

## **A 'Legitimate' Business Activity: Unofficial Stock Exchanges of Vijayawada**

S. ANANTH

**T**he history of the unofficial, illegal stock exchanges that operated in Vijayawada, Andhra Pradesh offers fascinating insights into the economic and cultural life of small towns and cities (non-metropolitan regions), and their response to the changing business environment in the immediate aftermath of globalisation and liberalisation in the early 1990s. But there is a far larger significance to the story that I would like to tell here. It has to do with the social and cultural foundations of economic activity in general, which social scientists have tended to underplay or completely ignore. The unofficial, illegal exchanges that thrived for a brief period in the 1990s were not shady organisations operating from some obscure corner of the town. Instead, they functioned openly and were the centres of phenomenal economic activity by the standards of the region. They used state-of-the-art technologies, which at that time were not available to most stock exchanges in the country. Further, their illegal status meant nothing to the populace, which accorded them high social respectability. The causes for this social respectability and widespread acceptance, despite their illegality, deserve greater attention. The leaders in the exchange shared the stage with important constitutional functionaries: Governors, Chief Ministers, Union and State Ministers among others. Indeed, this perceptible gap between legality and legitimacy throws up a number of interesting questions for the social scientist. The study of informal, unofficial exchanges of Vijayawada is necessary in order to understand the business culture of the region, how speculation operated at the ground level in the early 1990s, and other such region-specific issues. The history that I attempt to reconstruct here is of a business institution's social and cultural foundations. At this level of generality, the stock exchanges of Vijayawada are useful points of entry into a larger research problem.

Even the casual observer is struck by the way these stock exchanges leveraged the formal institutions to conduct and further their businesses – often along far more efficient lines than those carried out by their formal counterparts in different parts of the country. Quite clearly, small-town and provincial city businesses and networks were able to channelise capital from surrounding regions, often in competition with the metropolitan regions. How were they able to do so? That too when they were not even supposed to exist, according to the law. How do we understand this gap between the law and illegal reality?

Vijayawada, reputed to be the finance capital of Andhra Pradesh, housed five stock exchanges including the largest unofficial and illegal exchanges of the 1990s. These exchanges functioned just as any other legitimate business activity, often using state institutions to further their business interests. A detailed study of this phenomenon is imperative: not only to understand the investment behaviour of people in the region in the early years of the post-liberalisation era, but to also to counter the view, propagated by neo-liberals, that most 'unorganised' businesses lack sophistication, which arrives only with globalisation.

The largest of the exchanges was the Vijayawada Share Brokers Welfare Association (VSBWA). This and the other Vijayawada exchanges did not have the approval of any higher governmental authority or the larger 'official' exchanges in India (for example, the Bombay Stock Exchange). I focus here on VSBWA, which was an obvious choice of study in that the other Vijayawada exchanges were much smaller in terms of both membership and volume. Very often the smaller exchanges, namely Vijayawada Share Dealers Association, Delta Share Brokers Exchange, Vijayawada Stock Exchange and Andhra Stock Exchange, would imitate the systems and practices that existed in VSBWA. Apart from the Vijayawada Share Dealers Association (VSDA, popularly known as the 'one town exchange'), the others were only marginal players.

The following account is based on sources ranging from newspaper reports, court records, case files and records of the exchanges of Vijayawada. Most importantly, face-to-face interviews with the major players of the exchanges have been used to piece together a chapter of the city's history that a number of key participants are only too willing to forget. Information has been difficult to come by and is full of vast gaps. Nevertheless, it is valuable.

### **Beginnings of Stock Exchanges in Vijayawada**

Vijayawada has been known for its entrepreneurial and innovative spirit and the risks that people here are willing to take. This is also evident from the manner in which the exchanges functioned. Around 1988-89, a savvy set of five or six brokers who operated in Vijayawada thought that their business would be better off if congregated at one place, and if they tried to 'match' and consolidate the buying and selling of orders that might exist amongst themselves. The brokers realised that they had a lot of common orders. Consolidating the orders would help them to avoid paying large commissions to Bombay- and Madras-based brokers. Consolidation would enable them to reduce commissions to their clients. The participant brokers claim that the idea of establishing a stock exchange sprung from this 'matching' activity. The predominant motive behind this was the strong belief that an exchange would provide greater liquidity for them.

