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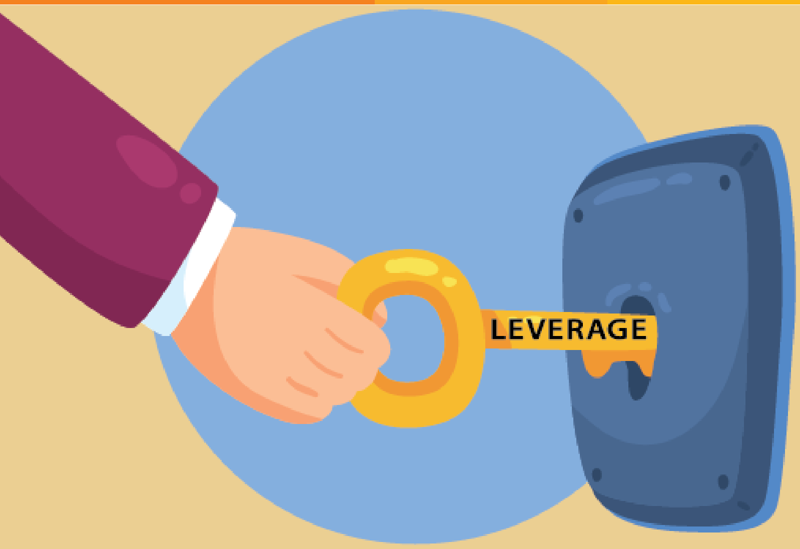
The Financial Kaleidoscope
Defining the different shapes of investment

June – September 2021



Introduction To Margin Trading

From The Editor's Desk

Dear Readers,

Firstly, we regret the delay in bringing out this edition of the newsletter. We would like to assure readers that we shall attempt to publish the future issues of the newsletter in timely manner.

Compounding and leveraging money are two critical aspects of investing and wealth creation and certain instances amid the constant ups and downs of the stock market offer plenty investment opportunities. However, leveraging these opportunities is not always possible due to limited cash reserves available with most retail investors.

Margin trading is one such concept that allows investors to trade in equities by paying only a part (or margin) instead of full consideration value of the trade. This is enabled by a broker who funds the balance amount and charges interest to client. The margin can be settled later by squaring off open position.

Since there are many factors involved in the process, margin trading facility is practiced more often by seasoned investors than a novice. It takes a fair amount of time to understand the workings of margin trading, so it is always advisable to consult a professional financial or investment planner.

To help you get an understanding, in this edition of The Financial Kaleidoscope, we are covering the basics of margin and margin trading. This is not financial advice, but a beginner's guide in the form of some basic questions you may have before starting.

NSDL is now present on LinkedIn. Please visit https://www.linkedin.com/company/national-securities-and-depository-limited to keep updated about NSDL webinars etc.

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Regards,
NSDL – Your Depository

Overview of Margin Trading

What is margin?

Let's take an example. You want to buy 100 shares of ABC Limited which is priced at ₹1,000 per share. The transaction value will be ₹1,00,000. Assuming there is nothing like margin, you will need to pay ₹1,00,000 to broker at the time of placing your buy order.

Now, assuming your broker is providing 50% margin facility, you can invest in those shares by paying just ₹50,000. The balance amount is funded by the broker and squared off at settlement.

So, in the context of stock markets, margin is the total amount or extent of leverage available to an investor. There are certain rules prescribed by stock exchanges which need to be followed by your stock broker regarding the extent of margin that can be available to you. This may vary from stock to stock and from time to time.

What is margin trading?

Having understood the meaning of Margin, it is easy to understand what Margin Trading is. In simple words, it is a facility provided by stock broker to clients whereby a client can buy or sell securities without paying 100% amount upfront towards purchase consideration or 100% shares that are sold.

The part paid by the investor is called 'Margin' and the portion that is not paid is the leverage given to client by the broker.

Investor can pay the margin in form of cash (not hard cash – by way of bank transfer) or by depositing securities. Securities provided as margin are also known as 'Collateral'.

What is rational behind Margin Requirements and Margin Trading?

1. Margin trading helps investors to buy securities of their choice without paying the full amount of money beforehand. They can make money when the earning from the trade is more than the margin.
2. Margin Trading helps in increasing trade volumes.
3. By enforcing margin requirements, exchange controls the trading activity in the market.
4. Margin requirements are used by exchanges to manage settlement risks.

