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A COMPARATIVE STUDY ON THE CAPITAL MARKETS OF INDIA AND THE UNITED KINGDOM

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ABSTRACT

In recent decades, India progressed in economic development, attaining quick and continuous growth with an average GDP expansion of nearly 7% per year during the last ten years. Similarly, the United Kingdom has seen tremendous economic growth during the same period. In the United Kingdom, the financial industry has been critical to the country's overall economic progress. This industry is well-developed, with well-established financial markets such as the stock and bond markets, which provide enterprises with various funding and investment alternatives. This advancement has enabled firms in the United Kingdom to acquire finance leverage and expand their operations, contributing to the country's overall economic growth. India and the UK have robust capital markets that offer various investment options for individuals and companies. However, there are significant differences in both countries in terms of the size of the markets, regulatory frameworks, and investor behaviour. This paper examines the comparative analysis of the capital markets of both countries.

Keywords: *Capital Markets, Derivatives, Risk and Returns, Financial Leverages.*

Introduction

For businesses to raise capital and investors to invest their savings in profitable assets, capital markets are essential for a nation's economic expansion and development. With various investment options available to investors, the capital markets in India and the UK are among the world's most prominent and active. Comparing these markets can offer insightful information about their similarities and differences and assist investors and governments in making defensible choices on investment opportunities in these areas. To thoroughly examine both markets' potential as investment opportunities, this study will look at several features of the Indian and UK capital markets, including their size, liquidity, regulation, risk profile, and historical performance.

Financial markets' expanding globalization and investors' increased interest diversified their investments across various countries and territories. Both India and the UK are strong economies with well-established capital markets that provide domestic and foreign investors with various investment options. As a result, a study of these markets can shed light on their similarities and differences and aid investors and decision-makers in determining whatever investment opportunities are available in these areas. Additionally, there have been significant changes to the Indian and UK capital markets in recent years, with regulatory reforms in India aimed at enhancing market efficiency, transparency, and investor protection. Similar regulatory reforms have taken place in the UK sector since the global financial crisis of 2008, leading to new regulatory bodies and reforms to the existing regulatory framework.

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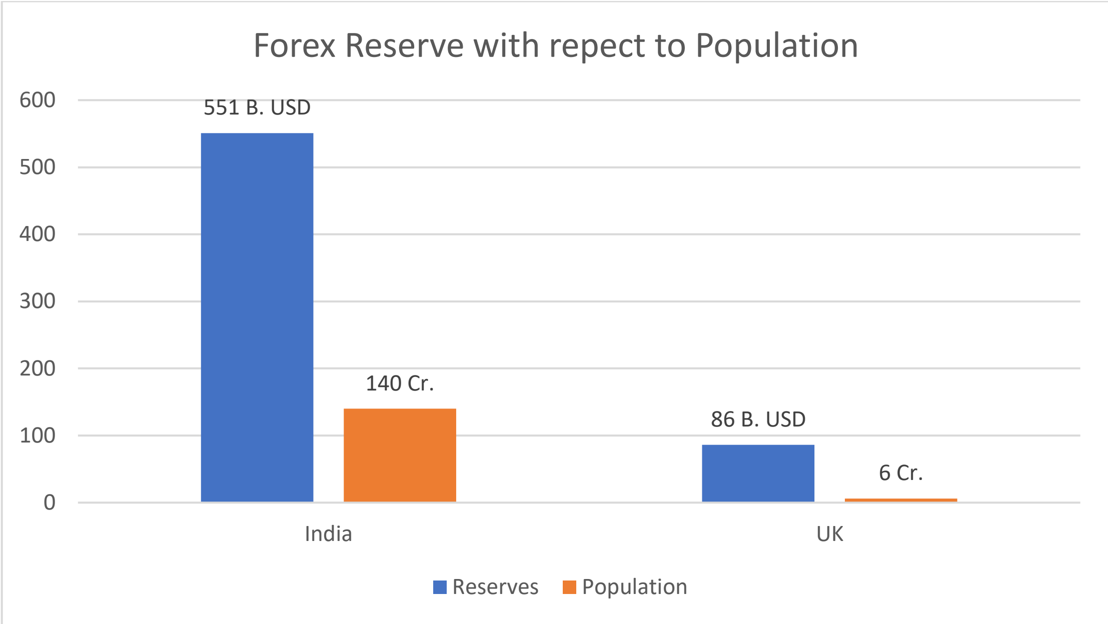

