Mini Presentation on PPI for Activities Auxiliary for Financial Services (India)
<table>
<thead>
<tr>
<th>Section</th>
<th>Division</th>
<th>Group</th>
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<tbody>
<tr>
<td>K – Financial and Insurance Activities</td>
<td>K – Financial and Insurance Activities</td>
<td>66- Other Financial activities</td>
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<tr>
<td></td>
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<td>66- Activities auxiliary to financial service and insurance activities</td>
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<td>663- Fund management activities</td>
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<tr>
<td>6611</td>
<td>Administration of financial markets (includes operation and supervision of financial market other than by public authorities, such as commodity contracts exchange, securities exchanges, stock exchanges stock or commodity option exchanges)</td>
<td>6611-</td>
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<td>6612</td>
<td>Security and commodity contracts brokerage (includes dealing in financial markets on behalf of others (e.g. stock broking) and related activities, securities brokerage, commodity contracts</td>
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<td>6619</td>
<td>Activities auxiliary to financial service activities n.e.c. (includes activities of investment advisors, mortgage advisors and brokers, financial transaction processing and settlement activities, trustee,</td>
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<td>6630</td>
<td>Fund management activities</td>
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<td>66302- Management of pension funds</td>
<td>66309- Management of other investment funds</td>
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COVERAGE

STOCK MARKET

Primary Market

Secondary Market

Bonds

Mutual Funds

Initial Public Offering

Stock

Derivatives

Stocks

Currency

Interest Rate
• Weights to be based on the relative share of each product in the securities market.
TRANSACTION COST

EXPLICIT COST

- Stocks & Derivatives
  - Brokerage Commission
  - Stamp Duty
  - Service Tax
  - Custody Charges

- Mutual Funds
  - Expense Ratio
  - Exit Load

- Corporate Bonds
  - Brokerage
  - Underwriter
  - Lead Arranger’s Fee
  - Annual Listing Fee
  - Initial Listing Fee
  - Trustee Fee
  - Printing, Advertisement and Distribution

- IPO
  - Underwriter’s Discount
  - Legal Advisory Cost
  - Financial Reporting Advisor
  - Printing
  - Registration fee
  - Exchange Listing Fee
TRANSACTION COST

IMPLICIT COST

Bid- ask Spread

Realised Spread

Opportunity cost of delayed execution or non execution
Factors Affecting Transaction Cost

1. Clearance and Settlement System: Cost differs for transactions based on the settlement system (delivery, non-delivery, squared up or carried forward).

2. Investor Profile: Institutional investors (Mutual funds, FII’s) pay lower brokerage than retail investors.

3. After trade practises: The cost like custody charges (higher for securities in physical form) vary depending on whether the shares are held in physical or dematerialised form.

4. Margins: Margins are different across different investors also forms an important part of the transaction cost.
• Some costs are measured on the basis of the volume of trade (brokerage commission), some are measured as flat rate on pre-transaction basis (custodian fee).

• Thus, to bring uniformity costs can be converted into basis points. (Raju M T and Marathe V, 1999)
Transaction cost

- To calculate transaction cost, following services can be included

1. Brokerage fee
2. Stamp duty
3. Custody Charges (Physical)
   - Safekeeping
   - Transaction fee
4. Custody Charges (Demat)
   - Safekeeping
   - Transaction fee
   * Buy
   * Sell
SOME APPROACHES
Effective Bid – ask Spread
(Raju M T, Karande K and Taneja S, 2002)

• Consider **percentage effective half spread** as a measure (price) of execution cost.

• **Effective half spread** is the difference between the trade price and the quote mid-point.

  where;

  **Trade price** is the price at which a security is currently selling

  **Quote mid point** is calculated as \([(A_{it} + B_{it})/2]\) where;

<table>
<thead>
<tr>
<th>(A_{it})</th>
<th>Ask Price (minimum price a seller is willing to receive for the security I at time T)</th>
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<tbody>
<tr>
<td>(B_{it})</td>
<td>Bid Price (maximum price a buyer is willing to pay for the security I at time T)</td>
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</tbody>
</table>
Numerically the measure of trading cost reflecting execution cost due to trading inside the quotations (trading at a price within the bid and ask price) is:

Effective percentage half spread \( it = \frac{100(Pit - Mit)}{Mit} \)

Where:

<table>
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<th>( Mit )</th>
<th>Quote Mid point price ( [(Ait + Bit)/2] )</th>
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<tr>
<td>( Pit )</td>
<td>Transaction Price (Price at which a security I is currently selling at time t)</td>
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Global Trading Cost
(Elkins/McSherry (E/M) )

• Total Trading Cost: Includes Commissions, fees and market impact.
Definitions

• **Average stock price:**
  - Average traded stock price in US Dollars in that country.

• **Average Fees:**
  - Average fee paid in that country.

• **Market Impact:**
  - Average cost of trading in that country.
  - Average cost to trade versus volume weighted average price
  - Alternatively, difference between the trade executed price and average of stock’s high, low, opening and closing price during trade date.
• Volume Weighted Average Price:
  - Ratio of sum of dollars traded for every transaction (price multiplied by number of shares traded) to the total shares traded for the day

• Total:
  - Total cost of trading in the country
  - Sum of costs of commission, fees and market impact
Total Trading cost, India

Value in US Dollar ($)

Year  Value
1997  70
1998  60
1999  60
2000  110
2001  80
2002  70
2003  70
2004  80
2005  70
2006  70
2007  80
2008  80
2009  90
2010  80
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THANK YOU