

Evolution of the Capital Markets and their Regulations in India*

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Ladies and Gentlemen,

I am honoured to be here amongst you to deliver the Rao Bahadur Kale Memorial Lecture 2009. Considering that the lectures have been annually delivered since 1937 and that illustrious personalities have delivered this lecture over the years, it is indeed an honour for me to be invited to deliver this lecture. I am thankful to the Gokhale Institute of Politics and Economics for this invitation.

During the course of my talk, I intend to share with you my understanding of the evolution of the capital markets and the regulation of the capital markets in India and what lies ahead of us. I do not intend to go too far into history let us take the year 1947 as the cut-off point.

As you all are aware, at its most basic level, the capital market is required first to enable issuers to get a diverse set of investors to invest in their projects by offering the investors a part ownership of the enterprise. This is called the primary market where the issuer is able to get investments from the investors in return for part ownership represented by the equity stock allotted to them. This in common parlance is called shares. The shares allotted to the investors may yield returns to them over a period of time, depending on the ability of the issuer to make a success of the enterprise he has undertaken. However, investors need not only returns on their investment but liquidity as well. They need to be able to get out of this investment if they spot a better opportunity or if they simply need the money to fulfil some other obligations. This would need a market for the shares issued by the issuers. This is called the secondary market in the capital market parlance. Thus, at the most basic level, the capital market will have a primary market and a secondary market.

In 1947, our primary market was subject to extensive controls under the Defense of India Rules. This might sound improbable that the defense of the country had anything to do with the primary market. The link, however, is fairly straightforward. During the Second World War, while India was still under the British rule, the colonial Government needed to raise money in order to support the war effort. The Government did not want to be crowded out by the private sector and, therefore, under the Defense of India Rules had put restrictions,

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