the grasp of Asian Financial Crisis. It may be for that reason that the market is less volatile than that of the other Asian market under study (Table 4.1 Chapter -iv). It is a strong trade partner of India (sixth highest among all the countries) with a bilateral trade amounted to $21,363.03 million during the financial year 2012-2013.

TAIWAN

Shift in the policy from agriculture to industry along with enormous help of America; Taiwan at present is one of the important economies of Asia Pacific region and an attractive destination of global investors. The present per capita GDP of $38,200 (2011) represents the economic soundness of the country.

Flow of foreign investment in Taiwan began in the early 1980s. To prevent rapid capital inflows, the qualified foreign institutional investor (QFII) system was introduced in 1992. The system continued for more than a decade, finally, it was abandoned in October 2003 and a new foreign portfolio regulatory system came in to existence. The country virtually passed through three phases of deregulation and at each stage it aimed to persuade to strengthen integration of Taiwan market with the rest of the world. The first phase allowed indirect investment in the domestic securities market by overseas investors. The second phase granted QFII's permission to make direct investment in local securities market. Third phase extended the same facility to other general investors. The ceiling on shareholding by foreign investors in listed companies was lifted in 2001. Though the QFFI system was abolished in 2003, it shielded Taiwan from the Asian Financial Crisis. Abolition of QFII's system helped to attract more foreign fund which resulted into substantial increase in FPI and FDI in flow. Currently, Taiwan govt. classified the foreign investors into two categories:

1) Foreign institutional investors (FINI)
2) Foreign individual investors (FIDI)

While there is no cap and quota restriction on FINIs, FIDIs continue to be bound by US$ 85 million cap. Both should be registered with Taiwan Stock Exchange and approval from the central Bank is a must. Both categories of investors can invest in TSE listed stocks bonds derivatives etc. In sum, the recent deregulation of foreign portfolio investment in Taiwan intends to extend market scale and treat foreign investors the same way as domestic investors, thus leading to further integration with international markets. These policies ushered liquidity of the market and helped to stabilize its activities.

Presently India is a very good trading partner of Taiwan. Bilateral trade between Taiwan and India amounted to $ 3,816.7 million in 2012-2013 financial year.

INDIA

The economy of India is the tenth-largest in the world by nominal GDP and the third-largest by purchasing power parity (PPP). The country is one of the G-20 major economies and a member of BRICS. However, Indian economy is weakest among the select sample countries in terms of per capita GDP which stood at $1501 in 2012 (lowest in the sample). This shows the problem of mal distribution of the wealth in this country. Never the less, India stock market is one of the oldest stock market in Asia, which is operating since 1875. It remained largely isolated and completely unaffected by the global integration process until the late 1980. With the help of World Bank and IMF number of developing countries during late 80s took different steps to reconstruct their stock market to smoothen free movement of capital in and outflow from the market. Following the global trend reform of Indian Stock market virtually started after the foundation of the securities and exchange board of India (SEBI) in 1988. Studies suggest in India only a modest change in financial services supervision and official attitude towards the economy have produced huge growth pay off [Rodrik et. al (2004), Milo (2007)]. Since regime shift, with some modest changes, market started to grow with a tremendous pace and now has become one of the largest stock markets of Asia, which is increasingly attracting the investors around the globe. The opening up of Indian economy to foreign investment (1991) is considered to be the most significant policy in the history of economic reform. The deregulation measures soon harvested positive results as industrial exports and foreign investment today is growing at countries fastest rate ever. The capital market is also keeping pace with it.

Indian economy started to liberalize in the year of 1991 with the announcement of new economic policy. Indian economy was in deep crisis in July 1991, when foreign currency reserves had plummeted to almost $1 billion; Inflation had roared to an annual rate of 17 percent; fiscal deficit was very high and had become unsustainable; foreign investors and NRIs had lost confidence in Indian Economy. Capital was flying

out of the country and we were close to defaulting on loans. These sorts of economic compulsions prompt our policy makers to impose an all-round change in our economic policy. Since then some land mark decisions were taken to open up the economy gradually.

