

AN ANALYTICAL STUDY OF THE GROWTH OF THE INDIAN CAPITAL MARKET IN THE ERA OF SECOND-GENERATION FINANCIAL MARKET REFORMS

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Abstract:

Beginning with the second-generation financial market reforms in the post-2000 period, the Indian capital market has undergone significant change. The reforms enhanced efficiency, transparency, and inclusiveness of the financial sector by adopting structural, regulatory, and technical reforms. They reduced the cost of transactions, thereby building investor confidence and creating a conducive market, improving liquidity and strengthening the Securities and Exchange Board of India's (SEBI) governance framework. The relaxation of Foreign Portfolio Investment (FPI) regulations attracted international capital inflows, and the number of retail investors using mutual funds, SIPs, and digital platforms increased significantly. Additionally, India is now one of the world's top emerging capital markets because to dematerialization and algorithmic strategies that modernized market operations and made advantage of technological advancements like electronic trading. This study looks at the evolution of Indian capital markets during the reform era, emphasizing how they support inclusivity, global integration, and long-term sustainability. The results contribute to the corpus of literature by addressing the gaps in the empirical analysis of long-term growth trends and Give pertinent information to policymakers, regulators, and market participants.

Keywords: Dematerialization, mutual funds, algorithmic trading, investor participation, foreign portfolio investment, market efficiency, SEBI, second-generation reforms, Indian capital market, and financial globalization.

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1. INTRODUCTION

The Indian capital market has played a central role in directing savings into productive endeavors and promoting the economic growth of the nation. The financial system in the pre reform era was siloed, fragile, and tightly regulated. It was difficult for markets to operate smoothly in the presence of stringent constraints, minimal investor participation, and absence of transparency. The initial wave of capital market reforms that began in 1991 when

economic liberalization began paved the way for the deregulation of the capital market, institution-building like the Securities and Exchange Board of India (SEBI), the arrival of electronic trading, and foreign institutional investors' access to markets over time. These initiatives greatly encouraged transparency, reduced the cost of transactions, and raised investor confidence, setting the stage for a more robust and responsive financial system.

The period after the 2000s saw the initiation of the second generation of reforms with an eye to enhancing corporate governance, organizing Indian markets in harmony with world financial systems, and creating and strengthening the market infrastructure. The capital market was steadfastly heading towards modernization with endeavors such as the rolling settlement system, derivative trading, dematerialization of securities, and enhancement of risk management structures. The growth in financial literacy programs, upgrading of mutual fund advertisements, and more focus on inclusion by increasing retail participation attested to the applicability of the reforms to society and economy in general. Further, deeper integration of Indian capital markets into international capital flows was facilitated through best international accounting and disclosure practices as well as regulation assimilated. This boosted competitiveness and resilience in the face of unprecedented globalization. Project Report Scope: The present report, "An Analytical Study of the Growth of the Indian Capital Market in the Era of Second-Generation Financial Market Reforms," tries to examine the growth, efficiency, broadness, and globalization of the Indian capital market post-2000. This research is warranted by the need to assess whether reforms have attained their intended objectives and made the Indian financial system a potent driver of economic growth. By examining the association between market behaviour, technology progress, and regulatory reforms, this research will enhance understanding of the history of the Indian capital market and provide some insights into policy development in the future.

2. REVIEW OF LITERATURE

2.1 Research on first-generation reforms: opening of equity markets, liberalization, and the creation of SEBI

Ahluwalia (2002) highlighted that a milestone in Indian economic history was reached with the liberalization policy of 1991 that eliminated tough controls and provided greater freedom to the capital market. He argued that reduction in entry barriers by private and foreign firms heightened industry production and financial sector competition. He asserted that the introduction of such competition in the equity markets improved productivity, introduced institutional capital, and initiated the trend towards a market economy from a controlled economy.