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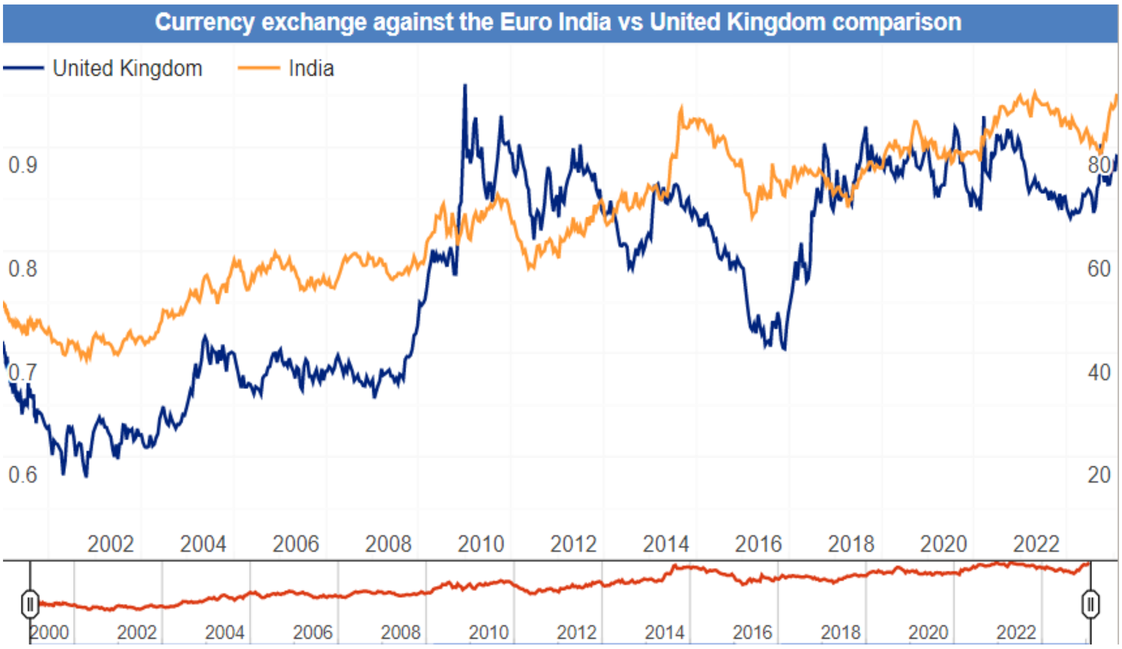

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Importance of Capital Market in the Economy

The role of capital markets in economies is similar the importance and significance of capital markets in a developing country is greater. Businesses, enterprises, and corporations are in any economy the critical factor that contributes to the scaling of a country. Capital markets are a beautiful mechanism to match the needs of these important entities and those of investors making it a win-win situation for both. This also leads to the circulation of money in the market too. In countries like Japan, the USA, and other developed countries whose rate of growth every year is growing at a very small proportion, capital markets of successfully developing countries like India is an investment opportunity for them.

In India capital markets largely help in the mobilization of savings and acceleration of growth, raising long-term capital, ready and continuous marketability, promotion of industrial growth, and technical assistance. In respect to the contribution of capital concerning performance, it helps in the development of backward areas, transparency in the financial system, easy liquidiy, foreign capital, and provision of variety of services.

In the respect to the United Kingdom, considering its current situation due to covid, political distress, and the ongoing war the economy is in a bad situation. Capital markets as a mechanism have helped business recover and fund at such times

As per an article by bnp Paribas, UK corporates are engaged in a range of capital markets activities, from debt and equity financing to hedging through derivatives. Mark Lynagh, Co-Head of Debt Markets EMEA, observes that "UK corporates are active in using a portfolio of funding tools when they look at their balance sheet." "Several UK corporates have issued bonds in the last twelve weeks, as there has been a large rebound in underlining investors' credit appetite, also bolstered by central bank liquidity," suggested Lynagh. In big-picture terms, the longer-term evolution of UK capital markets has been a story of diversification and simplifying market access, adds Lynagh. "Corporates have enjoyed a wide range of private to public capital markets options, with several borrowers adopting credit ratings to further widen their funding options. This has helped to diversify the number of sectors issuing regularly in the capital markets."