Apart from the Rupee Devaluation, Disinvestment, abolition of the industrial license and MRTP Act, several important changes were taken place regarding capital market too. Foreign Direct Investment (FDI) is allowed across a wide spectrum of industries and encouraging non-debt flows. Government has put in place a liberal and transparent foreign investment regime where most activities are opened to foreign investment on automatic route without any limit on the extent of foreign ownership. Some of the recent initiatives taken to further liberalize the FDI regime, inter alias, include opening up of sectors such as Insurance (up to 49%);development of integrated townships (up to 100%); defence industry (up to 26%); tea plantation (up to 100% subject to divestment of 26% within five years to FDI); enhancement of FDI limits in private sector banking, allowing FDI up to 100% under the automatic route for most manufacturing activities in SEZs; opening up B2B e-commerce; Internet Service Providers (ISPs) without Gateways; electronic mail and voice mail to100% foreign investment subject to 26% divestment condition; etc. The government has also strengthened investment facilitation measures through Foreign Investment Implementation Authority (FIIA).

The general policy and facilities for foreign direct investment as available to foreign investors/Companies are fully applicable to NRIs as well. In addition, Government has extended some concessions especially for NRIs and overseas corporate bodies having more than 60% stake by NRIs. Industries Reserved for the Public Sector were opened for Private Participation. Now there are only three industries reserved for the public sector. Peak customs tariff were reduced from over 300 per cent prior to the 30 per cent rate that applies now. Financial sector also experience very wide range of reforms, like deregulation of interest rates, strong regulation and supervisory systems, and the introduction of foreign/private sector competition. It was discussed earlier that most significant step towards globalization is Indian market is introduction of Foreign

Institutional Investors in 1992. They are now the most prolific player in this market. Indian investors are also allowed to invest internationally in GDR, ADR, and FCCB and now even in listed securities. The landmark step towards this drive was taken in 2004, when Indian firms were permitted to make overseas investments, through automatic route, up to 100 of their net worth. Now limit has been raised to 400%. The Liberalized Remittance Scheme (LRS) for Resident Individuals was further liberalized by enhancing the existing limit of US$ 100,000 per financial year to US$ 200,000 per financial year (April-March) in September-2007. The limit for portfolio investment by listed Indian companies in the equity of listed foreign companies was raised in September 2007 from 35% to 50 % of the net worth of the investing company as on the date of its last audited balance sheet. The aggregate ceiling for overseas investment by mutual funds, registered with SEBI, was enhanced from US$ 4 billion to US$ 7 billion in April 2008. The existing facility allows a limited number of qualified Indian mutual funds (MFs) to invest cumulatively up to US$ 1 billion in overseas Exchange Traded Funds, as may be permitted by the SEBI, would continue. The world has taken notice of India as an investor. The World Investment Report has observed India as a big investor having great technological and professional capabilities. The major drivers of phenomenal growth of India's Overseas Direct Investment (ODI) are:

1. Government's policy has encouraged ODI
2. Huge foreign exchange Reserves
3. Growing technological capabilities of Indian firms
4. Entrepreneurship of the Indians
5. Financial capabilities of Indian firms particularly on account of successful raising of funds abroad
6. Double Taxation Avoidance agreements with about 70 counties
7. Globalization policies in most of the countries.

From a tiny little market with a handful of listed companies the Bombay Stock exchange has now become a mammoth one with a highest density of transaction in the world behind only Taiwan (Biswal and Kamaya, 2001). Presently BSE is a largest

stock exchange of the world in terms of number of listed companies (5174 in 2012) with a market capitalization of $1.32 trillion in 2012 (IFS 2012). It is tenth largest stock exchange globally and it is running in the same category of the developed economies of the world in terms of ratio of market capitalization and global depository receipts [Hansda and Ray 2002].

The market capitalization of listed companies as a percentage of GDP increased to a phenomenal extent i.e, 94.4%, in 2010. Somehow, it reduced to 54.2% in 2011 and slightly increased to 68.6% in 2012. (Source: Global Annual Report, World Bank, 2012).

Despite odds, gradually India has become one of the favourite destinations of investment for the foreigners. The number of foreign institutional investors participating in India is increasing day by day. The number stood at 1247 in 2008 and increased to 1757 in financial year 2012-13 [Raj and Dhal (2008)] and www.bse.com. Subsequently, the flow of foreign portfolio also faced tremendous growth. The volume of F.P.I has expanded mammoth from USD 4 million in 1991 to USD 72,375 million in 2010-11.