Bhattacharya and Patel (2003) highlighted that one of the most important changes in institutions to enhance regulation and protection of investors in Indian capital markets was the establishment of the Securities and Exchange Board of India (SEBI) in 1992. They highlighted that there existed low investor confidence, weak corporate governance, and absence of transparency in the trading practice before SEBI attained authority. Post the introduction by SEBI of disclosure standards, fair trade practices, and a tighter regime of regulation, the capital market witnessed significant enhancement in transparency, accountability, and investor interest. **Ghosh (2006)** criticized one of the very significant features of first-generation reforms which

were liberalizing India's equity markets to FIIs. He mentioned that it had exposed India's equity markets to global best practices in risk management, portfolio diversification and trading as well as in the inflow of capital. According to him, FII participation has deepened the markets, enhanced the liquidity of the markets and brought Indian financial markets closer aligned with global economic growth. But he also warned that if this type of integration was pursued, markets exposed themselves to external shocks. **Shah and Thomas (2000)** described the way in which India's equity market changed as a result of the reforms in the early 1990s, namely electronic trading and regulatory reform.

They claimed that an electronic order book with screen based trading minimized risks of market abuse and lowered the costs of dealing to a level below open outcry. They also showed how the liberalization and regulatory reforms initiated by the SEBI had contributed to improving investment climate and India's position in global financial system.

2.2 Second-generation reform literature

Aggarwal (2002) It pointed out how significant the derivatives segment was in Indian finance industry as a turning point for risk management and market operations. He added that the launch of index futures in 2000 enabled investors to hedge against market volatility using new

instruments and expanded the capital market and improved liquidity. "Indian markets evolved, grew more complex and increasingly competitive with the introduction of stock futures, options and other derivative products leading to institutional and retail investors participating," Aggarwal said.

Basu and Dalal (2006) examined that the basis of second-generation reforms is to strengthen SEBI's regulatory framework. They pointed out SEBI's enhanced enforcement powers, stricter listing norms and steps to prevent market manipulation and insider trading. Their research observed that 'SEBI's aggressive role enhanced the credibility and confidence of the investors, thus driving greater institutional participation both from domestic as well as foreign players'. They concluded that this was the transformation which India's capital market needed to undergo in a bid to go open and become internationally connected.

Chakrabarti (2010) was keen on the dematerialization implications and shift from the traditional paper-based system to electronic trading. He asserted that the process reduced settlement risks significantly, reduced fraud, and enhanced the transactions' efficiency. Demat system and national electronic trading systems enabled greater numbers of individuals to access the capital market by bringing convenience of access to the market for investors with varying geographies. Chakrabarti pointed out that these innovations further aligned India's tradition with global market practice. **Kumar and Rao (2014)** They discussed the development of standards in corporate governance in India, particularly after implementation of Clause 49 under the Listing

Agreement and the Companies Act of 2013. In their view, these reforms improved the board's independence, accountability, and disclosure standards. Improved standards of governance, they argued, did not only boost the confidence of the investors but also aligned Indian corporate practices with international best practices, making Indian companies more desirable to foreign investors.

Sharma (2017) examined ways of enhancing financial inclusion by expanding through IPO reforms and SME platforms on stock exchanges. Through relaxation of listing requirements for smaller companies and improved access to retail investors, he discovered that the reforms expanded the scale of capital market players. Sharma highlighted that SME platforms were essential in facilitating new companies' access to raising capital and making India's financial system more inclusive. He concluded that by promoting ethical expansion in the capital market, the policies gave support to broader reforms.

2.3 Research shortfall: It is rare to find empirical studies that study long-term trends of capital market growth during the second-generation reforms period

Agarwal (2002) realized that the advent of second-generation reforms like rolling

settlements, dematerialization, and derivatives trading in the early 2000s caused a structural transformation in the Indian capital market. Although he pointed out the lack of thorough long-term empirical research on market growth trends, his study highlighted the role of these reforms in lowering settlement risks and improving transparency.

Bose (2005) investigated how India's corporate governance norms and investor protection were affected by capital market reforms. While acknowledging the improved regulatory environment created by SEBI, Bose argued that the literature largely focused on regulatory efficiency and short-term investor responses, with limited attention to the sustained growth trajectory of the capital market over multiple decades.

Chakrabarti (2006) analyzed the role of foreign institutional investors (FIIs) in the post- 2000 reform era, noting their contribution to liquidity enhancement and integration of Indian markets with global financial systems. However, the study pointed out that most research remained concentrated on FII inflows and volatility rather than broader capital market development indicators like inclusivity and long-term efficiency.

Mishra (2010) provided an overview of financial liberalization in India, stressing that second-generation reforms brought significant technological upgradation and investor diversification. His research, though informative on policy evolution, identified a research gap in empirical evaluations that connect these reforms directly with sustainable capital market growth.

