



WHO STOLE MY CAPITAL MARKET?

We, the Association of National Exchanges Members of India (ANMI) and BSE Brokers Forum (BBF) are associations of the Trading Members of the Stock Exchanges of India and represent the various participants of the Indian Capital Markets. Our members serve the length and breadth of our country and the world, playing significant roles as intermediaries between the investors and industries in raising the capital resources for capital formation and nation building.

Certain advertisements and articles have recently appeared in the newspapers that seem to indicate that the Securities Transaction Tax (STT) levied in the Capital Markets have not impacted the Capital Markets significantly, and the "benefits" extended to the Capital Markets in lieu of the STT is sufficient.

We believe that the STT levied on the Indian Capital Markets is hurting the efficient functioning and growth of the Indian Capital Markets. Reducing STT rates drastically immediately and phasing it out over time will bring about more VIBRANT and EFFICIENT Capital Market, where raising capital for growth from investors in India and abroad becomes easier and cheaper.

STT - A HISTORICAL PERSPECTIVE

STT was imposed w.e.f. October 2004 and in lieu of this levy, Long Term Capital Gains was reduced from 10% on listed shares to nil, Short Term Capital Gains was reduced to 10% and STT paid by investors not treating share dealings as Capital Gains was treated akin to an advance tax/TDS and adjusted against final tax liability, if any, as a rebate.

In 2005 and 2006, the rates of STT were increased across the board with reduction in tax benefits - Rate of tax on Short Term Capital Gains was increased from 10% to 15%.

In 2008, rates on delivery STT were further increased (subsequently rolled back in 2012).

In 2008, tax rebate for STT paid by investors not treating share dealings as Capital Gains was withdrawn - a levy which was loosely equivalent to "advance tax/TDS" now became the equivalent of an "excise duty".

In 2008, chargeability of STT on options traded was modified to premium value based charging and STT on exercised options was made at par with delivery STT and charged on settlement price.

This above levy and changes have affected the Capital Markets, especially the secondary markets over the period of time. The effect is brought out in the following observations

OBSERVATION 1 - A SKEWED MARKET



Post the imposition of STT and more so due to the changes in 2008 (primarily the withdrawal of the rebate), the turnover composition of the markets has been radically altered from 2004 (prior to STT regime) till date.

- The percentage of Cash Market delivery volume has fallen from 80% to 2%.
- The percentage of non-Delivery trading in the Cash Market has fallen from 20% to 6%.
- The percentage of Futures turnover (stock and index) has fallen from 20% to 15%.
- Options turnover (in notional value) as a percentage of the total turnover has increased to 77% and forms a bulk of the market. It may be noted that though the options volume in notional terms seem very high, the actual trade value is that of the premium amount, which is estimated at around 0.5% of the notional value. Thus, the transactions volumes have actually reduced.

OBSERVATION 2 - LOSS OF NATURAL GROWTH OF THE MARKET



It is generally expected that an increase in market capitalization would be accompanied by an increase in market turnover. The chart indicates the total market capitalization vs. the monthly turnover (for volumes other than options). In the Indian context, the volumes (other than options) have not kept pace with the increased market capitalization figures.

The levy of STT has stunted the Natural Growth that would have otherwise accrued to the Markets.

OBSERVATION 3 - INCREASING TURNOVER IN OTHER INDIAN MARKETS (COMMODITIES/CURRENCY)

The following table gives a comparison of the Equity Cash, Equity Futures, Equity Turnover Premium (approximate), Commodities Futures and Currency Futures Daily Average Turnover. It is apparent in the table that Options premiums are between 0.60 to 3.5% of Equity Futures and 1.6 to 2.47% of Commodities Future volumes.

Financial Year	Equity and Equity Derivatives (T/D in Rs. Cr.)				Commodities Futures Daily Average Turnover (Rs. Cr.)	Currency Futures Daily Turnover (Rs. Cr.)	Range of Equity Derivatives Volume to Equity Commodity Derivatives Volume
	Equity Daily Average Turnover (Rs. Cr.)	Equity Futures Daily Average Turnover (Rs. Cr.)	Equity Options Daily Average Turnover (Rs. Cr.)	Equity Futures Options Premium Daily Average Turnover (Rs. Cr.)			
2008-09	15,767	29,001	41	28,422	16,622	---	5%
2009-10	22,600	37,417	172	37,889	23,875	53	5%
2010-11	19,164	35,159	333	35,028	26,652	326	4%
2011-12	31,264	50,724	1,096	51,823	36,791	301	3%
2012 (1st Qtr)	15,696	30,099	1,091	31,090	15,529	370	3%

A comparative year-on-year comparison for Equity Cash and Non-Agricultural Commodities futures is furnished in the table below.

