Our Views

Instant settlement of transaction - Days of day trading are numbered

As we know, a trade settlement cycle is the period within which securities are delivered and funds are transferred after a trade is executed between a buyer and a seller. Obviously, an efficient settlement cycle enables quick ownership transfer and availability of funds. A faster settlement therefore enhances liquidity in the market and is better for all stakeholders.

A few decades ago, our equity settlements and delivery system took at least 30 days and sometimes even several months. Over time, the settlement cycle was gradually made more efficient and came down to T+2 days. This brought India at par with the rest of the developed world in terms of efficiency of capital markets. In another major step, in 2021, SEBI announced a move towards T+1 day settlement which not only better aligns India to the global trends, but in fact is amongst the best in the world.

Now, as the full implementation of T+1 settlement across all scrips is rolled out wholly by October 1, 2023, the SEBI Chairperson has communicated about an intended move towards real-time settlement. In her press briefing in the month of July earlier this year, she mentioned that “One of the things that we think is not very far off is an instantaneous settlement on the stock exchanges. We are currently working on that; we are engaged with the ecosystem, and we believe that not in the very far future we will have a mechanism which will facilitate instantaneous settlement of transactions on the stock exchange. Our markets moved from T+2 to T+1 but the technology stack that we have makes it possible to bring in a mechanism wherein trades can be settled instantaneously with entities getting money and the securities. We believe that in cash equity segment where T+1 exists, instant settlement can be done.” This, if achieved, will be revolutionary across global markets and will in fact set a new global standard.

The big question being debated is that a large segment of the market depends on day trading which is a non-delivery-based trading. Day traders try to draw profits from intra-day price fluctuations by buying and selling shares during the same trading day. They close all open positions by the end of the day and have no delivery pending or cash payable in the settlement cycle. The net gain or loss for the day is taken by the trader. At present, there are several such day traders operating in the market who in a way also provide significant liquidity and volumes in the market.

If we move to an instant settlement system, the concept of day trading will undergo a change. Every trade will have to be paid for and securities delivered. On first read, it appears that instant settlement will significantly reduce market volumes – the ability of day traders to trade all through the day without owning money or securities must result in larger volume.

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However, it is not entirely so. Even day trading requires a minimum margin money to be placed as a security cover for any adverse price movements. The day traders can use the same margin money to trade under instant settlement mechanism. They will receive immediate delivery of securities which can be offered back to sell again. This cycle can be rotated multiple times within the day across multiple securities. Effectively, it would mean churning the money (which is presently used as a margin) for settlement and rebooking all through the day.

In my view, the way Future and Options replaced the traditional badla system and in effect made the system more robust, future ready and secured; the instantaneous trading mechanism will also only improve the volumes in the market rather than restricting it.

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