

A comparative Study of Chinese and Indian Stock Markets

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Abstract

Both China and India are developing countries with large population and low revenue. This article mainly makes a comparative analysis of the macro environment of Chinese and Indian stock markets and their perspective features. The aim is to investigate the relationships between Indian stock markets and Chinese stock markets. Using Indian and Chinese stock price daily data over the period 1991 to 2019, we found price and spillovers effect from Indian stock market to Chinese stock market and vice versa.

Keywords: China, India, stock markets, price, spillover

1. Introduction

Both in terms of stock policy and in terms of stock efficiency, Chinese stock market lags behind other fields in the aspect of reform. This situation exerts unfavorable influences upon the overall reform effects. In the view that Indian stock market is a typical representative among all developing countries and that Indian stock market is faced with the same development task with China, it will be of great significance for both of the two countries to investigate the developmental process of the two countries and analyze the experiences in stock markets and corporate system.

Modelling stock price volatility is an emerging and challenging task in the financial econometrics literature, especially with the operation of financial globalization in the economy. This is primarily due to the random walk behaviour of stock time series, which is historical in nature with little/no to white noise. An understanding of stock price dynamics and its integration is fundamental to speculation, derivative pricing, risk management and real option valuation. Therefore, an accurate model is required to optimize the basic objectives of the rational investors. To them, volatility means the securities are not pricing fairly as it should.

2. The Development History of Chinese and Indian Stock Markets

The Indian stock market is older than China's and is more inclusive, market-oriented and internationalized. However, it took China just three decades to attain the development that the Indian stock market gained over more than a century. As China's stock market continues to expedite its opening-up process, foreign investment institutions are expected to be facilitated further. The Indian stock market is known as the oldest in Asia. The Bombay Stock Exchange (BSE), Asia's first stock exchange, was founded in 1875 in Mumbai. At present, India has two principal national exchanges: the BSE and the National Stock Exchange of India (NSE), established in Mumbai in 1992.

Relatively, China's stock market started later. The Shanghai Stock Exchange (SSE) was established at the end of 1990, and the Shenzhen Stock Exchange (SZSE) was established half a year later. In one word, an overall comparison of the Chinese and Indian stock markets makes it evident that Indian stock market is obviously in the lead. Compared with Indian stock market, Chinese stock market system lags behind far away in the aspects of the number of stock markets, the number of listed companies, the structure of stock markets, the market system and the market operation mechanism, etc. However, the institutional gap of this market system has obviously affected the actual economic development and future development potential of the two countries. In the following, this paper will make a detailed analysis of the differences between Chinese and Indian stock markets in terms of market development pattern, the corporate structure of listed companies and stock market supervision.

Table 1. Comparison of Chinese and Indian Stock Markets

Items	Countries	China	India
Main board stock market		Two (Shanghai Stock Exchange & Shenzhen Stock Exchange)	Two (Bombay Stock Exchange and National Stock Exchange)
Local regional market		0	21 (Networked)
Number of listed companies		1300	More than 10,000
Stock Market History		21 years	More than 100 years
Difference of transaction system		equity division	All in circulation
Average daily trading volume in national stocks		14 billion RMB	Equals to 40 billion RMB
World ranking in total trading volume		Far behind India	The third or the fourth
Ratio of total stock market capitalization to GDP		12% (In circulation)	More than 80%
Main board enterprises' listing capital threshold (RMB)		50 million	80 million
The dominant force in the stock market		Government policy dominance	Market allocation mechanism
Listed Corporate Governance Score (CLSA)		4.3	6.6
Stock Market Performance		Shares split into a multi-year bear market quagmire	vigorous upward country's economic development

2. A Detailed Comparative Analysis of Chinese and Indian Stock Markets

2.1 Comparison of Chinese and Indian Stock Markets in Terms of Corporate Governance Structure of Listed Companies

One prominent feature of Indian stock market lies in the fact that the supervision section conducts an extremely strict investigation into companies which apply for a listing. More importantly, the Indian law endows the supervision section with great supervision and management rights. It is exactly due to this extremely strict investigation, Indian listed companies are generally high quality. The purpose of listing is to strive for further expansion and development. The market value of Indian stock market is highly related to the operation performance of listed companies. Thus, the financing function and investing function of the capital market are put to good use. Among the list companies, quite a lot are stocks of private enterprises which are circulation stock companies. Therefore, their corporate governance capacity is relatively high and they have the stock market culture of taking responsibility for the value of the stockholders. Thus, almost all Indian listed companies take their initiatives in stabilizing the corporate structure, optimizing the corporate system and strengthening corporate governance.