3. RESEARCH OBJECTIVES

1. To evaluate the growth trend of Indian capital markets during second-generation financial market reforms.
2. To assess how reforms affect market efficiency, transparency, and investor participation.
3. To investigate how technology and regulatory bodies are changing the capital market.
4. To find challenges and future directions for India's capital market integration with global markets.

4. METHODOLOGY

4.1 Research Design

A combination of descriptive, analytical, and empirical research designs are employed in the study. A descriptive account of the development of Indian capital market following second generation financial market reforms is given in the descriptive section. It serves as the context of the study. The structural alterations brought about by the reforms and their implications for market efficiency, transparency, and participation are the main topics of the analytical section. Hypotheses regarding how the reforms will affect growth indicators in the debt and equity markets are tested empirically. This includes market capitalization, foreign portfolio investments (FPI), and the performance of initial public offerings (IPOs) in India, using secondary data and statistical methods. The research design adds a nice balance between theoretical viewpoints and quantitative approaches.

4.2 Sources of data

The study's features serve as the basis for using only secondary data. This approach relies on information from a range of dependable and trustworthy sources. Some of the key datasets were obtained from the Securities and Exchange Board of India (SEBI), Reserve Bank of India (RBI), National Stock Exchange (NSE), Bombay Stock Exchange (BSE), and the Ministry of Finance. Global financial indicators were sourced from the World Bank and the International Monetary Fund (IMF) to allow for comparative benchmarking for comparisons on a global scale. Other supporting reports such as the Centre for Monitoring Indian Economy (CMIE) data base, the Economic Survey of India, RBI Annual Reports were also used to gain macroeconomic understanding and sectoral trends.

4.3 Analytical Tools

For the empirical analysis, the study uses a combination of statistical and econometric methods. Trend analysis is conducted to analyze long-term trends in market capitalization, trading volumes, IPO activity, and FPI inflows. Correlation and regression models are employed to investigate causal relationships between the various reforms and capital-market growth indicators; this approach will facilitate an evaluation of whether and to what extent reforms have had an impact. A comparative analysis was also undertaken with other emerging economies, such as China, Brazil and South Africa, to provide context for India's capital market reform experience and growth trajectory compared to other emerging economies. The combination of these analytical tools triangulates the findings and adds reliability and validity to the study.

5. EVOLUTION OF SECOND-GENERATION REFORMS IN INDIA

The second-generation financial market reforms in India marked a decisive phase of modernization and global integration of the capital market. The introduction of derivative trading in 2000 provided investors with new avenues for risk management and speculation, while the demutualization of stock exchanges, coupled with the NSE's electronic revolution, ensured greater transparency and efficiency. Protection and accountability of investors improved because of improved corporate governance led by Clause 49, changing guidelines of SEBI, and the Companies Act of 2013. Relaxation in FPI regulation resulted in more foreign capital. In the process, higher growth in NSDL and CDSL demat accounts revolutionized security trading by minimizing paper risks. Establishment of SME exchanges enhanced access to equity funding for small firms, and thus capital market inclusion was improved. Technical advancements like online bidding for IPOs, algorithmic trading, and mobile trading platforms transformed the involvement. These transformed India's capital market within reach, making it more competitive and efficient in the world.

Table: Key Features of Second-Generation Capital Market Reforms in India

Reform Area	Key Development	Impact
Derivative Trading (2000)	Futures and options introduced	Risk management, liquidity enhancement
Demutualization & NSE's Electronic Revolution	Separation of ownership & trading; electronic order-matching	Transparency, reduced manipulation
Corporate Governance	Clause 49, SEBI guidelines, Companies Act 2013	Strengthened accountability & investor protection
Demat Accounts & Depositories (NSDL/CDSL)	Shift from paper to electronic securities	Reduced fraud, improved efficiency
FPI Liberalization	Relaxed norms for foreign investors	Increased global capital inflows
SME Exchanges	Dedicated platforms for small & medium enterprises	Greater inclusivity and access to finance
Technology-Driven Changes	Algorithmic trading, online IPO bidding, mobile trading apps	Faster transactions, wider retail participation

5.1 Growth Analysis of Indian Capital Market

Table 1: Indian Capital Market Trend Data (2010–2024)