In 1990, the existing brokers who were already trading amongst themselves informally entered into an agreement, and a Memorandum of Articles was signed to facilitate mutual trading. The Vijayawada Share Brokers Welfare Association, VSBWA, was registered under the Societies Registration Act XXI of 1860 at Bandar (the district headquarters) on 23 June 1990 (registration number 194 of 1990). The initial list consisted of 21 members (the maximum permissible). Gaddipati Satyanarayana (a Kamma), T. Srinivasu (a Vysya), C. Nageswara Rao (a Kamma), and Gopal Biyani (a Marwari) were appointed as founding president, vice-president, general secretary and treasurer respectively. The office bearers reflected the social composition of those involved in the exchange, which was drawing to it all the important and dominant trading communities in the region – Kammass, Vysyass and Marwaris. Very few of the brokers were worried about the unofficial status of the exchange. Thus the registration process only formalised the informal 'matching' with the ongoing mutuality between the traders taking the shape of an association.

Though the exchange was registered in 1990, for about a year it did not undertake any trading activity. Trading in the exchange was formally inaugurated by the then- Union Minister of Commerce Pranab Mukherjee, on 10 November 1991. Surprisingly, the unofficial status of the exchange did not seem to be an issue even for the minister. The visit of the minister along with various other high-profile personalities provided great legitimacy to the exchange in the early days of its existence. This legitimacy continued till about 1996. It is of course possible that at this point of time it was not clear to anyone outside the association that the grouping was going to be a stock exchange. Immediately after its registration, the only activity the exchange undertook was to provide its members with more information about quotations and other trade-related data.

### **Organisational Structure and Membership**

According to its bylaws, the management of the association was to be carried out by an executive committee of seven members, including the office bearers. The designated office bearers included the president, vice-president, general secretary and treasurer. In practice, the members of executive were co-opted by the president from among the members of the association. The number of executive members was subsequently increased to nine, including the office bearers. Each member of the executive committee held office for one year from the date of election. This was subsequently modified, and all office bearers and executive committee members held office for a period of two years. This system was later modified to include 'eminent' local citizens as part of the executive committee. An important criterion for a non-member to be co-opted as a member of the executive committee was that they had to have the knowledge of the stock market and should be a *peddamanishi* (lit. 'big man' in Telugu; usually refers to a prominent or respectable person) in the city. The office bearers and the executive committee were popularly referred to as the 'committee'.

The exchange called for membership in three different phases. The first phase was immediately after the registration of the society. There seems to have been very little rush to become members. Membership was given to people who paid Rs 7,500. During the

second phase, applicants paid Rs 15,000 for membership. The last phase was characterised by extreme demand (about 1000 applications) for membership, and the fee was Rs 30,000. Applicants exerted pressure on the office bearers; some had their cases recommended by ministers, members of the legislative assembly and members of parliament. The members increased from about 20 at the time of the initial registration to about 73 (in early 1990), and finally rose to about 287 at the end of the membership drive in 1991. The first expansion was carried out in order to accommodate the large clients who were already in business under the brokers of the exchange. The second expansion was carried out due to the increasing popularity of the exchange, and pressure from various sections to grant membership. Each member was allowed two trading assistants. At its height, the card value quoted as high as Rs 8 lakh.

During this first phase, friends, acquaintances and relatives of existing members were enrolled as members. This informal nature of enrolment was in tune with the general procedures at the exchange and the economic activity in the region in general. Business in the region thrives on an informal culture that may shock an outsider. Law, courts, and other formal institutions are brought into the picture only when there is a collapse of the informal order. This general pattern, it soon became clear, was repeated even in VSBWA.

The erstwhile office bearers, however, proudly proclaim that they followed strict 'procedures' in the selection process. In personal interviews, Koneru Vasudeva Rao, the treasurer of the exchange during its zenith, claimed the exchange took care to select "only educated young people". He denies that caste or other considerations had any role to play. Most of the old hands, however, deny that a rigorous selection procedure was followed.

