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The Bombay Stock Exchange and BSE SENSEX: A Comprehensive Analysis of Functions, Liquidity, Investment & Trading Segments, and Major Investment Segments

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Abstract*: This research paper provides a detailed examination of the Bombay Stock Exchange (BSE) with a focus on the S&P BSE SENSEX index, encompassing its functions, investment and trading segments, and major investment strategies. The Bombay Stock Exchange, established in 1875, has emerged as one of Asia's oldest and leading stock exchanges, playing a crucial role in shaping India's financial landscape.*

The functions of the Bombay Stock Exchange are explored in detail, highlighting its role as a primary platform for Price Determination, Contribution to the Economy, Facilitates Liquidity and Transactional Safety. The investment and trading segments within the BSE are scrutinized, emphasizing the diverse range of financial instruments traded, including equities, debt instrument, and government securities. An examination of the market structure, trading mechanisms, and technological advancements within the exchange provides insights into the efficiency and competitiveness of the BSE.

Furthermore, the paper explores the major investment segments within the BSE, such as primary market offerings, secondary market transactions, and the growing presence of foreign institutional investors. The impact of economic factors, geopolitical events, and regulatory changes on investment decisions is examined to provide a comprehensive understanding of the BSE's market.

In conclusion, this research paper contributes to the existing literature by offering a comprehensive analysis of the Bombay Stock Exchange, with a specific focus on the S&P BSE SENSEX.

Keywords: BSE SENSEX

I. INTRODUCTION

The Bombay Stock Exchange, which has been in operation for 133 years, is the oldest stock exchange in Asia with a rich history spanning three centuries. What is now popularly known as BSE was established as "The Native Share & Stock Brokers' Association" in 1875.

Under the Securities Contracts (Regulation) Act of 1956, the Government of India granted permanent status to the country's first stock exchange, BSE, in 1956. It is well acknowledged that BSE played a crucial and leading role in the growth of the Indian capital market. In 1995, it transitioned from an open outcry to an online screen-based order-driven trading system.

BSE, which was previously an Association of Persons (AOP), is now a corporatised and demutualised organization formed under the provisions of the Companies Act, 1956, in accordance with the BSE (Corporatisation and Demutualisation) Scheme, 2005, as announced by the Securities and Exchange Board of India. Deutsche Börse and Singapore Exchange, two of the top exchanges in the world, are BSE's strategic partners following demutualization.

Over the last 133 years, the BSE has aided the expansion of the Indian corporate sector by ensuring efficient access to resources. Probably no significant Indian corporation has not used the BSE's facilities to raise funds from the capital market. As of right now, BSE ranks fifth globally in terms of transaction volume and first globally in terms of listed firms. As of December 31, 2007, the market capitalization was 1.79 trillion USD. There are around 4,700 listed companies from which an investor might choose.

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The S&P BSE SENSEX, often known as the BSE Index, is the first stock market index in India and is widely followed globally. It has an iconic status. It is an index consisting of thirty equities from twelve main industries. Because it is built using a "free-float" technique, the S&P BSE SENSEX is responsive to both market sentiment and reality. The BSE provides 21 indices, including 12 sectoral indices, in addition to the S&P BSE SENSEX. Deutsche Börse and BSE have signed an index collaboration agreement. Investors in Europe and America can now access S&P BSE SENSEX and other BSE indexes thanks to this agreement.

II. FUNCTIONS OF BOMBAY STOCK EXCHANGE

- **Price Determination:** The prices of securities in the secondary market are determined by their demand and supply. Thus, BSE contributes to this process by regularly valuing all listed securities. Additionally, investors can simply follow the values of these securities using the SENSEX index.
- **Contribution to the Economy:** BSE provides a trading platform for securities from various companies. Reinvestment and disinvestment occur continuously during the trading process. This provides opportunities for capital generation, fund movement, and economic growth.
- **Facilitates Liquidity:** The most significant role of the BSE is to provide a convenient platform for the sale and acquisition of securities. This gives investors the confidence that their existing securities can be converted into cash at any time. Because of this, investors have tremendous liquidity and can buy and sell at any time.
- **Transactional Safety:** BSE confirms the listing of the securities after confirming the status of the company. Additionally, all listed businesses have to abide by the guidelines established by the regulatory agency, the Securities and Exchange Board of India (SEBI).

III. INVESTMENT AND TRADING SEGMENTS

Securities listed on the Bombay Stock Exchange can be traded either directly or indirectly, depending on transaction volume. Bulk trades on the BSE are only available through licensed brokerage firms and institutional investors. Retail investors, on the other hand, have the option of conducting transactions through certified stock brokers, broking firms, or any stock investment platform. Consequently, secondary trading in India is governed by the Financial Industry Regulatory Authority (FINRA). Investors must open a demat account to conduct financial transactions using this technology.