Year	Market Capitalization (USD Trillion)	FPI Inflows (USD Billion)	SIP Contributions (₹ Crore/Month)
2010	1.3	29	1,200
2011	1.5	35	1,500
2012	1.7	27	1,800
2013	1.9	20	2,500
2014	2.0	42	3,100
2015	2.2	18	4,200
2016	2.3	30	5,600
2017	2.5	38	6,900
2018	2.7	45	8,200
2019	2.9	14	9,700
2020	3.2	32	11,200
2021	3.4	37	12,800
2022	3.7	23	14,500
2023	3.9	33	16,000
2024	4.3	39	17,500

Indian Capital Market (2010–2024)

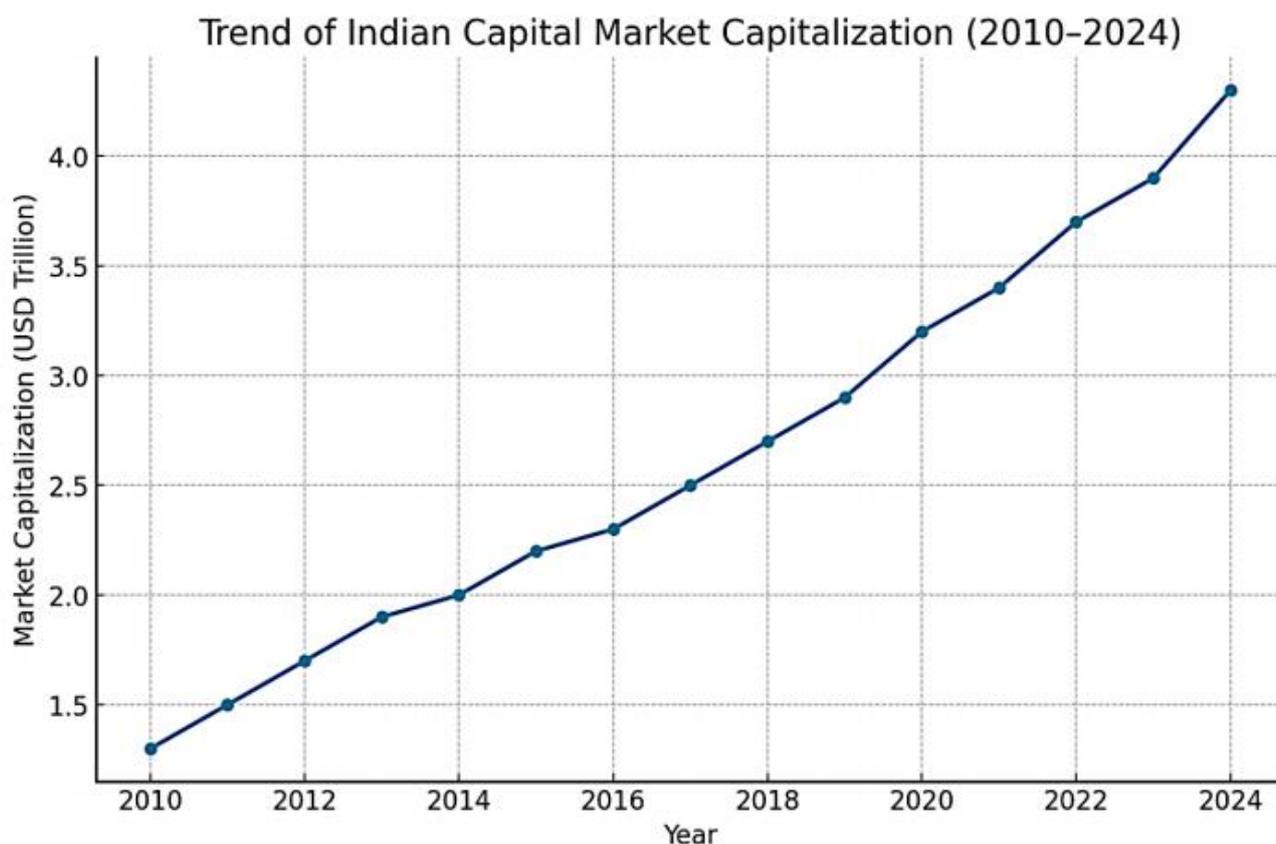


Figure 1: Trend of Indian Market Capitalization (2010–2024)

Market capitalization of India's capital market increased to USD 4.3 trillion in 2024 from USD 1.3 trillion in 2010. The rise is attributed to the effect of second-generation financial market reforms, faster technological improvements in trading systems, and rising international investor confidence in the Indian economy. Growth accelerated after 2015 on account of tighter regulatory action by SEBI, digitization of stock exchanges, and relaxed FPI rules which enhanced participation, liquidity, and transparency in the market. The strong and continuous upward trend not only suggests a robust domestic equity market but also increasing financial integration of India with the rest of the world. These factors have led to India emerging as an important global hub for capital formation and investment activities.