One member closely associated with the exchange argues that the exchange was very careful while selecting members. The exchange selected only those who would be 'useful' to the growth of the institution. For people to meet this criterion, they had to be either prominent speculators/traders, or financiers, or *peddamanushulu*, eminent/prominent citizens. A large number of *peddamanushulu* were given free membership. One broker estimates that about 10% of the total membership was allocated in this manner. *Peddamanushulu* were selected from a range of fields, and included criminals-turned-politicians, government officials who were given *benami* membership (under assumed names), and leading professionals. Some of these people paid for their membership, and this category is said to have included police officers, journalists, and of course the leaders of local criminal gangs which have had a considerable presence in all spheres of life in the town, including its economic activity. Among the journalists who were active in the exchange were Anka Babu (of the daily newspaper *Udayam*) and Venkateswarulu (the then- finance manager of the newspaper *Andhra Jyothi*) – two prominent citizens of Vijayawada at that time. It is difficult to believe that the selection procedure was objective in a situation where 'recommendations' or references are an essential part of the business culture.

### Trading and Settlement Practices

Interestingly, VSBWA was far ahead of the official exchanges such as the Bombay Stock Exchange (henceforth referred to as BSE) in its trading and settlement practices. It followed

a weekly settlement (Monday to Friday). This was in contrast to the official exchanges such as BSE, which normally followed a fortnightly settlement. Exchange office-bearers proudly point out that unlike the BSE, which would often merge settlements (leading to delayed payments), the VSBWA never followed this practice. The pay-in and pay-out was always completed as scheduled.<sup>1</sup>

A unique aspect of the VSBWA was the time of trading. There were two sessions in a day: from 9.30 am to 11.00 am, and from 4.00 pm to 5.00 pm. There was trading on Saturday from 9.00 am to 11.00 am. The Vijayawada bourses were the only exchanges in India that had Saturday trading. These timings were in complete contrast to the official stock exchanges, which trade between 10 am and 3.30 pm. The timings in Vijayawada exchanges gave the smart traders excellent arbitrage opportunities. They could buy in one exchange at a discount and sell in another exchange.

A distinctive feature of the exchange was the rules governing new listings of company shares that were eligible for trading – there were none. This seems to have attracted speculators from different parts of India to this bourse. The erstwhile office bearers claim that the exchange had clear-cut rules for a company to start trading of its shares on the Vijayawada bourse. They claim that any person who wanted to trade in a particular stock/share had to furnish evidence that trade had commenced in that counter in any of the official exchanges of the country, and then members were allowed to begin trading in that counter. Critics of the committee claim that this rule was selectively used. Traders who were considered to be supporters of the committee would be given a free hand to deal in the shares of any companies, while opponents of the committee would have to abide by the letter and spirit of the rule. This caused some consternation among the opponents, as they believed that the committee was unjustly curtailing their business. Never mind the fact that these practices were illegal.

The VSBWA claimed to be trading in about 220 companies in 1992; by 1993, when the exchange activity had reached its peak, about 400 companies were involved in trading. The average daily volume of the exchange gradually increased to about Rs 20 crores in 1992, and Rs 30 crores by 1993. In this year the VSBWA reached its zenith, supposedly reaching a gross volume of between Rs 2,500 and Rs 3,000 crores. In a letter to the Chief Editor of *Eenadu*, the largest Telugu daily newspaper, the VSBWA claimed that in 1994-95 they had recorded a gross volume of Rs 4,600 crores. The volumes were far more than the average daily volumes of the official regional exchange, the Hyderabad Stock Exchange. A comparison with some of the other official stock exchanges provides greater evidence of the phenomenal success of the VSBWA. In 1990, the Cochin Stock Exchange had 476 members while the Ahmedabad Stock Exchange had 295, the Delhi Stock Exchange 124, and the Bangalore Stock Exchange had 233 members. In the Cochin Stock Exchange, about 200-250 companies were traded, and daily trading volume increased to about Rs 8 crores in 1989. VSBWA was about twice the size of the Cochin Stock Exchange, which was the biggest in South India and the fourth-largest in the country after Bombay, Calcutta and Delhi.