Objectives

- To compare the capital markets of India and United Kingdom.
- To understand the impact of regulatory frameworks on the development of capital markets in India and the UK

Literature Review

In the study paper "Comparative Analysis of Indian Stock Market with International Markets," published in 2007 the performance of the Indian stock market is compared to that of important foreign stock markets like the US, UK, China, and Japan. Using statistical techniques including the GARCH model and co-integration analysis, the study examines stock market data from January 2006 to December 2015. In comparison to the US, UK, and Japanese stock markets, the Indian stock market has larger returns but also more volatility, according to the article. The report also emphasizes the necessity of regulatory reforms to increase market efficiency and stability as well as the significance of international diversification for portfolio management.

" David A Bogle, Christopher Coyle, John D Turner's journal article Capital market development over the long run: the portfolios of UK life assurers over two centuries published in 202 The article examines the investment portfolios of UK life insurers from 1800 to 2010 to study the long-term development of capital markets. The authors find that life assurers played a critical role in the evolution of capital markets and adapted their investment strategies to changing market conditions and regulatory requirements. Their investment behavior influenced the pricing and availability of capital for other market participants, emphasizing the importance of long-term institutional investors in the development of capital markets

Rajdeep Kumar Kaur, Niladri Das, and Ramkrishna Mishra 's work, Behaviour of Individual Investors in Stock Market Trading: Evidence from India published in 2018, examines the factors that underpin individual investors' investment decision-making behavior to find whether the Indian financial market is efficient and investors make rational decisions. The result indicates that the investors are significantly influenced by herding, information cascades, anchoring, representativeness, and overconfidence while contagion shows the insignificant result

Fanyi Wang, Ruobing Zhang, Faraz Ahmed, and Syer Mir Muhammed Shah. 's paper Impact of investment behavior on financial markets during COVID-19: a case of UK published in 2021, studies study the impact of investment behavior on the study determined significant moderation of covid-19 uncertainty over the relationship of risk perception and general risk to tolerance. (Rajdeep Kumar Kaur)

Research Methodology

An evaluation of the Indian and UK stock markets using a quantitative research approach and secondary data constitutes the research technique. To ensure that only accurate and relevant secondary data are used in the analysis, the study uses a purposive sampling technique. Quantitative and qualitative data will be gathered during the data-gathering process using financial statements, the database of the Bank of England, RBI, JP Morgan Publications, and other pertinent sources. The study will guarantee that the data collection procedure is objective, trustworthy, and legitimate. Graphs, statistics, and Excel tools will all be used in the data analysis process to examine the gathered data. The research will add to the body of knowledge on comparative capital market studies and offer investors useful information.

Data Analysis and Interpretation

- **Stock Exchanges**

The Stock Exchange market is a vital component of a stock market. It facilitates the transaction between traders of financial instruments and targeted buyers. Stocks not listed on a reputed stock exchange can still be traded in an 'Over The Counter Market'. However, such shares would not be highly esteemed in the stock exchange market. Generally, the Financial market can be classified into currency markets, money markets, derivative markets, and capital markets. Capital markets can be further classified into primary and secondary markets.

Securities and Exchange Board of India(SEBI) is the regulatory body of all stock exchanges in India, similar to the Financial Conduct Authority (FCA) in the United Kingdom.

London interbank market is a major component of the UK's money markets. It sets the LIBOR (London Interbank Offered Rate) interest rate, which is the interest rate banks charge when lending to each other. In the UK, the primary financial instruments in the money market are treasury bills (issued by the government) and commercial bills (issued by commercial banks), similar to the happenings in the Indian capital market.

Financial instruments in the UK can be transacted through The London Stock Exchange, one of the world's oldest and most important financial institutions. There are around 7 stock market exchanges in the UK but it is primarily traded through LSE. In variance, India has 9 stock exchanges most National Stock Exchange and Bombay Stock Exchange are of prominent importance.

LSE stands at a market capitalisation of market cap of $50.93 (Companies market Cap, 2022) (Wikipedia, 2022) Billion in comparison to NSE's market cap of US$3.4 trillion (Wikipedia, 2022) and of BSE at USD 3.56 Trillion.