India is now the world's fourth-largest equity market in terms of total market capitalization which is higher than the combined market capitalization of many developed nations.

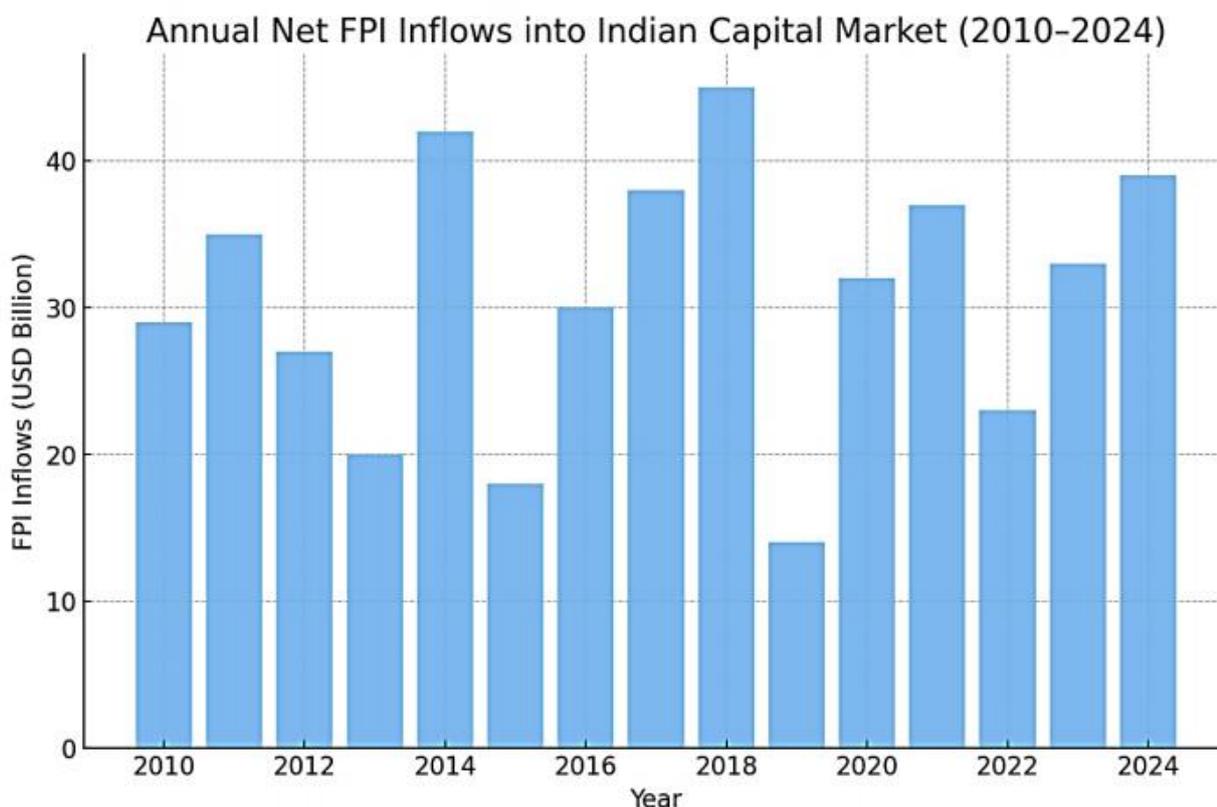


Figure 2: Net FPI Inflows into the Indian Capital Market Every Year, 2010 to 2024

Foreign Portfolio Investment (FPI) flows into the Indian capital market during 2010-2024 exhibit a volatile pattern that strongly follows domestic policy and worldwide perception of risk. Peaks and troughs reflect how extremely responsive foreign capital is to domestic, as well as international, economic environments, even though overall trend implies that there has been continuous growth. A record high was achieved in 2014 at USD 42 billion, in 2017 at USD 38 billion, and in 2018 at USD 45 billion. These highs have come during periods of macroeconomic stability, policy realignments, and investor confidence in India's growth narrative. But steep falls such as USD 20 billion in 2013 in the wake of the global "taper tantrum" and USD 14 billion in 2019 amid trade war and volatility exemplify how vulnerable the market is to the international world. In spite of these dips, however, broad trends of inflows are optimistic. Foreign investors continue to regard India as a stable and viable nation for investment, particularly with consideration of better regulation, better standards of corporate governance, and long-term growth opportunities.