The success of the Vijayawada bourses was extended due to what came to be known as the 'grey' market – a completely illegal market within an illegal and unofficial market. This

'grey' market trading was frowned upon by a number of brokers and was considered to be speculative beyond acceptable levels.

The 'grey' market was speculation in its purest form. Here trading would start even before an Initial Public Offering (IPO) had closed its subscription. Two brokers would enter into trades (buying and selling) and would sign undated contract notes. These would not be submitted to the exchange; instead, these trades would be submitted and settled only after the exchange permitted regular trading at a later date. Thus, no cash actually changed hands at the 'grey' market stage. Initial public offerings of a number of fly-by-night companies were sold to unknowing investors by getting news published about the fictitious premiums that their issues were trading in at the Vijayawada bourses, in the grey market. The use of the term 'grey' market in an unofficial and illegal exchange is worth noting. It indicates that the members of the exchange had a clear sense what was legitimate and what was not.

### **Stock Financing (*Badla*) in VSBWA**

In the 1990s, every recognised stock exchange in India was allowed to operate a stock lending and borrowing mechanism, known as the *badla* system. It has traditionally been the mechanism used for financing stock purchases by speculators. However, in the official stock exchanges the rules, regulations as well as margin requirements are clearly indicated to the lender as well as borrower. In the 1990s, a large part of the speculation in all the stock was financed through this *badla* system. In this system, the lender keeps the stocks purchased as security while collecting interest for the monies lent. The official stock exchanges guarantee the genuineness of the stocks deposited as security.

The success of all the Vijayawada stock exchanges was in large measure due to the *badla* system that was practised in the region. One broker in a personal interview proudly declared that in the Vijayawada exchange "there were no payment crises and the only risk that existed was the market risk". This was in sharp contrast to the official exchanges, which often faced such problems. The secret of this success was the variant of the '*badla* finance' that was followed in Vijayawada. Interestingly the *badla* system continued to exist in Vijayawada even after Securities and Exchange Board of India (henceforth SEBI) banned *badla* in the official exchanges. In fact, this system existed as long as the exchanges remained in existence.

*Badla* financing was largely restricted to VSBWA and VSDA, but practised in all the local exchanges. There were two parts to the *badla* system. The first part was a private agreement in good faith between the borrower and the lender, and the second part, when the exchange agrees to guarantee the trade in which the duly entered agreement is formalised in the exchange system. In the first part of the *badla* transaction, two people – one borrower and one lender – would agree to finance either a security or some securities that a broker had to take delivery of in the settlement. The lender would take the delivery of the securities on behalf of the borrower and would lend the money. However, this taking delivery on behalf of the borrower was the informal agreement. The money would be given

to the borrower in the form of a cheque, as in the case of any other borrowing transaction. This transaction would complete the first part of the deal. In the second part, immediately after taking delivery of the securities, the *badla* financier who took the delivery would enter into a contract with the broker. The broker (who had borrowed the money in the first place) would buy back the securities at cost plus 1% or 2%, in a post-dated contract note.

This post-dated contract would be submitted to the exchange on the agreed date, usually the very beginning of next settlement day. Once it was submitted, the exchange would guarantee the trade. This carry forward could be continued for as long as the borrower and financier wished to. In case the financier was not willing to carry on with this arrangement into the next settlement, the borrower would either find a new financier, or would simply renegotiate the interest rates and offer higher interest. Such high returns (4% or more in a month) led to the increased participation of financiers in the exchanges.

The consequence of this easy availability of *badla* is difficult to gauge. Clearly, it led to increased speculation. Many financiers and businessmen purchased membership, only to lend money through *badla*. A significant number of rice mill owners, and even a local MLA's brother known for his criminal activities, were lending large amounts to brokers through this *badla*. The press estimated that there were about 120 *badla* financiers in the two main exchanges, VSBWA and VSDA (*Indian Express*, 18 November 1995, 27 October 1997, p. 1). Rough estimates of *badla* are put at about Rs 20 crores per settlement (essentially on a weekly basis) at the peak of the exchange's activities. A rough calculation indicates that *badla*-based volumes amounted to over Rs 900 crores; this translates into roughly 25-50% of the gross volume, based on the gross volume figures declared by VSBWA.