However, Indian market is not fully liberalized. Certain restrictions are there in terms of FEMA I999 (Foreign Exchange Monitoring Act), CACC (Capital Account Convertibility Law) etc. Repatriation law still effective very strongly and capital is not fully convertible here [(ii) & (iii)].

Above discussion may compel us to comment that, though Indian capital market is liberalized a lot but complete liberalization or globalization is still at a far reaching distance (Appendix-1). But the matter of fact is, we are moving towards that destination slowly but surely irrespective of that whether it is good or bad.

Table-2.1

Economic and Market Indicators of the Sample Countries 2012 (amt. in Million USD)

COUNTRIES	GDP*	FOREX**	EXP	IMP	CURNT A/C	CAP A/C	MARKET CAP	LIST. COS
India	1501	170247.05	302965.43	464426.57	-71700	-516	1320000	5174
USA	51704	32482.10	1480405.20	2265844.00	-440423	6956	16613000	1867
UK	39161	42258.13	479252.76	639886.50	-93560	5983.744	33266000	2983
Hong Kong	36676	206379.64	428732.00	485633.00	3486	-185.486	16985000	1477
Japan	46707	776603.86	822564.16	854072.80	60859	-1017.167	3300000	2292
Korea	22589	206190.13	556601.01	524336.41	48335	602.1	1100000	1796
Indonesia	3594	68908.34	200587.08	176881.08	-24074	37.467	426780	462
Malaysia	10345	87799.11	228086.02	187473.07	18688	52.537	189000	818
Singapore	60799	153303.39	409503.21	365770.42	65323	NA	934543	776
Taiwan	20336	270091.24	308257.30	281437.50	-	810.302	810302.49	758

*GDP is in USD not in million ** Forex reserve is in SDR. (1SDR. =.65035 USD)

Data Source:

IMF (International Monetary Fund) DATA, WORLD BANK, IFS (International Financial Statistics) and WEF (World Exchange Federation).

EXP & IMP stands for export and import respectively and CURNT & CAP A/C indicate current account balance and capital account balance in balance of payment. MARKT CAP indicates market capitalization of the stock exchanges of respective countries. LIST.COS means the number of listed companies in the leading stock exchanges of the respective countries.

2.3 QUALITY OF MARKET

Following tables give some impression relating to quality of market both developed and developing as measured by FTSE. Large volume of information included in the table consists of efficiency of trading mechanism, regulatory environment, settlement, liquidity, transaction costs, broker service, depth of the market, restriction on foreign investment etc. Foreign investors usually consider above along with other information while deciding upon destiny of fund. Surely development of appropriate rule is essential, but not sufficient. A stable structure of human interactions that guarantees enforcement of the rule and maintains procedural efficiency is to be developed to attract foreign funds interested to diversify abroad. Developed rules and strengthen 'governance related' activities can only improve quality of the market.

