

Sebi to shorten trade settlement cycle to one day, starting 2022

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MUMBAI : The settlement or transfer of ownership of stocks on exchanges can be cut to just one business day after the trade is executed starting next year, the markets regulator said.

The Securities and Exchange Board of India (Sebi) decided to allow stock exchanges the option to offer the faster T+1 trade cycle instead of the existing T+2 cycle from 1 January, conceding a long-running demand from retail investors.

"Sebi has been receiving requests from stakeholders to further shorten the settlement cycle. Based on discussions with market infrastructure institutions (stock exchanges, clearing corporations and depositories), it has been decided to provide flexibility to stock exchanges to offer either T+1 or T+2 settlement cycle," the Sebi circular said.

The change to a shorter cycle is likely to benefit retail investors, who will get quicker access to cash and securities after trades are executed. It will also reduce the risks associated with fluctuations of stocks during the settlement cycle.

The proposed T+1 settlement cycle will, however, not be mandatory, with exchanges retaining the option to continue to offer the T+2 settlement cycle. A stock exchange may choose to offer the T+1 settlement cycle on any stock after giving advance notice of at least one month regarding the change in the settlement cycle to the public.

After opting for the T+1 settlement cycle for a stock, the exchange will have to mandatorily continue with the same for a minimum period of six months. Thereafter, in case the stock exchange intends to switch back to the T+2 settlement cycle, it can do so by giving one-month advance notice to investors.

Sebi added that any subsequent switch from T+1 to T+2 or vice versa shall be subject to six-month minimum lock-in period and one-month advance notice period. "There shall be no netting between T+1 and T+2 settlements," Sebi said. Netting is a method of reducing risks in financial contracts by aggregating multiple financial obligations to arrive at a net obligation amount.

The settlement option for securities shall be applicable to all types of transactions in the security on that stock exchange. For example, if a stock is placed under the T+1 settlement on a stock exchange, the regular market deals and block deals will follow the T+1 settlement cycle on that stock exchange, Sebi said.

Sebi has directed stock exchanges, clearing corporations and depositories to take necessary steps to put in place proper systems and procedures for the smooth introduction of the T+1 settlement cycle, including necessary amendments to the relevant bye-laws, rules and regulations.

However, the stockbrokers' lobby group Association of National Exchanges Members of India (ANMI), had earlier raised concerns on implementation of T+1 settlement system. "The window will be too short for securities lending and borrowing to practically work, and there could be spill over," ANMI said in a letter to Sebi on 28 August.

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Several operational and technical challenges would need to be tackled before implementing the T+1 settlement system. At present, the infrastructure available with market infrastructure institutions is not able to efficiently meet timely issuance of pay-in and pay-out and to send files on time, it said. Besides operational and technical challenges, implementing the new system will increase working capital requirements for brokers and extended working hours for banks and depository participants, ANMI said.

It also pointed out that global investors will face difficulties in a short cycle of settlement as securities settlement of FPIs is operationally very complex, involving coordination among multiple entities such as fund managers, global and local custodians, brokers, clearing members, and exchanges. "If the settlement of T+1 is adopted, the MSCI country classification methodology may look at it negatively as it is likely to result in Indian market being a pre-funded market. This may result in a drop in the weightage to India in its MSCI emerging market Index. This will adversely affect flows," ANMI had said.

In 2003, Sebi shortened the settlement cycle from T+3 rolling settlement to T+2.