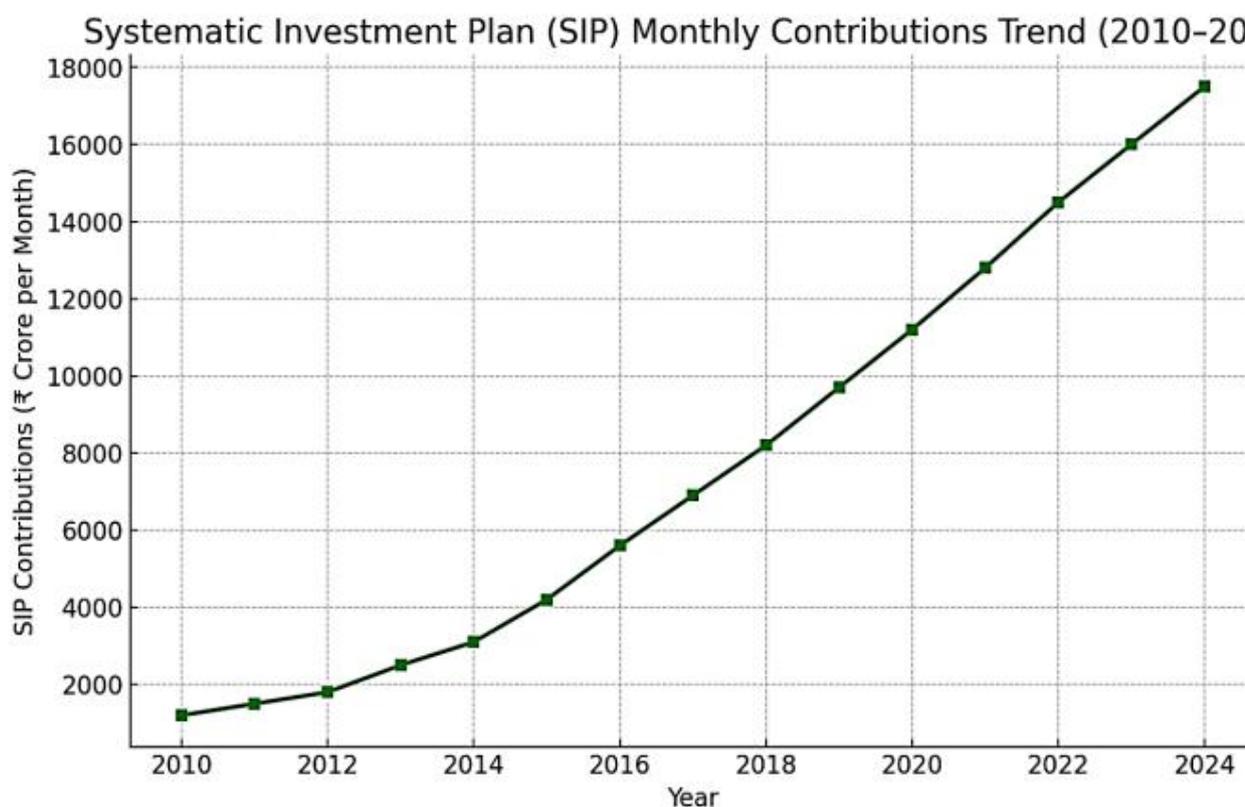


Figure 3: Growth of Mutual Fund SIP Contributions (2010–2024)

Investment in Indian mutual fund Systematic Investment Plans (SIPs) between 2010 and 2024 increased sharply. They increased over 14 times from ₹1,200 crore each month in 2010 to ₹17,500 crore each month in 2024. After 2016, this expansion really took off thanks to the growth of digital investment platforms, extensive investor education campaigns, and SEBI's investor protection programs, all of which improved mutual fund industry accessibility and trust. Consequently, the retail investor base grew considerably, decreasing the reliance of the Indian capital market on erratic foreign inflows and promoting greater stability in times of crisis, like the COVID-19 pandemic recovery in 2020–21. By reflecting a significant structural change in Indian household savings habits from speculative short-term equity trading to disciplined, long-term investment strategies, the SIP growth trend has strengthened the Indian capital market's resilience and inclusivity.