What Are the Different Types of Margins?

There are different types of margins applicable to equity trading in India. Each has its own rational. Let's have a look at the types of margins for cash segment –

Value at Risk (VaR) Margin or Initial Margin (IM)

It is intended to cover the largest loss that can be encountered on 99% of the days. For liquid stocks, the margin covers one-day losses while for illiquid stocks, it covers three-day losses to allow the exchange to liquidate the position over three days.

Extreme Loss Margin (ELM) Margin

It is a second line of defense to cover extended losses that go beyond 99% risk which is covered under the VaR margin.

Mark to Market (MTM) Margin

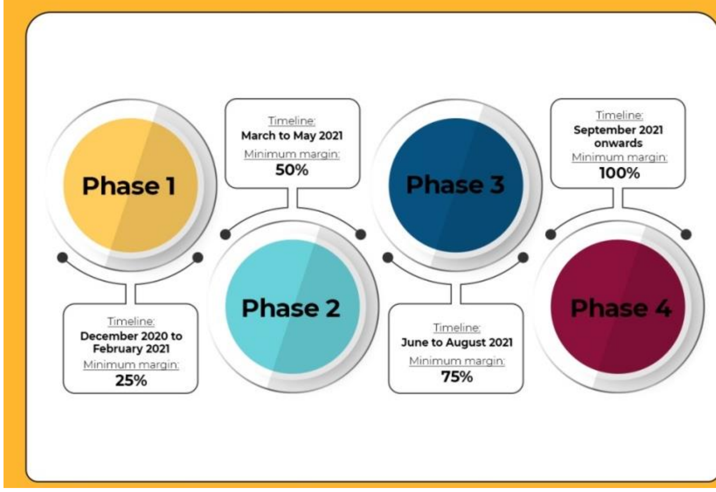
MTM is calculated on all open positions of an investor on any trading day as difference between transaction price and the closing price of the share. If the closing price is less than the transaction price, then the notional loss needs to be paid to the exchange.

Peak Margin

1. Peak Margin is the minimum margin that must be collected by brokers from their clients in advance of placing any intraday / delivery order in the Cash and Derivatives segments.
2. Clearing corporations take at least four random snapshots of all margin status during the trading session.
3. Brokers gets margin calls from clearing corporation as per their aggregate trading volumes etc. They need to fulfil their margin obligations and report to clearing corporation.
4. The highest margin requirement that emerges from the different snapshots would become the 'Peak Margin' for the day. This peak margin is then compared with the available margin of investors.
5. Penalty may be imposed by Clearing Corporation on broker if peak margin requirement is more than the available margin.

There have been important changes with respect to peak margin requirements of recently. In order to make markets safer for investors, SEBI directed stock exchanges to increase the peak margin in a phased manner. As can be seen from the graphic below, with effect from September 1, 2021, peak margin requirement is 100%.

Schedule of 'Peak Margin' rollout



How will it impact retail investors?

The increasing margin would logically affect regular traders because of their reduced ability to leverage their funds or having to raise additional funds to continue trading.

In the earlier system of calculating margin requirement at the end of the day, traders could sell shares of a certain value and buy another lot of shares of the same value due to the net availability of margin.

Under the new peak margin system, the margin required for a particular transaction could change throughout the day. This needs investors to maintain additional funds and reduce the risk from intraday transactions.

Workings of Margin Trading

What is the difference between intraday and delivery trades?

In simple terms, intraday trade happens when investors buy and sells same quantity of shares on the same day, albeit at different prices. Buy and sell trades are executed with an intention to achieve the situation wherein total quantity sold and bought are same. This results in zero delivery obligations at the end of day for the traders. This is also called as 'Squaring off' the positions or trade.

If investor do not square off the sell trades at the end of the trading day, then he / she needs to pay for those shares and then shares are delivered or credit to his / her demat account. These kinds of trades are known as delivery trade.

What is the rational or purpose behind intraday trades?

The main purpose behind undertaking intraday trades is to earn benefit on account of difference in the selling and buying price of the stock.

Typically, an intraday trade involves an investor setting target price for specific stocks to trade in. If the share price falls below the target price, investor buys it and sells it as soon as it hits the target price (of course target price will be higher than buy price). Investor also set a stop loss target at which he/she sells shares in case the price falls to limit their intraday losses.