Table 2.2

Microstructure of Global Markets

2.2. a) FTSE QUALITY OF MARKETS CRITERIA (AMERICAS) as at March 2013

FTSE QUALITY OF MARKETS CRITERIA (AMERICAS) as at September 2012

CRITERIA	COUNTRY NAMES											
	DEV	Canada	USA	ADV EMG	Brazil	Mexico	EMG	Chile	Colombia	Peru	FRONT	Argentina
World Bank GNI Per Capita Rating, 2011		High	High		Upper Middle	Upper Middle		Upper Middle	Upper Middle	Upper Middle		Upper Middle
Credit Worthiness		Investment	Investment		Investment	Investment		Investment	Investment	Investment		Speculative
Market and Regulatory Environment												
Formal stock market regulatory authorities actively monitor market (e.g. SEC, FSA, SFC)	X	Pass	Pass	X	Pass	Pass	X	Pass	Pass	Pass	X	Not Met
Fair and non-prejudicial treatment of minority shareholders	X	Pass	Pass	X	Restricted	Pass		Pass	Pass	Not Met		Not Met
Non or selective incidence of foreign ownership restrictions	X	Pass	Pass	X	Pass	Restricted		Pass	Pass	Pass		Pass
No coercion to or significant restrictions or penalties applied to the investment of capital or the repatriation of capital and income	X	Pass	Pass	X	Pass	Pass	X	Restricted	Pass	Pass	X	Not Met
Free and well-developed equity market	X	Pass	Pass	X	Pass	Pass		Restricted	Pass	Not Met		Not Met
Free and well-developed foreign exchange market	X	Pass	Pass	X	Restricted	Pass		Pass	Pass	Pass		Not Met
Non or simple registration process for foreign investors	X	Pass	Pass	X	Pass	Pass		Pass	Pass	Pass		Pass
Custody and Settlement												
Settlement - Rare incidence of failed trades	X	Pass	Pass	X	Pass	Pass	X	Pass	Pass	Pass	X	Pass
Custody Sufficient competition to ensure high quality custodian services	X	Pass	Pass	X	Pass	Pass	X	Pass	Pass	Not Met		Pass
Clearing & settlement - T+3 - T+5 for Frontier	X	T+3	T+3	X	T+3	T+3	X	T+2	T+3	T+3	X	T+3
Stock Lending is permitted	X	Pass	Pass		Pass	Pass		Not Met	Restricted	Restricted		Not Met
Settlement - Free delivery available	X	Pass	Pass		Pass	Pass		Restricted	Not Met	Restricted		Not Met
Custody - Omnibus account facilities available to international investors	X	Pass	Pass	X	Pass	Pass		Not Met	Pass	Pass		Not Met
Dealing Landscape												
Brokerage - Sufficient competition to ensure high quality broker services	X	Pass	Pass	X	Pass	Pass	X	Pass	Pass	Pass		Pass
Liquidity - Sufficient broad market liquidity to support sizeable global investment	X	Pass	Pass	X	Pass	Pass	X	Pass	Restricted	Not Met		Not Met
Transaction costs - implicit and explicit costs to be reasonable and competitive	X	Pass	Pass	X	Pass	Pass	X	Pass	Pass	Pass		Pass
Short sales permitted	X	Pass	Pass		Pass	Pass		Restricted	Restricted	Restricted		Pass
Off exchange transactions permitted	X	Pass	Pass		Not Met	Pass		Not Met	Pass	Pass		Pass
Efficient trading mechanism	X	Pass	Pass		Pass	Pass		Pass	Pass	Pass		Pass
Transparency - market depth information - visibility and timely trade reporting process	X	Pass	Pass	X	Pass	Pass	X	Pass	Pass	Not Met	X	Pass
Derivatives												
Developed Derivatives Market	X	Pass	Pass		Pass	Pass		Not Met	Not Met	Not Met		Not Met
Size of Market												
Market Capitalisation $mn (as at 31st Dec 2011)		1,912,122	15,640,707		1,228,936	408,690		27,289	201,298	31,978		41,580
Total Number of Listed Companies (as at 31st Dec 2011)		3,845	4171		366	128		229	70	202		99