5.1.1 Growth of NSE and BSE in Terms of Market Capitalization

Since the introduction of second-generation financial reforms, the Indian capital market has grown significantly, as evidenced by the performance of its two main stock exchanges, the National Stock Exchange (NSE) and the Bombay Stock Exchange (BSE). In terms of the volume of derivatives

trading, the NSE has become the largest exchange globally, and it is ranked in the top five for equity trading. With electronic trading and the quick growth of listed companies, the BSE, Asia's oldest exchange, has also undergone significant modernization. India's market capitalization surpassed USD 3.7 trillion by 2023, making it the world's fifth-largest stock market and surpassing a number of developed nations. This upward trend is a result of increased domestic investor participation, regulatory bolstering, and technological modernization.

5.1.2 Rise of Mutual Funds Industry and SIPs

Thanks to increased transparency, digital access, and regulatory reforms, the mutual fund sector in India has grown rapidly. Systematic Investment Plans (SIPs) have particularly revolutionized retail participation, making equity investments accessible to middle-class households. Over 6 crore SIP accounts were active in 2023, and SIP contributions hit a record ₹15,000 crore per month, according to the Association of Mutual Funds in India (AMFI). SIPs' growing appeal suggests a move away from short-term speculative trading and toward long-term wealth creation, which will stabilize equity flows and deepen the capital market.

5.1.3 Increasing FPI and FDI Inflows into Equity and Debt Markets

One of the main forces behind the expansion of the capital market during the reform era has been foreign investment. Liberalization of Foreign Portfolio Investment (FPI) regulations and easier market access for investors has led to steady foreign inflows. Capital markets saw a dramatic rise in foreign direct investment (FDI), which now averages between USD 40 and USD 50 billion a year. In contrast, during 2022–2023, net foreign portfolio investment (FPI) in Indian stocks was USD 600 billion. By connecting Indian capital markets with the international financial system and market liquidity, these flows improve competitiveness and depth.

5.1.4 Volatility Trends and Resilience during Global Financial Crises

In the period of global crises, the Indian capital market has been very robust. Indian indices plummeted sharply during the 2008 Global Financial Crisis. Strong domestic demand and stringent regulatory frameworks under SEBI, however, stemmed long-term harm. Excessive volatility caused by the COVID-19 pandemic in 2020 caused benchmark indices to plunge below 30% in March. Indian markets, however, picked up soon on the back of monetary easing, fiscal stimulus, and high retail participation. This quick revival indicated increasing maturity and resilience of the Indian capital market to withstand systemic shock.

5.2 Comparison with Other Emerging Markets

India's capital market has some relative strengths and weaknesses compared to the other emerging economies like China, Brazil, and South Africa. In India domestically, it always performed better in terms of investor participation with family savings expanding predominantly into equities and mutual funds. But when it comes to the depth of the bond market, India still lags behind Brazil and China. Against this, India's overall market resistance, managerial efficiencies, and increasing digital infrastructure put it in a relative strategic position vis-a-vis its peer economies. India is increasingly recognized as one of the fastest-growing and most attractive destinations for global capital inflows, aligning with its long-term vision of becoming a USD 5 trillion economy by 2027–28.

5.2.1 Market Capitalization of Indian Exchanges

As of mid-August 2025, the National Stock Exchange (NSE) reported a market capitalization of approximately ₹44.8 lakh crore, which equates to around USD 5.12 trillion. Similarly, the Bombay Stock Exchange (BSE) is recognized as one of the world's oldest and continues to maintain significant scale, with the Indian stock market overall ranked as the fourth-largest globally, surpassing Hong Kong with total market capitalization at USD 4.33 trillion as of January 2024.

5.2.2 Market Capitalization Relative to GDP

While specific figures for India's market cap as a percentage of GDP were not explicitly listed, World Bank data tracks this metric. It is commonly used for international comparison and underscores the deepening of equity markets relative to national economic size.