3.1 Investment Methods

Investors can invest in a stock exchange of India through these two ways –

1. Primary Market: This market creates securities and act as a platform where firms float their new stock options and bonds for the general public to acquire. It is where companies enlist there shares for the first time.

2. Secondary Market: The secondary market is also known as the stock market; it acts as a trading platform for investors. Here, investors trade in securities without involving the companies who issued them in the first place with the help of brokers. This market is further broken down into- auction market and dealer market.

3.2 Major Investment Segment:

To raise funds for the business, all companies under the BSE can employ the following financial instrument-

Equity: The most frequent equity instruments are shares issued by a firm to raise sufficient paid-up capital for smooth business operations. A large amount of equity is raised during the primary market's initial public offering (IPO). However, due to the volatility of stock prices at this time, the issue of additional shares is subject to tight SEBI guidelines. Later, the previously raised equity is traded in the secondary market by ordinary investors via a stockbroker.

Debt Instrument: The underlying corporation offers these securities to raise capital without providing investors with ownership rights. These securities are not very risky. Investors can also trade them in primary and secondary markets, depending on the type of instrument.

Government Securities: Capital-indexed bonds, zero coupon bonds, variable rate bonds, and dated securities are common government securities that trade on the BSE.

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IV. LIQUIDITY MEASURES ON BSE

Liquidity measures are an important part of trading on the Bombay Stock Exchange. These measures affect how easily investors can purchase or sell shares on the exchange. It is easier to execute trades swiftly and fairly when there is greater liquidity. In this section, we'll look at the various liquidity measures utilized on the BSE and their impact on trading.

Trading Volume: One of the most fundamental indicators of liquidity on the BSE is trading volume. It shows how many shares are purchased and sold on the exchange during a specific time frame. Since there are more buyers and sellers in the market, a higher trading volume also translates into higher liquidity. For instance, a stock with a daily trading volume of one million shares indicates that one million shares of that stocks were purchased and sold on the BSE during that day.

Bid-Ask Spread: The bid-ask spread represents the difference between the highest price a buyer is willing to pay (bid) and the lowest price a seller is willing to accept (ask) for a security. A narrow bid-ask spread shows increased liquidity because there is little difference between what buyers are ready to pay and what sellers are asking for. Conversely, a large bid-ask spread denotes reduced liquidity because it shows a big gap between sellers' asking prices and buyers' willingness to pay.

Market Depth: Market depth refers to the number of orders available for a specific asset at various price levels. Higher liquidity is indicated by a deep market because there are several orders available at various price points. As a result, investors can purchase or sell a lot of securities without having a big impact on the market price. Conversely, a shallow market denotes less liquidity because there aren't enough orders available at various price points. This implies that in order to execute their deals, investors could have to accept a less advantageous price.

Turnover Ratio: The turnover ratio is calculated by dividing the total market capitalization of all listed firms by the total value of shares traded on the exchange. A higher turnover ratio suggests greater liquidity because there is a large volume of trading relative to the market's size. This implies that securities can be bought and sold by investors with ease and without having a big effect on the market price.

Impact Cost: The impact cost is the expense incurred by an investor when executing a trade of a specific size. It is determined by contrasting the trade's execution price with the going rate in the market at the time of the trade. Higher liquidity is indicated by a reduced impact cost since it is simpler to conduct deals at a fair price without appreciably impacting the market price. Conversely, a higher impact cost denotes less liquidity because it is more challenging to make trades without materially shifting the market price.Each liquidity measure on the BSE offers a distinct viewpoint on the ease of trading on the market. Although each of these metrics is significant, traders ought to focus on the ones that are most pertinent to their trading approaches. For instance, a long-term investor could concentrate on turnover ratio and market depth, whereas a day trader might concentrate on trading volume and bid-ask spread. All things considered, investors need a deep and liquid market in order to execute trades quickly and fairly.

V. MAJOR INDICES IN BSE

The primary index of the Bombay Stock Exchange is the Sensex. It is a free float market-weighted index that measures the performance of India's top 30 firms. As a result, the BSE share market uses the Sensex to track the performance of these companies in order to forecast whether the Indian capital market would fall or rise in response to stock price movements.

Apart from the benchmark index, BSE offers other sectoral indices. Some of them are –

1.S&P BSE Auto
2.S&P BSE Bankex
3. S&P BSE Capital Goods
4. S&P BSE Consumer Durables
5. S&P BSE Fast Moving Consumer Goods

Furthermore, the BSE has created indices that categorize companies into small and mid-cap depending on market capitalization. They are referred to as the BSE small-cap and BSE midcap indexes. Furthermore, index mutual funds that seek to profit from these companies' capital appreciation can track these indices.

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VI. REVIEW OF LITERATURE

Balan and Srinivasan (2017), in the study of determinants of share price in BSE, using multiple regression, found that DPS and sales are significant variables among various financial variables considered for study.