On the other hand, in delivery trading, the shares purchased are credited to investor's demat account. So, the investor becomes the beneficial owner of the shares and remains so till the shares are sold.

Is intra-day trading possible for all shares?

There are some stocks which are traded in 'Trade for Trade' segment. Investors need to deliver the gross quantity of shares sold by them which are under this segment. Similarly, they need to pay the full consideration for shares bought by them. In other words, intraday trading is not applicable for such shares.

How to find margin required for any trade?

As explained earlier, there are various types of margins applicable on one trade whether buy or sell. Exact margin requirement varies from exchange to exchange. Within the limits prescribed by the exchange, final amount of margin may differ from broker to broker.

In general, stock brokers adhere to maximum margin norms prescribed by the exchanges. So, stock exchanges like NSE offer an online calculator to help investors to know the margin requirement before undertaking the trade. Click here to check it yourself.

What are the implications of not fulfilling margin requirements?

In margin trading, it is critical for investors to keep sufficient funds as minimum margin to account for a stock's volatility through the day. It is particularly important if you intend to hold open positions. If the minimum margin exceeds the available margin during the trading period, it may trigger a margin call. And incase investor fails to meet the gap; it would lead to broker squaring of the position or / and liquidate assets in the margin account of the investor to compensate shortfall. So, once you know your margin obligation, best thing to do is to fulfil it at the earliest.

How to fulfil margin requirements?

1. Margin can be paid by depositing amount in designated bank account of broker.
2. Margin can also be paid by creating a 'Margin Pledge' in favor of the broker.

- Modes of providing Margin - Funds

1. Free and unencumbered Balances (funds and securities) available with the Broker in different segments of the Exchange.
2. Bank guarantee issued by any approved bank and discharged in favor of the Broker.
3. Fixed deposit receipts issued by any approved bank and lien marked in favor of the Broker.

- Modes of providing Margin - Securities

1. Margin Pledge of eligible Securities in dematerialized form with appropriate haircut.
2. Units of liquid mutual funds in dematerialized form, Government securities and Treasury bills in electronic form with appropriate haircut.
3. Securities given as margin which are sold in the cash market and the securities are in the pool account of the Trading Broker but are not given as early pay-in, benefit of margin be given to the client till T+1 day from the sale of securities without any haircut.
4. Free and Unencumbered funds / securities in the demat or bank account of the client for which the client has given Power of Attorney in favor of the broker may be considered as fulfilment of margin requirements by client if broker or its associate company is a DP.
5. Securities received in pay out shall be considered only after it is actually received from the clearing corporation.
6. Early pay- in received from clients may be considered while calculating the ledger balance for the purpose of reporting of margins till T+1.

What are the margin requirements for Buy Today, Sell Tomorrow transactions?

In case client buys a share on T day with upfront payment of applicable margin and if client sells the same shares on T+1 day, then

1. Client needs to pay separate margin for sale trades also, as Buy and Sell trades are executed in different settlements.
2. Broker may choose to pay for the buy position of client (buy value – margin paid by the client) and collect the payout of shares on T+2 day in Client Unpaid Securities Account (CUSA).
3. Broker may deliver the shares from CUSA on T+3 day towards pay-in for sale trade on T+1 day.
4. Broker may also choose to post the buy and sale value of shares to client's account upon execution of sale transaction, which could be used towards margin for subsequent trades of the client.
5. Securities received in pay out and available in CUSA account (reduced by the minimum 20% haircut) after adjusting any debit balances in client ledger shall be considered for collection and reporting of margin.

Margin Pledge

What is margin pledge?

A pledge in the context of stock trading is the use of shares as collateral for a loan or monetary advance. A margin pledge is a collateral in the form of securities accepted by intermediaries to receive funds for margin trading. With the use of securities as collaterals, investors can limit their risks.

With all the margin deposits in their possession, brokers and intermediaries who offer margin trading facilities are considered custodians. This led to misuse of client securities and funds by some brokers in recent past.

Acting on the concerns arising of this situation, margin pledge requirements were strengthened by SEBI.