The characteristics of the governance structure of listed companies in China are mainly shown in the following aspects.

1). There are many kinds of stocks issued by listed companies. Shareholders of different kinds of stocks have different influences on the corporate governance structure. There are both A shares and B shares in all stocks issued by companies listed in Shenzhen and Shanghai. A shares include national legal person shares, social legal person shares, labor shares and social public shares. B shares contain foreign capital legal person shares, foreign capital shares, shares of social legal persons within the borders and individual shares within the borders. Therefore, there are

a large number of parties that have direct or indirect interest relations with the company, which makes the governance structure of listed companies in China become more complex due to the extensive scopes involved. 2). The shareholding structure is dominated by non-mainstream common shares such as state shares and legal person shares, especially the state shares. The shareholding structure is, thereby, unreasonable. 3). The debt proportion of listed companies is small, leading to unreasonable bond structure. 4). Internal directors account for the vast majority in the board of directors. Therefore, the unreasonable structure of the board of directors leads to the imbalance of power.

Generally speaking, listed companies in India have diversified shareholdings, while listed companies in China is characterized by the single-large shareholder. The single-large shareholder of China's listed companies makes the listed companies behave as strong stock holders. As the state-owned share property rights of strong shareholders are not clear, the phenomenon of insider control is prominent.

2.2 Comparison of Issuing Pattern and Trading Pattern of Chinese and Indian Stock Markets

India has loosened regulation in the stock issuance market, and laid emphasis on broadening the market foundation, improving market liquidity, strengthening risk management and maintaining market stability in the circulation market. In 1992, the "Capital Issue Control Act (1947)" was repealed. Under the guidance of relevant regulatory rules, enterprises have the right to obtain market financing opportunities. Companies planning to issue shares can issue securities without prior approval from the government, but only after obtaining approval from the Securities and Exchange Board of India. In 1995, India implemented the bidding pricing method in the IPO pricing, thus improving the efficiency of stock issuance. The examination and approval system was adopted at the beginning of stock issuance in China, and replaced by the approval system since March 2001. The approval system means that before issuing securities, the issuer should not only disclose the true information about the issuance of securities, but also comply with the essential conditions for issuing securities stipulated in the Company Law and the Securities Law. The securities authority has the right to reject applications for securities issuance that do not meet the material requirements. The current issue price in China is "negotiated between the issuer and the lead underwriter," and it is likely that the two will form a "community of interests" to set a lower price to ensure the success of the offering and the lowest possible risk. This still leaves a huge price gap between the primary and secondary markets.

India's mandatory electronic trading of stock exchanges is mainly to promote the screen and computer transformation of stock exchanges, modernize the means of trading and increase the transparency of trading, which plays a positive role in improving market efficiency. Following international practice, the stock exchange has adopted an electronic online trading matching system, abolished the open outcry system, improved the efficiency of market price discovery, reduced transaction costs, and replaced most scrip physical transactions with electronic and paperless transactions. In 2002, close to international practices, India implemented T+3 settlement system and further T+2 settlement system. Technological developments in the settlement of Indian stock transactions have contributed powerfully to the improvement of market efficiency. All the major exchanges in India have established Settlement Guarantee Funds (SGFs) to ensure timely settlement of stock trades. Especially, in times of intense market volatility, the rapidness and high efficiency of settlement system play an important role in maintaining market liquidity and stability. Each exchange center has established a settlement center, which effectively reduces the counterparty risk of the settlement system.