There are 1.2 crore active investors (Live Mint, FY2022)in India compared to 0.33 crore investors in the UK.

Indian Equity Market has shown aggressive growth even after the pandemic beat down the economy. The Indian equity market has soared from its lows of March 2020, edging to beat the UK equity market in terms of market value and cut the chase to be among the top 5 world equity markets.

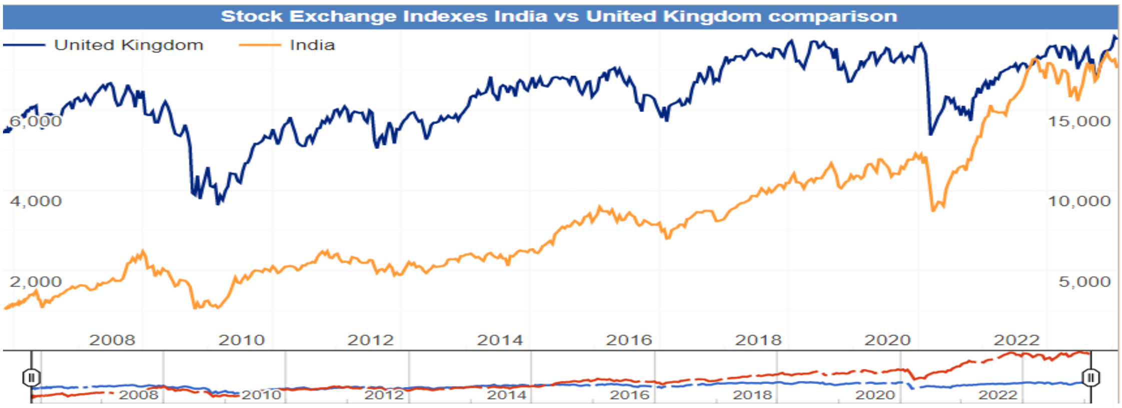
As per the Bloomberg data of the combined value of companies with a primary listing alone, the Indian equity market value stands at $3.46 trillion, representing a 37% surge this year. While the UK market value stood at $3.59 trillion, representing only a 9% surge for the same period. These numbers exclude the secondary listings and depositary receipts, which could show a far larger divergence between the two markets.

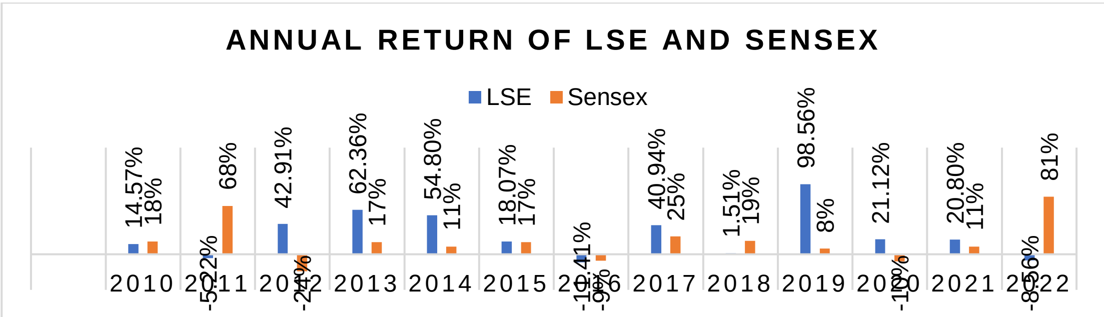
The boom seen in the Indian Equity Market was led by the higher growth potential of the Indian market and the IPO rush in the tech sector, with more Indian startup companies going public. The latter has fueled the growth, giving the developed markets good competition, as the sentiment toward the Chinese markets seems to turn sour. Indian equity market strikes as a promising domestic stock market from among the developing nations. This potential was realized and backed by a stable and reformist political base.

The failure of the UK market to keep up with its stellar performance and hold its high horse is stained by the uncertainties the Brexit concerns looming over it.