*USA Size of Market data based on combined figures from NYSE & Nasdaq

Shading indicates a change from March 2012

Source: FTSE, 2013

2.2. b) FTSE QUALITY OF MARKETS CRITERIA (EUROPE) as at March 2013

FTSE QUALITY OF MARKETS CRITERIA (EUROPE Developed) as at March 2013

CRITERIA	COUNTRY NAMES															
	DEV	Austria	Belg/Lux	Denmark	Finland	France	Germany	Greece	Ireland	Italy	Netherlands	Norway	Portugal	Spain	Sweden	Switzerland	UK
World Bank GNI Per Capita Rating, 2011		High	High	High	High	High	High	High	High	High	High	High	High	High	High	High	High
Credit Worthiness		Investment	Investment	Investment	Investment	Investment	Investment	Selective Default	Speculative	Investment	Investment	Investment	Speculative	Investment	Investment	Investment	Investment
Market and Regulatory Environment																	
Formal stock market regulatory authorities actively monitor market (e.g. SEC, FSA, SFC)	X	Pass	Pass	Pass	Pass	Pass	Pass	Pass	Pass	Pass	Pass	Pass	Pass	Pass	Pass	Pass	Pass
Fair and non-prejudicial treatment of minority shareholders	X	Pass	Pass	Pass	Pass	Restricted	**Pass**	Pass	Pass	Restricted	Pass	Pass	Pass	Pass	**Pass**	Restricted	Pass
Non or selective incidence of foreign ownership restrictions	X	Pass	Pass	Pass	Pass	Pass	Pass	Pass	Pass	Pass	Pass	Pass	Pass	Pass	Pass	Pass	Pass
No objection to or significant restrictions or penalties applied to the investment of capital or the repatriation of capital and income	X	Pass	Pass	Pass	Pass	Pass	Pass	Pass	Pass	Pass	Pass	Pass	Pass	Pass	Pass	Pass	Pass
Free and well-developed equity market	X	Pass	Pass	Pass	Pass	Pass	Pass	Pass	Pass	Pass	Pass	Pass	Pass	Pass	Pass	Pass	Pass
Free and well-developed foreign exchange market	X	Pass	Pass	Pass	Pass	Pass	Pass	Pass	Pass	Pass	Pass	Pass	Pass	Pass	Pass	Pass	Pass
Non or simple registration process for foreign investors	X	Pass	Pass	Pass	Pass	Pass	Pass	Pass	Pass	Pass	Pass	Pass	Pass	Pass	Pass	Pass	Pass
Custody and Settlement																	
Settlement - Rare incidence of failed trades	X	Pass	Pass	Pass	Pass	Pass	Pass	Pass	Pass	Pass	Pass	Pass	Pass	Pass	Pass	Pass	Pass
Custody-Sufficient competition to ensure high quality custodian services	X	Pass	Pass	Pass	Pass	Pass	Pass	Pass	Pass	Pass	Pass	Pass	Pass	Pass	Pass	Pass	Pass
Clearing & settlement - T + 1, T + 3 for Frontier	X	T+3	T+3	T+3	T+3	T+3	T+2	T+3	T+3	T+3	T+3	T+3	T+3	T+3	T+3	T+3	T+3
Stock Lending is permitted	X	Pass	Pass	Pass	Pass	Pass	Pass	Restricted	Pass	Pass	Pass	Pass	Pass	Pass	Pass	Pass	Pass
Settlement - Free delivery available	X	Pass	Pass	Pass	Pass	Pass	Pass	Pass	Pass	Pass	Pass	Pass	Pass	Restricted	Pass	Pass	Pass
Custody - Omnibus account facilities available to international investors	X	Pass	Pass	Pass	Pass	Pass	Pass	Restricted	Pass	Pass	Pass	Pass	Pass	Pass	Pass	Pass	Pass
Dealing Landscape																	
Brokerage - Sufficient competition to ensure high quality broker services	X	Pass	Pass	Pass	Pass	Pass	Pass	Pass	Pass	Pass	Pass	Pass	Pass	Pass	Pass	Pass	Pass
Liquidity - Sufficient broad market liquidity to support sizeable global investment	X	**Pass**	Restricted	Restricted	Pass	Pass	Pass	Pass	Pass	Pass	Pass	Pass	Restricted	Pass	Pass	Pass	Pass
Transaction costs - implicit and explicit costs to be reasonable and competitive	X	Pass	Pass	Pass	Pass	Pass	Pass	Pass	Restricted	Pass	Pass	Pass	Pass	Pass	Pass	Pass	Restricted
Short sales permitted	X	Pass	Pass	Pass	Pass	Pass	Pass	Restricted	Pass	Pass	Pass	Pass	Restricted	Restricted	Pass	Pass	Pass
Off-exchange transactions permitted	X	Pass	Pass	Pass	Pass	Pass	Pass	Restricted	Pass	Pass	Pass	Pass	Pass	Pass	Pass	Pass	Pass
Efficient trading mechanism	X	Pass	Pass	Pass	Pass	Pass	Pass	Pass	Pass	Pass	Pass	Pass	Pass	Pass	Pass	Pass	Pass
Transparency - market depth information - visibility and timely trade reporting process	X	Pass	Pass	Pass	Pass	Pass	Pass	Pass	Pass	Pass	Pass	Pass	Pass	Pass	Pass	Pass	Pass
Derivatives																	
Developed Derivatives Market	X	Pass	Pass	Pass	Pass	Pass	Pass	Pass	Pass	Pass	Pass	Pass	Pass	Pass	Pass	Pass	Pass
Size of Market																	
Market Capitalisation $mn as at 31st Dec 2012		136,227	299,517	226,898	147,436	1,906,159	1,496,315	44,877	128,989	436,233	650,311	242,758	85,515	995,799	571,947	1,220,403	3,398,500
Total Number of Listed Companies as at 31st Dec 2012		84	119	168	122	505	663	262	42	282	103	184	45	3,147	256	238	2,175