1. W.e.f. August 1, 2020, collaterals in form of securities can be accepted by stock brokers only in form of margin pledge created on the securities held in client's demat account.
2. Instruction to create margin pledge on securities can be given by client or by the person holding the Power of Attorney, in physical form or electronically through SPEED-e.

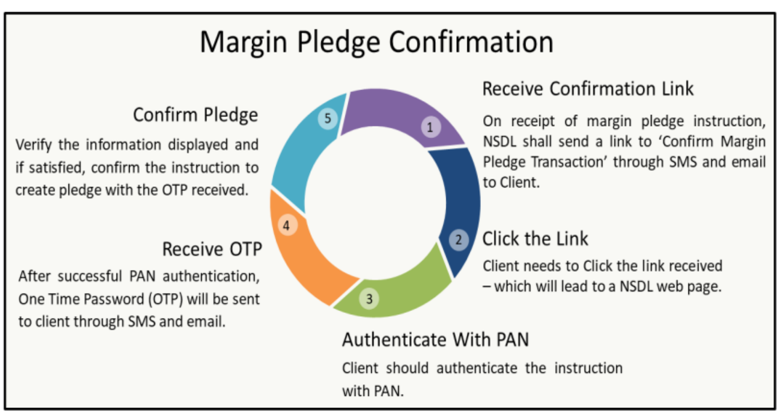
3. Such margin pledge can be created in favour of a specially designated demat account of the stock broker (opened as TM – Client Securities Margin Pledge Account or TM / CM – Client Securities Margin Pledge Account).

How to submit margin pledge instructions?

You may fill up, sign and submit ‘Form 43 – Margin Pledge Form’ in paper form to your DP. NSDL clients can also submit margin pledges electronically through NSDL’s SPEED-e platform if you are a registered user (password user or e-token user). For details, please visit www.eservices.nsdl.com.

Points to keep in mind:

a. Once created, margin pledge instruction will wait for pledgee’s confirmation to become effective.
b. If the pledgee has opted for automatic confirmation of pledge instruction, then margin pledge instruction created as above will become effective immediately.
c. Make sure to create a margin pledge for securities that are approved by your stockbroker for margin purposes.
d. Create margin pledge for quantity according to the value of the security and haircut applicable.



Inter-operable Platform for enhancing investors’ experience in Mutual Fund transactions / service requests

In order to make it more convenient to the existing and future mutual fund investors to transact and avail services, SEBI has directed that RTAs shall jointly develop a common industry wide platform that will deliver an integrated, harmonized, elevated experience to the investors across the industry. This platform shall enable a user-friendly interface for investors for execution of mutual fund transactions such as purchase, redemption, switch etc.

This platform shall be made operational in a phased manner (starting with non-financial transactions) and shall be fully operational by December 31, 2021.

Reference: Circular No. NSDL/CIR/II/19/2021 dated July 30, 2021 available on NSDL website.

Nomination for Trading and Demat Accounts

With effect from October 1, 2021 new Trading and Demat accounts of clients shall be activated by the Broker and DP respectively only if the

client has provided details of nominees or has submitted a declaration to opt out from nomination. Now, on-line nomination and Declaration form may be signed using e-Sign facility and in that case, witness will not be required.

All existing eligible trading and demat account holders shall provide choice of nomination on or before March 31, 2022, failing which the trading accounts shall be frozen for trading and demat account shall be frozen for debits.

Reference: Circular No. NSDL/POLICY/2021/0078 dated July 26, 2021 available on NSDL website.

Guidelines for online closure of demat accounts

With effect from September 1, 2021, DPs which are offering online account opening are now required to introduce the facility for online closure of demat accounts.

Reference: Circular No. NSDL/POLICY/2021/0087 dated August 19, 2021 available on NSDL website.

Block Mechanism in demat account of clients undertaking sell transactions

SEBI has prescribed a new mechanism whereby a client intending to undertake a sell transaction, can block shares in favour of the Clearing Corporation. If sell transaction is not executed (or obligation details are not received from clearing corporation), shares shall be unblocked on T+2 day. Thus, this mechanism will do away with the movement of shares from client's demat account for early pay-in and back to client's demat account if trade is not executed. This mechanism is made available to clients with effect from August 1, 2021.

When any client intends to avail Block with Early Pay-in facility, Participants are required to obtain such instruction in the prescribed format. This is an optional facility for clients.