The S&P BSE Sensex index has outperformed the major national benchmarks and surged more than 130% since its March 2020 lows. The investors were handsomely rewarded with ~15% (in dollar terms) annualized RoE over five years, which is more than double of U.K.'s benchmark FTSE 100 Index returns that clocked at 6%. (Moneycontrol, 2022)

According to Goldman Sachs Group Inc., India will attain the 5 trillion dollar share market capitalization milestone by 2024. The IPOs introduced in the next 2-3 years alone would add a whopping $400 billion to the market value.





- **Investment Behaviour**

Financial analysts' perception that rationale thinking, risk perception, and rate of profitability were the only vital factors governing investment decisions has changed lately. It is essential now to also consider elements of behavioral science and human perception to judge the behavior of investors in markets as the nature of the market has changed mainly due to the injection of a more significant influence of media and influencers, especially among the new age investors. Investment behavior turns out to be a pivotal factor to study in the due process of comparison of these two financial markets with differing, risk tolerance, financial literacy rates, and consumer behavior. As it is evident India is getting into a brighter space concerning financial literacy, which turns out to be an important factor in the penetration of active investors, and positive returns and plays a vital role in making the demand side respond to supply-side interventions. However, as per the report by SEBI, only 27 percent of the population is financially literate. This highlights the need for increased financial literacy across the country, especially in Tier 2/ 3 cities and beyond. This calls for a statistic that says only 10 percent of equity investors are financially literate which can rationally infer that 90 percent of the wealth is made by 10 percent of investors. Lack of financial literacy is a key factor why a lot of retail investors invest what we call 'TIPS' in the market which might sound foreign to many countries abroad. This also boils down to the reason why most investors lose money in the capital markets of India. (BNB PARIBAS) **(Indian Brand Equity Foundation) (Security and Exchange Board of India)**

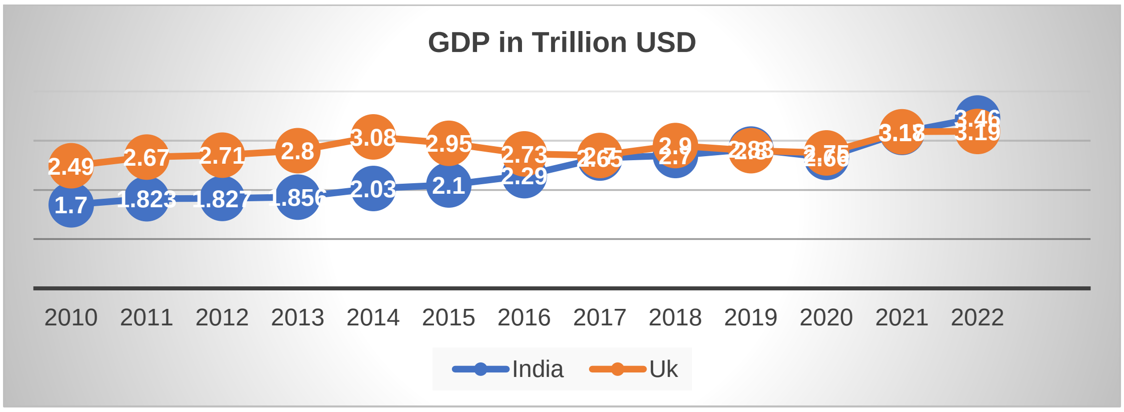
When we take into account the volume of trade 1 percent of the total volume accounts for equity trade, 9 percent amounts to intraday trades, and the rest is accumulated in future and options trade.

In respect to retail investors(who have invested less than 2 lack rupees), are hesitant to invest largely because of the lack of trust in markets (despite good returns) and greater belief in traditional instruments such as gold and fixed deposits. Indian consumer base has less risk appetite because of comparatively less per capita income. As they are less financially literate, people tend to lose money in the trial of making quick money sometimes and this reciprocates among the markets leading to a lack of trust in returns from the markets. Various fraudulent activities over time have also to a lack of trust. Institutional investors on the other side have greater control in the market by using advanced options and optimizing the opportunities in the market. Parikh (2009) proposed that the harmony of sound intellect and emotional discipline is the only way for rational behavior which Indian investors have to consciously work towards.

In a complex economy, like The United Kingdom, the capital markets play a huge role in the growth of the economy. As per the report of The Organization for Economic Co-operation and Development (OECD), the UK enjoys a 67 percent financial literacy rate as compared to other developed nations USA(57%), and Europe (71%). The market here has a greater penetration rate of active investors, higher risk appetite, and per capita income.