### **Nature of Trading in Vijayawada**

Most of the trading was speculative in nature, as with most stock exchanges, but only much more so, though the office bearers of the always played down this aspect of their business. In a number of instances (especially during the annual general meetings) the office bearers themselves declared that their aim was to reduce speculation: they estimated the volumes of speculative trading at 60% of the total trading, and the aim of the exchange was to decrease this to about 40%, supposedly.

The VSBWA regularly advertised its virtues, including the claim that it was a solid "systems"-based company with "an unblemished track record", and which gave a high priority to investor protection. The exchange frequently advertised its commitment to "maintenance of high standards, exercising expertise in trading settlement, implementing self-regulating systems, creating awareness among investors, educating investors in investment skills and tuning our services to suit the changes in the market scene" and "pioneers in the stock market cult in the state" [sic] (*Eenadu*, 15 August 1993, p. 6).

What exactly were these "systems"?

And did they really function as efficiently as was claimed?

One such "system" was that of settlement, which undoubtedly worked well. Its smooth functioning attracted various groups. The Trade Guarantee Fund was another. A fund of this

type did not exist in any of the official exchanges of India. The local exchanges claimed that this was one of the 'advanced systems' in place in Vijayawada that did not exist even in Bombay Stock Exchange, the oldest and largest bourse. Such a fund would mean that investors would be paid by a separate exchange controlled fund in case of default by a broker who may have entered a trade. The other system that existed but only on paper was the Investor Grievance Cell (henceforth referred to as IGC). The IGC was constituted with three eminent individuals as its members. These *peddamanushulu* from the city were selected by the president of the Exchange Committee. But they actually took up very few cases, and nearly all the members concur that there was very little chance for an aggrieved investor to get justice from the internal mechanisms that existed within the stock exchange. The only time the IGC preformed its duties fully was when both the aggrieved parties were brokers. Small wonder that most of the investors opted to take their grievances to the *panchayats* of the local criminal syndicates. But there was little an aggrieved party could do if the problem was a part of the structural deficiency of the exchange itself. The president was the final arbiter in any issue, and his factional approach allegedly created more problems.

### **Decline and Collapse of the VSBWA**

The actual trigger for the closure of the exchange was a court case filed by Rama Koteswara Rao, a leading financier in Vijayawada who was also a *badla* financier in the exchange. The case was filed through a proxy. The reason for the proxy, according to him, was that he wanted to avoid the impression that there was a personal loss and hence revenge motive in the filing of the case. A dispute arose between him and the exchange when the latter refused to pay him money amounting to over Rs 5 lakhs that he was owed in Settlement 42.<sup>2</sup> At a later date he was paid a little over Rs 2 lakhs. After the failure of efforts to get the money through the usual local 'settlement' methods of approaching and involving *peddamanushulu*, he filed a case in the Andhra Pradesh High Court (Writ Petition No. 11523/1995 on 29.9.1995).

The court's single bench was willing to let VSBWA off after ordering it to apologise, as the legal authorities viewed the case primarily as a minor breach of trust and not a major offence. Moreover, the legality of the exchange itself did not come under scrutiny. One may even believe that the 'legitimate business' paradigm operated even as far as the court was concerned. The exchanged faced problems only after the petitioners filed a writ in the AP High Court against the single bench decision, following which it went to the full bench and was heard by the Chief Justice. The High Court instructed SEBI to depute officials to study the exchange. After investigation SEBI conceded that VSBWA and VSDA were "indulging in the sale and purchase of securities which is illegal and contrary to the provisions of the Securities Contract (Regulation) Act, 1956".