Different from the multi-level stock market in India, China's stock market has a single level. Before 1999, China's stock market had formed a multi-level structure consisting of Shanghai and Shenzhen stock exchanges, SATQ and NET stock exchange markets and 27 local stock exchange centers. With the development of the national financial risk prevention work, the local trading center and the legal person stock market have been cleaned up one after another, forming the current highly concentrated stock circulation mainly concentrated re-exchange pattern, in addition to the agent stock transfer system (i.e., the third board market) as the place for the stock transfer of delisted companies. On the whole, the level of China's stock market has the characteristics of singleness. Under the current market pattern, the difference between Shanghai and Shenzhen stock markets is only geographical, but there is no division of labor and hierarchical relationship between them in business and function. They are highly homogenous in trading varieties, listed company size, trading and regulatory mechanism, and even market trends.

By comparing the issuance pattern and trading pattern of the Chinese and Indian stock markets, it is not difficult to see that an important measure for the development of the Indian capital market is to commit to the internationalization and liberalization of the capital market, allowing private mutual funds, foreign institutional investors and state funds to enter the capital market. For China, as a developing country, there is a strong demand for capital from all sides, which cannot be met by attracting domestic savings alone. Formulating relevant regulations to

attract foreign investment through domestic and foreign capital markets is of great help to increase the amount of capital in the capital market and further regulate the market.

2.3 A comparison of Stock Market Regulation in China and India

Strict supervision is the basic guarantee for the effective operation of the Indian securities market and the high quality of the management of listed companies. The Securities and Exchange Board of India supervises the operation of the securities market, rigorously examines and approves the trading rules of the securities market, and grasps the information feedback from the secondary market advisory committee and the stock exchange. The Indian government announced in early 1992 to set up in 1988 of India's securities and exchange commission (SEC) as the legal management committee of the capital market, to the management of the necessary power, namely the inspection on various mutual funds and all kinds of stock exchange, to control of commercial bank's bank in the morning, decided to broker intermediary such as registration procedure, Make the Securities and Exchange Commission the regulator for new securities issued by the company. In October 1995, the Government of India also promulgated the Securities and Exchange Commission Regulation Act, which defined the scope of fraud and unfair trading in the securities market and gave the Securities and Exchange Commission of India certain powers to stop such practices. The Indian government also approved the creation of the National Stock Exchange of India in 1994 to regulate and integrate the country's securities markets. So far, the Securities Commission of India has approved lending restrictions that allow foreign individuals, companies, hedge funds and others to register directly in the Indian securities market.

The government has stepped up its oversight of illegal trading and taken other important steps, building on the extensive control measures taken over the past few years and the correction of irregularities in daily trading. 1) Merge the Financial Oversight Board and the Advisory Board to control and supervise commercial banks, financial institutions and non-bank financial companies. 2) Lowering the validity period of bank receipts from 30 days to 15 days, and imposing penalties on units and individuals who violate the regulations. 3) Amend the punitive provisions to enable the Reserve Bank to impose heavier penalties for violations of guidelines and guidelines. 4) Allow brokers to participate in interbank securities trading within the trading system of the National Stock Exchange. 5) Prior approval from the Reserve Bank is required before the introduction of the Securities Trading Services System. 6) Appoint a working group to investigate the internal management and audit of the Bank. 7) Develop a plan to investigate the situation of defaulting debtors and publicize the intentional defaulters. These measures will monitor, control and punish violations from different perspectives and at different levels to minimize violations in the capital market.

With the development of the securities market, the supervision system of China's securities market has undergone a process from decentralization and multiple supervision to centralized and unified supervision. Especially since the China Securities Regulatory Commission (CSRC) unified supervision of the market in 1997, the market size has been expanding continuously, which marks that China's securities market has begun to take the road of having laws to follow and governing the market according to law. In 1999, according to the requirements of the Securities Law, a new Issuance Audit Committee was established and the Regulations on the Issuance Audit Committee of Shares was issued. In 2000, we further reformed the stock issuance system, abolished the approval system, and began to implement the management system of recommendation by the lead underwriter, examination by the issuing bank audit committee, and approval by the China Securities Regulatory Commission. On February 22, 2001, the CSRC issued the "Measures for Suspension and Termination of Listing of Loss-making Listed Companies" according to the "Company Law", and began to launch the withdrawal mechanism of listed companies. With the advance of the marketization of China's stock market, the thinking of securities supervision in China has correspondingly undergone a major change, from the original thinking of controlling and supervising with strong planning color to the thinking of revealing risks following the law of market operation. However, a large number of irregularities exist in China's stock market at present, such as fraudulent listing, financial fraud, institutional cooperation, insider trading, malicious speculation and other illegal and irregular behaviors occur from time to time, which indicates that the supervision level of China's securities market needs to be improved. There are still some problems in the market supervision, such as the lack of independence of the supervision department, the lack of long-term system construction, the low efficiency of supervision, and the lack of institutional guarantee for the protection of investors, especially small and medium-sized investors.