As people are comparatively more financially literate investors make rational decisions and get good returns compared to retail investors in India. However, the concept of fund managers and outsourcing your savings to these people is more prevalent here. Hence, there are more structured systems for NBFCs because it has a larger significance in the economy. (Impact of investment behaviour on financial markets during COVID-19: a case of UK Fanyi Wang, Ruobing Zhang, Faraz Ahmed &Syed Mir Muhammed Shah)

COVID-19 would mainly cause several financial services categories in 2020 as they are considered the opportunity for the development of sales that are restricted severely and lack the confidence of consumers However, several categories are very important and will recover well in the long go. Also, the implications of COVID-19 result in a recession, due to which the insurers are coming under an increase in pressure from the issue of price sensitivity. Individual investors are such people who purchase securities on their behalf. These investors trade in minimal amounts and are mainly involved in the activities of the stock market . It is considered acceptable for the investors to face issues while making rational and accurate decisions for funding the managers. They did not contain the relevant data or access to official information about the UK stock market, which resulted in rapid rational and logical decision-making for the investment process as it resulted in rushed decisions. It is assumed that the market and organizational factors are changing investor behaviour in the UK during COVID-19.



- **Derivatives Market**

Derivative markets play a crucial role in the financial sector, providing tools for risk management and investment. In India and the UK, derivative markets have developed over the years and are used by a wide range of participants, including commercial banks, institutional investors, and retail traders. In this essay, we will compare the derivative markets of India and the UK in terms of market structure, regulation, and product offerings.

- **Market Structure:** In India, the derivative market is dominated by the National Stock Exchange (NSE) and the Bombay Stock Exchange (BSE). These two exchanges account for the majority of derivative trading in the country. In contrast, the UK has a more fragmented derivative market, with multiple exchanges and over-the-counter (OTC) market participants. The London Stock Exchange (LSE) is the largest exchange in the UK, but it faces competition from other exchanges such as Euronext and the Intercontinental Exchange (ICE).
- **Regulation:** Both India and the UK have regulatory bodies responsible for overseeing their respective derivative markets. In India, the Securities and Exchange Board of India (SEBI) is the primary regulator of the securities market, including derivatives. SEBI sets guidelines for market participants and ensures compliance with the regulations. In the UK, the Financial Conduct Authority (FCA) is responsible for regulating the financial markets, including derivatives. The FCA sets standards for market participants and has the power to enforce compliance.

- **Product Offerings:** Both India and the UK have a wide range of derivative products available for trade. In India, the most commonly traded derivative products are futures and options on stocks, indices, and commodities. The NSE and BSE offer futures and options contracts on several underlying assets, including stocks, indices, and commodities. In the UK, a broader range of derivatives products are available, including futures, options, swaps, and other OTC products. The LSE, Euronext, and ICE all offer a wide range of derivative products, including futures and options on stocks, indices, commodities, and currencies.

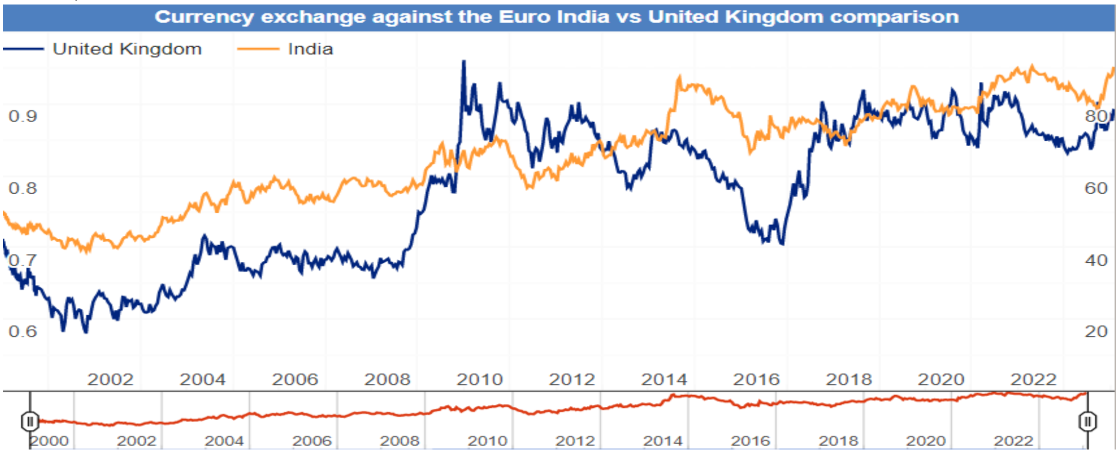
Both the derivative markets of India and the UK have their strengths and weaknesses. The Indian market is dominated by two major exchanges, the NSE and BSE, while the UK has a more fragmented market with multiple exchanges and OTC participants. In terms of regulation, both countries have regulatory bodies responsible for ensuring market integrity and compliance. In terms of product offerings, both markets offer a wide range of derivative products, with the UK having a slightly more diverse range of products available. Overall, both markets play a crucial role in their respective financial sectors and provide tools for risk management and investment.