The initial response of the members of the exchange was very typical of Vijayawada's business groups: they were confident that their connections and respectability would help them overcome the crisis. When asked by a local Telugu business paper about the court

case, Nagabhusanam (the president of the exchange) responded, "Nothing will happen just because three investors have gone to the court. [The exchange] still enjoys the confidence of four lakh investors in Vijayawada" (*Money Business*, 22-28 July 1995, p. 3). Members continued to claim that they were unaware of the legal status of the exchange, a claim difficult to believe. The ignorance of the members seems shocking in light of the statements made by SEBI from time to time. The local papers prominently covered the statements of G.V. Ramakrishna, the then chairman of SEBI, who clearly announced that such exchanges were illegal, and that SEBI had written to the state authorities to take necessary action. Newspaper articles were already questioning the status of the exchange. Interestingly, in March 1995 M.S.N. Reddy, one of the members of the exchange, had lodged a specific complaint to the Union Ministry of Finance, and the Central Bureau of Investigation. The Finance Ministry replied in June 1995 that it had "instructed the Securities and Exchange Board of India, the District Magistrate and the Police authorities at Vijayawada to take action against promoters/organisations for running the unrecognised stock exchange" (letter dated 15 June 1995; reference no F.1/17/SE/95, signed by V. Sachdeva, Section Officer, Ministry of Finance).

The role of the press merits special attention here. In the case of Vijayawada, considering that the newspapers were at that point of time the only sources of information about the local exchanges (and since the publicity till mid-1995 was all positive), the middle classes seem to have become convinced from local news coverage that the neighbourhood stock exchange was a very convenient and short road to wealth. Common press coverage was of the record levels of Bombay Stock Exchange Sensitive Index (Sensex) and the increased amount of foreign investment and the record subscription procured for the new offerings of companies keen on selling their shares.

Structural problems and the general bearishness that set in the markets had a great deal to do with the demise of the exchange. Bad deliveries, fake certificates and frauds increasingly made investors weary and suspicious, and most brokers agree that this led to greater risks and reduced interest in stock market speculation. Speculative capital went in search of new avenues, and there was a gradual withdrawal from the local exchange. The onset of a bear market in 1995 led to investors becoming gradually disillusioned with the potential of stocks. The internal squabbling of the exchange, and the court cases in which it was implicated, occurred at the time of the birth of National Stock Exchange (NSE), which might be interpreted as the final blow to the Vijayawada bourse. With a screen-based national market and the practice of low commissions, accompanied by an excellent price discovery mechanism, NSE made the open outcry system (or trading hall where members jostle to execute an order) of even the legal, official traditional exchanges redundant. VSBWA did not stand a chance against such a competitor. The Vijayawada exchanges also became a major centre for transactions in fake shares. It was easy to sell these locally, as there was little or no institutional protocol in place to protect investors and brokers.

Selling such shares in an official exchange would have been a problem for brokers, due to various penal provisions that could be applied. This was not the case in Vijayawada.

Since early 1995, the illegal bourses had been facing various kinds of pressures due to bad media publicity. Income tax raids, SEBI accusations, denunciation by the finance ministry, all had affected the public image of the exchange; and a series of defaults and scams involving members led to the disintegration of the trading systems. Fake shares were one of the major problems with the exchange. A report in the *Deccan Chronicle* cited the case of 1600 fake share certificates of UTI Master Gain. This report also cited the case of a dispute arbitrator (in Vijayawada, a *peddamanishi*) who forced one party to hand over 30,000 fake shares to their rivals.

The case of fake Essar Shipping shares is quite unique. About 2000 shares were sent to the share transfer agent in Madras (Data Soft Research Company Limited); these shares were returned with a letter declaring that the shares were fake. Interestingly, the police refused to even register a case (*Deccan Chronicle*, 10 July 1995, p. 17).

The strength of VSBWA had been its reputation, founded in the assurance to investors that it had a smooth settlement system in which there would be no delays in pay-in and pay-out. The collapse of broking outfits destroyed the bourse's foundations. The largest such collapse was that of Mega Corp Securities Private Limited, which had been promoted by 13 members of VSBWA. Its chairman was T. Srinivasu, who was also the general secretary of VSBWA. The total amount defaulted had been estimated at Rs 60 lakhs (*Eenadu*, 7 July 1995, p. 5). However, local brokers in personal interviews claim that it was about Rs 2 crores. In a number of ways, the collapse of Mega Corp Securities marked the beginning of the bourse's decline.