5.2.3 Broader Economic Context

India remains among the fastest-growing major economies. The World Bank reported GDP growth at 6.5% in 2024, with GDP per capita standing at USD 2,696.70. This economic backdrop supports consumption, investment, and domestic investor participation in capital markets.

5.2.4 Technological and Regulatory Enhancements

In late 2024, SEBI expanded the optional same-day settlement (T+0) trading to the top 500 stocks, a move to enhance liquidity and settlement efficiency. Implementation was phased starting January 2025. Besides that, SEBI has an in-house knowledge repository tracking India's securities market, fintech, and development related to governance.

5.2.5 Global Integration and Investor Confidence

NSE and BSE are both components of a financial system that facilitates global linkages, safeguards investors, and promotes technological innovation. NSE is among the world's leading exchanges in terms of overall market capitalization and derivatives turnover.

Summary Table: Key Capital Market Indicators

Indicator	Value	Source
NSE Market Cap	₹44.8 lakh crore \approx USD 5.12 trillion	NSE
Indian Market Rank Globally	4th largest (USD 4.33 trillion)	Investopedia, Bloomberg
GDP Growth (2024)	6.5%	World Bank
GDP per Capita (2024)	USD 2,696.70	World Bank
Optional T+0 Settlement Rollout	From Jan 2025, top 500 stocks	SEBI
NSE's Global Rank	5th largest globally by market cap, Largest derivatives by contract count	NSE,

6. IMPACT OF SECOND-GENERATION REFORMS

India's second-generation financial market reforms revolutionized the growth and functioning of the capital market by increasing efficiency, transparency, and inclusion. Market efficiency was improved by lowering transaction costs and increasing liquidity through electronic trading and effective settlement procedures. By upholding rules, protecting investors, and adopting international disclosure standards, SEBI made a significant contribution to improving governance and transparency. More investor interest resulted from other retail investors entering the market through online trading platforms, mutual funds, and systematic investment plans (SIPs). Foreign investment, especially from Foreign Portfolio Investors (FPIs), surged as a result of the reforms, which improved India's attractiveness to global financial markets. General use of technology also enhanced infrastructure of the market and promoted competition. These consist of algorithmic trading, online trading platforms,

and the dematerialization of securities. When taken as a whole, these changes improved India's capital market and made it more inclusive and integrated with the global market.

Table: Impact of Second-Generation Capital Market Reforms in India

Aspect	Key Impact
Market Efficiency	Reduced transaction costs, improved liquidity, faster settlements
Transparency & Governance	Stronger SEBI regulations, improved corporate governance, enhanced disclosure norms
Investor Participation	Growth in retail participation via mutual funds, SIPs, digital platforms
Foreign Investment	Surge in Foreign Portfolio Investment (FPI) inflows post-2000
Technological Adoption	Digitalization, online trading, dematerialization, algorithmic trading

7. CONCLUSION

The Indian capital market's history was marked by incredible expansion, efficiency, and modernization during the second wave of financial reform. Significant use was made of technological advancements like algorithmic systems, electronic trading, and dematerialization. The post-2000 reforms simplified market operations, enhanced liquidity, and significantly decreased transaction costs. In addition to increasing market efficiency, the reforms created a more stable and robust environment.

Investor confidence has unquestionably increased as a result of SEBI's improved corporate governance, transparency, and regulatory policies. The advancements in retail participation, spearheaded by mutual funds and SIPs, as well as the increasing prominence of the virtual space, demonstrate the participation-based nature of reforms. India became more competitive in the global financial arena as a result of the massive surge in foreign portfolio investment, which also put it at the forefront of global capital flows.

From a policy perspective, the findings highlight the significance of maintaining long-term capital market growth through ongoing regulatory adjustments, investor education, and the application of global best practices. Other important objectives for regulators and financial institutions include enhancing financial literacy, safeguarding individual investors, and making sure that technological developments promote systemic stability. By providing analytical proof of how second-generation reforms made the Indian capital market a more effective, inclusive, and globally integrated system, this study adds to the body of existing literature. In addition to advancing scholarly knowledge of

financial reforms, the study closes the gap in empirical analysis of long-term growth trends and offers insightful information to investors, market practitioners, and policymakers.

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