- **Returns & Growth**
- **History Performance:** Key performance metrics, such as the benchmark index, can be used to compare the historical performance of the Indian and UK capital markets. The S&P BSE Sensex, which tracks the performance of the top 30 businesses listed on the Bombay Stock Exchange, is the benchmark index in India (BSE). The FTSE 100, which tracks the performance of the top 100 businesses listed on the London Stock Exchange, is the benchmark index for the UK (LSE).

The FTSE 100 has returned an average of about 6% over the past ten years, compared to the S&P BSE Sensex's annual return of over 10% (Moneycontrol, 2022). This shows that historically, the Indian capital market has outpaced the UK capital market.

- **Volatility:** The India VIX and the FTSE 100 Volatility Index, which represent the respective volatility indexes, can be used to compare the volatility of the Indian and UK capital markets. (Investing.com, 2022)

The India VIX has had an average reading over the past five years of about 16, whereas the FTSE 100 Volatility Index has an average reading of about 13. This shows that compared to the UK market, the Indian market is more volatile.



Sources:(Moneycontrol, 2022)

Findings

The report suggests that while the Indian market has exhibited higher returns on average, it has also shown higher risk and volatility levels than the UK market. On the other hand, the UK market has displayed more consistent performance over the years with lower levels of volatility and risk. These findings indicate that while making investment decisions, investors should consider the particular risk-return tradeoffs of each market. In particular, for the Indian market, the comparison emphasizes the necessity of regulatory reforms to improve market efficiency and stability. The comparison also sheds light on the advantages of global diversity for portfolio management, which can lower risk by investing in various markets.

Furthermore, the comparison also emphasizes how macroeconomic variables like interest rates, inflation, and political stability affect how well the two markets perform. The Indian market is more vulnerable to domestic political and economic instability and external shocks, affecting market performance. The UK market, in comparison, is more steady and resistant to such shocks, which reflects its advanced economy and institutional structure.

For the Indian capital markets, The Indian capital market is one of the most important capital markets in the world. As India's economy is snowballing, India's capital market is also following a similar trend. However, the market's problems must be removed to make the capital market more efficient and inclusive.

Conclusion

This paper compares the Indian and UK capital markets based on several factors: past performance, volatility, liquidity, returns, risks, daily traded volume, and regulatory structure. According to the data, the Indian capital market has historically outperformed the UK capital market but is also more volatile. The UK market, on the other hand, has a more stable regulatory environment and is more liquid. Before deciding to invest in any market, investors should consider these considerations, their individual investment goals, and risk tolerance. In addition, policymakers and regulators can use the report's insights to strengthen investor protection, boost market efficiency, and improve the regulatory frameworks of their respective markets.

Financial Scams, Insider trading, price manipulation, inadequate debt instruments, the decline in trade volume in regional exchanges, and low information efficiency are still a few significant problems the Indian financial system faces at a large scale. However, consistent efforts to regulate this have been sincerely made.

Based on the comparison of the Indian and UK capital markets, several suggestions can be made for investors, policymakers, and regulators

- Increase transparency
- Enhance market liquidity
- Strengthen regulatory frameworks.

Overall, comparing the Indian and UK capital markets offered helpful information on the similarities and differences between both countries, giving investors and decision-makers a chance to make well-informed choices about financial investments and regulatory frameworks. We may further our understanding of capital markets and their evolution by conducting additional research that builds on this analysis.

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