### The Success of VSBWA

The unofficial, illegal exchanges of Vijayawada were a phenomenal success. Such was the popularity of the stock trading pioneered by VSBWA that it was estimated that there were about 2,978 brokers (including brokers and their authorised agents but excluding sub-brokers) at a time when the total population of the city was estimated at about 800,000. At its peak in 1994-95, the exchange claimed that its "gross total volumes were about Rs 4,000 crores" (VSBWA/PR.PB/95/3367 dated 22.07.95), while the Vijayawada Share Dealers Association (VSDA) claimed that its turnover in the first nine months of 1994-95 was Rs 1,653 crores (*Eenadu*, City Edition, 13 January 1995).

The success of VSBWA was largely due to the fact that they were one of the first organisations to initiate the process of marketing stocks like any other financial product. In a personal interview, Shyam Prasad, one of the early brokers, said that "people sold shares in Vijayawada as if they were cereals and jaggery".

The ease with which people could find a broker aided the process of rapid trading. This ease with which trading could be done led the entry of a large number of people who had little or no knowledge of speculation and investment.

VSBWA was indeed an organisation that pioneered cutting-edge technologies in trading and related technologies, including trading software, much before they were introduced by any of the official exchanges. In some cases their pioneering work had not even been

thought of by the official exchanges, and their ideas foresaw future developments in the country – for example, screen-based trading, which was the unique feature of the National Stock Exchange. From 1993 (about six months after the establishment of satellite television channels in Vijayawada), the exchanges started broadcasting real-time quotes on the local network, via the Master Channel. A significant intervention took place in mid-1994: the exchange contracted CMC Limited (at that point of time, a government undertaking) to design and implement a screen-based online trading system, which the VSBWA called 'MEGA PROJECT', for the Vijayawada exchange. The CMC was paid about Rs 1 crore and 20 lakhs for the software and basic hardware, while WIPRO Acer was paid about Rs 60 lakhs for providing members with computer terminals and other accessories. The BSE subsequently introduced a system based on similar software.

### Legality and Social Acceptability

Why were the unofficial stock exchanges in Vijayawada such a roaring success? The visibility of the stock exchange and the stockbroking community in Vijayawada's social and economic life seems to have led many people to believe that trading was not illegal, though it was conducted through an unofficial exchange. This impression held till mid-1995. By late July 1995, increasing number of income tax raids and talk about SEBI enquiries, along with the news of defaults, slowly changed the general attitude towards the exchange. People began to believe that there was 'something seriously wrong'. It is plausible that the VSBWA and VSDA did not expect the State to really crack the whip. The members seem to have believed that they had sufficient 'contacts' and influence to regularise their exchange. The exchange even issued press statements that SEBI would clear their proposal to establish an official stock exchange (*The Economic Times*, 15 March 1997).

The broking community (along with print media and local cable channel) which played a substantial role in the coverage it gave to the Vijayawada stock exchanges may be considered to be largely responsible for the growth and the subsequent collapse of these exchanges. Most of the prominent dailies (except *The Hindu*; coincidentally *Business Line*, an associate publication of *The Hindu*, was the first to carry a news item that all was not well with the exchange) carried the VSBWA's daily stock quotes, as well as those of the other official exchanges. This practice had been started by *Enadu*, and was continued by others. They even carried the *badla* rates on Saturday, along with the *badla* rates of the BSE. This led a number of investors to believe that it was safe to trade in the exchange. In case any client had a doubt, the broker would always convince them, saying that he would be a guarantor to their trades. This created complacency among the investors, and it was in the interest of the brokers to foster such a lack of vigilance.

The fact that the unofficial exchanges prospered in Vijayawada should not surprise people familiar with the nature of the town's business practices. Trading and speculation were not something new to Vijayawada culture. The prosperity of the surrounding areas led to the city attracting large amounts of surplus capital, which was in turn deployed in trading and related activities long before the establishment of the stock exchange.