Shading indicates a change from September 2012

Market size of Italy includes AIM and MAC

Source: FTSE, 2013

2.2. c) FTSE QUALITY OF MARKETS CRITERIA (ASIA-OCEANIA) as at March 2013

FTSE QUALITY OF MARKETS CRITERIA (ASIA PACIFIC) as at March 2013

ERIA	DEV	Australia	Hong Kong	Japan	New Zealand	Singapore	South Korea	DEV WATCH	ADV EMG	COUNTRY NAMES: Taiwan	Malaysia	Thailand	EMG	India	Indonesia	Pakistan	Bangladesh	Sri Lanka	Vietnam
ank GNI Per Capita Rating, 2011											Upper Middle	Upper Middle		Lower Middle	Lower Middle	Lower Middle	Low	Lower Middle	Lower Middle
ectness		Restricted	Restricted	Restricted	Restricted	Restricted	Restricted			Restricted	Restricted	Restricted		Restricted	Restricted	Restricted	Restricted	Restricted	Restricted
and Regulatory Environment																			
stock market regulatory authority active, funds higher [illegible]	X	Pass	Pass	Pass	Pass	Restricted	Pass	X	X	Pass	Pass	Pass	X	Pass	Restricted	Pass	Pass	Pass	Pass
Prior previous market if length organisation	X	Pass	Pass	Pass	Pass	Pass	Pass	X	X	Pass	Pass	Pass		Number	Number	Pass	Restricted	Restricted	Restricted
take the incentive if they remaining restrictions	X	Pass	Pass	Restricted	Restricted	Pass	Restricted	X	X	Pass	Restricted	Restricted		Number	Pass	Pass	Pass	Restricted	Restricted
there is a significant restriction a penalties applied if the [illegible] of the regulation if capital and income	X	Pass	Pass	Pass	Pass	Pass	Pass	X	X	Pass	Pass	Pass	X	Pass	Pass	Pass	Pass	Pass	Pass
Developed equity market	X	Pass	Pass	Pass	Pass	Pass	Pass	X	X	Pass	Pass	Pass		Pass	Pass	Pass	Restricted	Restricted	Restricted
Developed foreign exchange market	X	Pass	Pass	Pass	Pass	Pass	Restricted	X	X	Restricted	Restricted	Restricted		Number	Restricted	Restricted	Number	Number	Restricted
simple registration process for foreign investor	X	Pass	Pass	Pass	Pass	Pass	Pass	X	X	Pass	Pass	Pass		Restricted	Pass	Pass	Restricted	Restricted	Restricted
y and Settlement																			
[illegible] rights including of shareholder	X	Pass	Pass	Pass	Pass	Pass	Pass	X	X	Pass	Pass	Pass	X	Pass	Pass	Pass	Pass	Pass	Pass
[illegible] sufficient information to ensure high quality of the [illegible]	X	Pass	Pass	Pass	Pass	Pass	Pass	X	X	Pass	Pass	Pass	X	Pass	Pass	Pass	Pass	Pass	Pass
[illegible] settlement T+1 T+2 T+3 or T+4	X	T+3	T+2	T+2	T+3	T+3	T+3	X	X	Restricted	T+2	T+3	X	T+2	T+1	T+2	T+1, T+2	T+3	T+3
lending is permitted	X	Pass	Pass	Pass	Pass	Pass	Pass	X		Restricted	Restricted	Pass		Pass	Pass	Restricted	Number	Number	Restricted
[illegible] Flow between markets	X	Pass	Pass	Pass	Pass	Pass	Restricted	X		Restricted	Pass	Pass		Pass	Restricted	Pass	Number	Number	Number
[illegible] account balance equation in international [illegible]	X	Pass	Pass	Pass	Pass	Pass	Pass	X	X	Pass	Pass	Pass		Number	Pass	Restricted	Number	Number	Pass
e Landscape																			
[illegible] sufficient information to ensure high quality of the [illegible]	X	Pass	Pass	Pass	Pass	Pass	Pass	X	X	Pass	Pass	Pass	X	Pass	Pass	Pass	Pass	Pass	Pass
[illegible] sufficient large market liquidity to support investor investment	X	Pass	Pass	Pass	Pass	Pass	Pass	X	X	Pass	Pass	Pass	X	Pass	Pass	Pass	Restricted	Number	Restricted
[illegible] open and aspect costs to the requirement and [illegible]	X	Pass	Pass	Pass	Pass	Pass	Pass	X	X	Pass	Pass	Pass	X	Pass	Restricted	Pass	Pass	Pass	Pass
[illegible] permitted	X	Pass	Restricted	Restricted	Pass	Pass	Pass	X		Restricted	Restricted	Pass		Pass	Pass	Restricted	Number	Number	Number
Foreign transactions permitted	X	Pass	Pass	Pass	Pass	Pass	Restricted	X		Restricted	Pass	Pass		Number	Pass	Pass	Number	Number	Pass
Trading mechanism	X	Pass	Pass	Pass	Pass	Pass	Restricted	X		Pass	Pass	Pass		Restricted	Pass	Pass	Restricted	Restricted	Restricted
[illegible] market data information, including all broker trade [illegible]	X	Pass	Pass	Pass	Pass	Pass	Pass	X	X	Pass	Pass	Pass	X	Pass	Pass	Pass	Restricted	Pass	Pass
ives																			
[illegible] Derivatives Market	X	Pass	Pass	Pass	Restricted	Pass	Pass	X		Pass	Number	Restricted		Restricted	Number	Number	Number	Number	Number
f Market																			
[illegible] Size as at Mar Dec 2011		[illegible]	[illegible]	[illegible]	[illegible]	[illegible]	[illegible]			[illegible]	[illegible]	[illegible]		[illegible]	[illegible]	[illegible]	[illegible]	[illegible]	[illegible]
Number of listed companies as at Mar Dec 2011		[illegible]	[illegible]	[illegible]	[illegible]	[illegible]	[illegible]			[illegible]	[illegible]	[illegible]		[illegible]	[illegible]	[illegible]	[illegible]	[illegible]	[illegible]