In a word, the centralized and unified market supervision system, the law and regulation system with information disclosure as the core, and the strict market supervision rules make India have a high level of stock market supervision. From the perspective of the construction of China's stock market supervision system, a centralized and

unified supervision system has been initially formed and the market system has been constantly improved. But in general, the level of market supervision still needs to be improved, and the laws and regulations and systems need to be further improved.

3. Policy Recommendations for Improving China's Stock Market Learning From Indian Experience

3.1 Solve the Problem of "Post-Split Shares" and Optimize the Corporate Governance Structure

India has implemented worldwide unified stock with "full circulation", running ahead in all aspects. The reform of non-tradable shares of China's listed companies which started on May 9, 2005 was basically completed at the end of 2006. According to the provisions of the "notice about issues related with the pilot reform of non-tradable shares of listed companies" proposed by the Securities and Futures Commission, the non-tradable shares of listed companies should not be listed and circulated within 12 months ever since the date of getting the right to receive; likewise, the number of non-tradable shares held by shareholders holding more than 5% shall not exceed 5% of the total share capital within 12 to 24 months from the date of obtaining the tradable right; the number of the above shareholders shall not exceed 10% of the total share capital within 12 to 36 months from the date of obtaining the tradable right. Since June 2006, the non-tradable shares with the right of circulation have been listed and circulated, which would have a certain impact on the market. In December 2009, the statutory lockup period ended. This would coincide with a three-fold increase in the market capitalisation. If the shareholders of non-tradable shares all reduce their holdings, and the incremental capital of the market does not enter the market in the same proportion, the result of market expansion may lead to excessive blood loss and collapse. Therefore, it is of great practical significance to analyze the motivation of non-tradable stock shareholders to reduce their holdings and to calculate the amount of reduction quantitatively, and to study the measures to stabilize the market on this basis.

3.2 Establish Effective Supervision System and Perfect Market Supervision

The existing problems in China's securities market are mainly caused by historical reasons, but the lack of market supervision and legal means is also an important reason. In order to change the irregular operation of the securities market and effectively protect the interests of investors, it is especially necessary to attract and manage the foreign capital appropriately. Therefore, it is necessary to draw lessons from international practices to strengthen market supervision and establish an orderly competitive market order and a perfect market supervision system by learning and studying the experience of international securities supervision. The problems that can be solved by the market should be solved by the market. The government should transform direct market intervention into indirect market regulation and establish a regulatory system with market regulation as the main part and government regulation as the auxiliary part, so as to fundamentally improve the regulatory efficiency of the securities market. As for the challenges to market supervision caused by foreign capital entry, the regulatory authorities should pay close attention to the changes of domestic and foreign economic factors, study the transmission mechanism and ripple effect of foreign capital entry on the mainland stock market, fully study and summarize the rules, and take effective measures as far as possible to weaken the adverse effects. In addition, economic tax measures can also be adopted, such as levying different taxes on different time and amount of inward and outward remittance of funds, so as to limit the unreasonable flow of funds.

4. Conclusion

A well-regulated information disclosure system is the most important core factor of security market and security development. It not only helps to make decisions, but also helps the market price mechanism to play a role. The stock market reflects the information by the stock price and its fluctuation. When the information is sufficient and true, the stock price will be correctly determined and the allocation of resources will be optimized. Only then can the function of the stock market be brought into full play and the efficiency of the market be gradually improved. According to the principle of national treatment of the World Trade Organization, foreign investors must enjoy equal information status with domestic investors. Therefore, China must establish an international information disclosure system with standardized accounting system as the core as soon as possible, requiring listed companies to provide financial information and accounting data in accordance with international standards in a timely, open and fair manner to reduce the differences with international practices. Only in this way can China's securities market move towards the track of healthy development, provide a good market environment for foreign institutional investors, and create a good market atmosphere for attracting more foreign investment into the market.

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