Stock trading and speculation had become increasingly accepted largely because a large number of people seem to think that it is one of the few means to make quick profits. The concept of rapid and easy profit is ingrained in the culture of Vijayawada, due to the large petty-bourgeois class in the region. Vijayawada is unique in that it is probably one of the few regions in India where nearly all the *big/grande* bourgeois elements have petty-bourgeois origins. The latter, aspiring to join the ranks of the rich, believe that stock market trading and speculating is one of the few opportunities available for their social advancement. Trading was a successful practice also because it was associated with all the important sections of Vijayawada society and economy. The participation or support of nearly all the powerful elements of local society (financiers, gang leaders, journalists, police), along with the fact of huge sums of money being at the disposal of the exchange, also meant that people were not willing to antagonise them.

Despite their illegality, Vijayawada stock exchanges were not taboo. They were the nerve centres of speculation, trading and financing activity. They took up various activities, including the organising of New Year celebrations where members and their families were invited and given expensive gifts. One area of the exchange deserves special mention: the active organising of seminars in Vijayawada. The exchange invited well-known members of the stock-broking fraternity, financial administrators and government functionaries. These included Pranab Mukherjee for the inauguration of the trading floor, M. Narasimham, former governor of the Reserve Bank of India, Sundar Iyyar, Director of Bombay Stock Exchange, and M.R. Mayya, former Executive Director of BSE. These events were largely public relations exercises to reinforce claims to legality rather than aimed at actual investor education and protection.

The experience of the unofficial, illegal exchanges clearly indicates that as long as they functioned, these organisations worked in a manner that was no different from official organisations. The fact that they operated and thrived in a system that was reinforced by existent formal networks merely adds to the dichotomy of Indian business culture. Weber (1930:22) believed that the stock exchanges are places which "rationalise speculation", but in the case of Vijayawada exchanges seemed to have been places that allowed speculation to flourish unhindered as long as it was profitable for capital. Once the risks involved in speculation far exceeded the rewards, the market place rather than governmental action killed off these speculative unregulated enterprises. The Vijayawada exchanges seem to have aggravated the modern regulatory dilemma that has essentially followed the Weberian paradigm – regulating the individual speculator (or the financial strength of the speculator), rather than curbing speculation itself. Weber in his study of agricultural commodity exchanges believed that it was impossible to stop speculation; therefore it was better to regulate the class of speculators rather than trying to curb speculation itself. Such regulation would reduce the possibility of systemic collapse. The case of Vijayawada exchanges seem to suggest that Indian regulators, like their international counterparts, believe this to be the easier option.

A large part of this research was funded by a liberal grant from the Sarai Independent Fellowship Programme, 2004-05. This is a modified version of the paper presented at the Sarai Independent Fellowship Workshop held in Delhi in August 2005.

## NOTES

1. There are different stages in stock market trading. Executing a trade is just one part of stock market transaction. The settlement of the transaction is essentially a back office operation and takes place after the end of the trading period (known as settlement). All the trades are settled by way of paying cash (on the part of the buyers) and delivering securities/shares (on the part of the sellers). The pay-in denotes a period when both the parties to complete their payment and then lodge their securities (as may be the case). Pay-out is a term used to denote disbursement of the cash and securities. In the past, the BSE followed a system where the trades were settled on a monthly basis, in order to allow investors from non-metropolitan areas to send money and share certificates. As it was believed that this led to rampant speculation, this was reduced to two weeks. Vijayawada exchanges had a weekly settlement system, one of the first in the country.
2. At the end of each week, trades in the bourse are settled through the giving of cash or the delivery of stocks. A settlement number is assigned by the exchange to all transactions of that particular week; 1 April being the start of the financial year, the trades of that week fall within Settlement 1. Settlement 42 can thus be identified as a transaction that took place 42 weeks from this date.

## REFERENCE

Weber, Max. *The Protestant Ethic and the Spirit of Capitalism* (George Allen & Unwin, 1930, London).