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T+1 SETTLEMENT CYCLE: WHAT IT MEANS FOR INVESTORS

Relevant for: Economy | Topic: Issues relating to Growth & Development - Capital Market & SEBI

Sebi is planning to implement allotment of shares in T+1 which is currently T+2. As a stock market investor, if a person buys shares of any company in BSE or NSE today, he will get transfer of shares in his DMAT account in trade + 2 days (T+2). Thereafter he can sell his shares or hold it. On the other side, the investor selling the shares will get funds transferred in his account within T+48 hours. Now this settlement is proposed to be T+1 day. Earlier till year 2003 settlement cycle was T+3 days.

The settlement cycle in stock markets refers to the time between the trade date, when an order is executed in the market, and the settlement date, when participants exchange cash for securities or shares. Sebi has given the option to exchanges to adopt T+1 based on their readiness from year 2022. The Sebi circular states that if the stock exchange wants to opt for the T+2 settlement cycle in between, it will have to give notice one month in advance.

What is the intention of Sebi behind bringing this new arrangement of settlement?

On the request of market participants, SEBI has come up with this proposal to change trade settlement cycle to T+1 which means shares will now be transferred in T+24 hours.

SEBI has taken this move in consultation with market infrastructure institutions such as stock exchanges, clearing corporations and depositors. A few market players have express their concerns on operation problems in this arrangement of T+1 settlement.

Reducing the settlement cycle will create greater efficiencies in the market and further protect investors' interest. Accelerating the settlement cycle will help reduce operational risk, liquidity needs, counterparty risk which would also reduce margin requirements and collateral requirements for broker-dealers.

What is means for different types of investors?

This move will be much beneficial to large volume investors like corporates, FIIs, DIIs, who invest large amounts. One day earlier settlement can give them more liquidity and reduce margin requirement. While for small or retail investor it shall not impact much in T+1 day settlement.

However, it is worth stating here that retail individual investors contribute 45% of daily trading volumes on exchanges and balance 55% comprises of corporates, FIIs, DIIs, proprietary traders and others.

What are the advantages and disadvantages for common investors of the T+1 settlement cycle?

It will provide investors with earlier receipt of their funds post trade execution and settlement. Further, many operational and market risks can be mitigated.

Moving to a T+1 settlement cycle is a complex undertaking and will require significant planning, execution, and testing and it would fundamentally change market structure.

We believe if infrastructure is upgraded with robust technology and settlement process to be made fast and seamless the probabilities of technical glitches can be mitigated.

Will the new cycle of settlement make any difference to the volatility in the market?

Volatility in the market will definitely increase and investors have to closely keep an eye on their new bets. Most of the stock exchanges in developed countries like USA, UK & Japan currently follow T+2 trade settlement cycle.

There will be the complexities in this arrangement but reducing the settlement cycle will generate greater operational efficiencies and substantially lower capital requirements. We recommend to do the pilot testing for two days and if it works well than it can be extended to one week and on its successful testing it can be implemented permanently.

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