STT to the tune of almost Rs. 8577 Crore was collected in FY 2007-08. The scrutiny of STT in Capital Market and its transaction Tax on commodities and later on currencies resulted in traders, speculators and investors shifting from investments in equities market to BULLION speculation. This can be seen in the following table where turnover of equities + equities futures market went down 70% STT collection also went down 70% and Commodities derivatives market went up nearly 50% 70%.

Financial Year	Capital Market		Non-Agricultural Commodities Market		Securities Transaction Tax Collected (Rs. Cr.)
	Volumes (Rs. Cr.)	Y-o-Y Growth	Volumes (Rs. Cr.)	Y-o-Y Growth	
2007-08	16,12,300	49%	14,32,000	3%	8,071
2008-09	26,17,375	75%	14,57,612	2%	5,114
2009-10	12,15,551	45%	16,22,048	4%	7,301
2010-11	16,30,218	35%	17,24,801	5%	7,552
2011-12	24,71,819	48%	18,21,180	5%	8,288

It may be observed that STT had a negative impact on the volume and thereby even STT is coming down while the market capitalization has increased by 124%.

Absence of such levies has allowed the other markets to flourish and grow while on the other hand, the cost disadvantage lead to Capital Markets finding itself as not being able to give a value proposition to potential participants.

We have no comment to offer on whether other markets should indeed be levied with any transaction costs. Any levy would have to be seen in the light of the quantum of levy and the benefits extended against the said levy and the overall impact on the markets and the country as a whole.

However, uniform "rules of the game" between markets is being desired by market participants and if other organized markets do not have such transaction tax then it is in all fairness that it should not be levied on Capital Markets.

SUBMISSIONS

- Indian Exchanges have put in place robust systems, processes and technologies to compete with the world but it requires conducive and competitive tax structures and policy parameters.
- Shallowness of the Stock markets due to the high cost of transaction exposes it to increased volatility and high impact costs.
- Markets cannot function effectively without the co-existence of all its constituents namely Investors, Speculators, Arbitrageurs and Hedgers. It is essential for the Government and Regulators to ensure the equilibrium between their respective roles and influence over the market through the desired regulatory framework and ensuring cost structure in the form of taxes, fees and levies.
- High Powered Expert Committee headed by Mr. Parry Mehta and a committee on Financial Sector Reform headed by the current Chief Economic Advisor to GOI Mr. Raghuram Rajan have categorically recommended for phasing out of STT at the earliest.
- SEBI which is widely seen and appreciated as an independent Regulator has opined from time to time that STT is hurting the Capital Markets.
- It may be noted that STT was introduced in lieu of Capital Gain Tax to encourage long term investors and rebate of STT paid on other transactions was allowed to compensate the other constituents namely hedgers, arbitrageurs and speculators who do not get benefit of lower Capital Gain Tax. However, over the years, not only the rates of STT were increased but the rebate of STT paid was removed which has over period of time, seriously disturbed the equilibrium in the market place.
- The shifting of a component of volume from the market with STT regime to the market with non STT regime, within and outside India is evident from the turnover data and will continue further till the equilibrium in cost structure between all the related segment which deals in financial instruments are established.
- It is well known that initiating any type of transaction in the market carry high potential of loss as well as profit. The Government is justified to tax profits at appropriate rates but paying taxes on losses is extremely discouraging for any participants and affects their business models.
- In view of this, it is required that a call beyond the immediate revenue constraints be taken to address the long term needs of this market which we are sure would be much more rewarding for the country in terms of benefits it would propel through Capital Formation and Nation Building.

APPEAL TO GOVERNMENT OF INDIA

- We request:
- That STT rates be significantly reduced from the current levels and over time to abolish STT completely on all stock market transactions.
 - That rebate under Section 88C of the Income Tax Act be restored to assesses who treat share dealings as income other than that of Capital Gains.