Sharif, et al. (2015), in the study of factors affecting share price in Bahrain Stock Exchange, during the period of 2010-2016, using regression, found that ROE, Book Value per share, DPS, Dividend Yield, PE and Firm Size are significant determinants of share price in Bahrain stock market.

Almumani (2014), in the study of determinants of share prices of banking stock in Amman Stock Exchange during the period of 2005-2011, by using ratios, correlation, linear multiple regression, found that Book Value, EPS, PE and Firm Size are significant determinants.

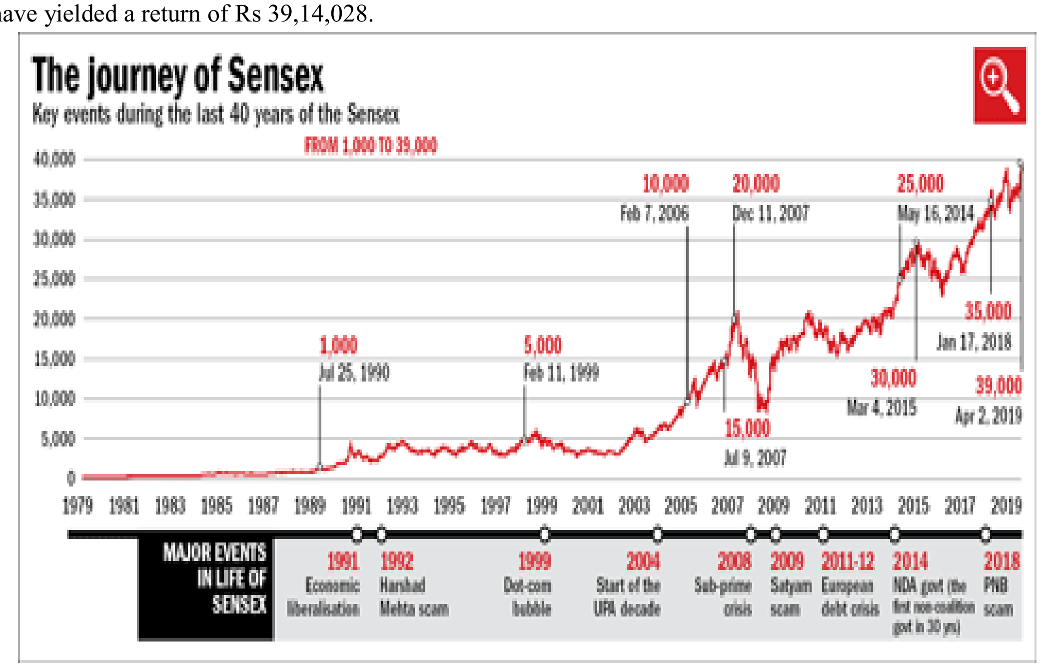
Menike and Prabath (2014), conducted a study to measure the impact of accounting variables on stock prices in Colombo Stock Exchange, Sri Lanka during the period of 2008-2012 and found that DPS, EPS, Book Value of share have significant impact.

Tandon and Malhotra, (2013) found that EPS, Book Value per share, P/E Ratio have significant impact in determining the share price in NSE. The study used correlation and multiple regression using the data of 2007- 2012.

Gill, et al. (2012), conducted a study on American Firms and found that EPS, DPS, P/E Ratio are found significant in determining the share price of equity shares during 2009-2011.

VII. RESEARCH METHODOLOGY

The term 'Sensex' is a mix of 'sensitive' and 'index'. Sensex is India's first real-time index. Sensex was introduced on April 1, 1986, but its base year was established as April 1, 1979, with a value of 100. This means that though the history of the Sensex is available from 1979, it came into being only from 1986. Examining its past, the Sensex yielded a 16.1% compound annual growth rate between 1979 and 2019. Until 1986, when the Sensex was not available but was traced back, the returns were 27.9 percent CAGR. After its inception in 1986, it returned 13.7% per year on average. Since 1979, gold has grown 45 times (CAGR 10%), but the Sensex has grown 390 times (CAGR 16.1%). In 1979, Rs 10,000 invested in gold would have transformed into Rs 4,50,620 by 2019. Investing the same amount in the Sensex would have yielded a return of Rs 39,14,028.



VIII. CONCLUSION

Sensex is an indicator of the movements in the Indian stock market. A rise in it indicates that the stocks have gone up for that particular period. However, the ride was never smooth. The investors who have survived the crisis namely- the market crash of 2008 will agree that surviving another day was the only way to make money from stock markets. Undoubtedly the market crash of 2008 was a global financial crisis and made things rough for the India stock market as well. But during the following 5 years i.e. 2008-2013, **the SENSEX went up by 150% boasting a CAGR of 20%.** The ones who pulled their money out during this period and choose to "stay safe" clearly missed the opportunity. Therefore, it is essential to understand the volatile nature of the market. The market can appreciate any time as economic cycles turn.

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