Reference: Circular Nos. NSDL/POLICY/2021/0073 dated July 17, 2021, NSDL/POLICY/2021/0074 dated July 17, 2021 and NSDL/POLICY/2021/0082 dated July 31, 2021 available on NSDL website.

Mandatory update of certain attributes of KYC of clients - Extension

With effect from August 1, 2021, it is mandatory for clients to provide certain KYC information to DP at the time of account opening. This includes – Name, Address, PAN, mobile number, email ID and income range.

Existing demat account holders must ensure that above information is correctly recorded in their demat account before December 31, 2021.

Reference: Circular No. NSDL/POLICY/2021/0100 dated September 28, 2021 available on NSDL website.

Linking of PAN with Aadhaar

SEBI has issued a Press Release dated September 3, 2021 regarding Linking of PAN with Aadhaar mentioning as below:

- As per Central Board of Direct Taxes (CBDT) notification G.S.R 112(E) dated February 13, 2020, the Permanent Account Number (PAN) of a person allotted as on July 01, 2017 shall become inoperative if it is not linked with Aadhaar by March 31, 2022.
- Since, PAN is sole identification number for all transactions in the Securities Market, in view of the said CBDT notification, all SEBI registered entities including Market Infrastructure Institutions (MIIs) should ensure compliance of said notification and accept only operative PAN (meaning PAN which is linked to Aadhaar) by the client while opening new accounts after March 31, 2022.
- All the existing investors are advised to ensure linking of their PAN with Aadhaar prior to March 31, 2022 for continual and smooth transactions in securities market and to avoid any consequences of non-

compliance of said notification on their transactions in securities market.

Reference: Circular No. NSDL/POLICY/2021/0093 dated September 7, 2021 available on NSDL website.

Join Our Investor Awareness Webinars

NSDL conducts Investor Awareness Programs (IAPs) throughout the country to ensure investors are aware of different aspects of investing. In view of the prevailing situation, NSDL is continuing the investor awareness programs in form of webinars.

The schedule of the forthcoming programs/ webinars is published online at https://nsdl.co.in/Investor-Awareness-Programmes.php.

Prior registration is required for joining the webinar. Link for registration is available along with schedule.

We shall be happy to conduct IAP for your organization / institute / society. Please write to us at info@nsdl.co.in for such requests.

Forthcoming Investor Awareness Programmes

Sr. No.	Date	Timing	Topic	Language
1	20-Oct-21	04.00 p.m. - 05.30 p.m.	Introduction to Securities Market	Marathi
2	21-Oct-21	05.30 p.m. - 07.00 p.m.	Understanding Different Asset Classes	Hindi
3	22-Oct-21	05.30 p.m. - 07.00 p.m.	NSDLs e-Services for Investors	English
4	27-Oct-21	04.00 p.m. - 05.30 p.m.	Introduction to Securities Market	English
5	28-Oct-21	05.30 p.m. - 07.00 p.m.	Understanding Derivatives	English
6	29-Oct-21	05.30 p.m. - 07.00 p.m.	Investment in Government Securities - Why and How for Retail Investors	Hindi

More the education, more the prudence

Knowledge Wins Contest

How Can a Client Give Margin In Form Of Securities?

To send your replies: visit/click www.nsdl.co.in/knowledge-win-contest.php
or
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Atul Patange - Pune
Bakul Shukla - Ahmedabad
Bhavik Shah - Ahmedabad
Bhuvaneswari Kannan - Chennai
Chenthil Kumar - Chennai
Fenil Modi - Gandhinagar
Gaurav Garg Dakshina - Kannada
Govindaraj Jeyakumar - Chennai

H V Dwaraki Nath - Bengaluru
Hardeep Singh - Gurgaon
Hrishikesh Puranik - Ahmedabad
Kamal Mohan - Pathankot
Mukul Rustagi - Delhi
Parthasarathy R - Chennai
Raghav Ajmani - Singur
Rajeev Dethe - Nagpur

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NSDL Offices

Head office: Trade World, A wing, 4th Floor, Kamala Mills Compound, Lower Parel, Mumbai - 400013
1800 1020 990 / 1800 224 430

Branch Offices

Ahmedabad • Bengaluru • GIFT City Gandhinagar • Hyderabad • Jaipur • Kochi • Kolkata • Lucknow • New Delhi

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