*Japan Size of Market data based on combined figures from Tokyo, Osaka & Jasdaq Stock Exchanges
*India Size of Market data based on combined figures from Mumbai & National Stock Exchange of India
*Pakistan Size of Market data based on Karachi SE
*Vietnam Size of Market data based on HoChiMin SE & Hanoi Securities Trading Center
*Bangladesh Size of Market data based on Dhaka Stock Exchange Ltd
*China A & B Size of Market data based on Shanghai Stock Exchange & Shenzhen Stock Exchange

[illegible] indicates a change from [illegible]

Source: FTSE, 2013

2.4 CONCLUSION

So long we were mainly involved in describing the current status of the sample countries, incentives and constraints to foreign flow of fund, micro structure of the market, the issues that all together to an extent promote or restrain capital market integration. Analysis was mainly descriptive in nature.

In the next section, firstly, we will attempt to analyse objectively the level of integration of the sample countries in response to popular concepts of globalization that is ruling over the modern day's economy. Secondly, an attempt will be made to answer the query - Why some capital markets are less integrated; incapable to attract foreign investment hence the markets are illiquid, thin and failing to promote itself in the category of developed market.

END NOTE:

I. Some restrictions were: convertibility of sterling [1958], restriction on direct investment outside sterling area [1961], controls on portfolio investment [1971].

II. FEMA 1999: Realisation and repatriation of foreign exchange. - Save as otherwise provided in this Act, where any amount of foreign exchange is due or has accrued to any person resident in India, such person shall take all reasonable steps to realize and repatriate to India such foreign exchange within such period and in such manner as may be specified by the Reserve Bank

III. i) Sectors prohibited for FDI i. Retail trading (except Single Brand Product retailing) ii. Atomic Energy iii. Lottery business iv. Gambling and Betting (ii) Prior approval of the Government would be required only in following two cases: (a) Where the foreign investor has an existing joint venture or technology transfer/trademark agreement in the 'same' field. (b) Where more than 24% foreign equity is proposed to be inducted for manufacture of items reserved for the Small Scale sector. (iii) Sectors/ activities with certain restrictions: In 28 cases, FDI is allowed subject certain Sector cap, statutory limits or other guidelines/restrictions. (iv) FDI is permitted up to 100%, under automatic route, in all other cases.)