The trade-plus-one(T+1) settlement plan

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In news– After China, India will become the second country in the world to start the ‘trade-plus-one’ (T+1) settlement cycle in top listed securities.

What is the T+1 settlement plan?

- **The T+1 settlement cycle means that trade-related settlements must be done within a day, or 24 hours,** of the completion of a transaction.
- For example, under T+1, if a customer bought shares on Wednesday, they would be credited to the customer’s demat account on Thursday.
- **This is different from T+2,** where they will be settled on Friday.
- As many as 256 large-cap and top mid-cap stocks, including Nifty and Sensex stocks, will come under the T+1 settlement.
- **Until 2001, stock markets had a weekly settlement system.** The markets then moved to a rolling settlement system of T+3, and then to T+2 in 2003.
- **T+1 is being implemented despite opposition from foreign investors.** The United States, United Kingdom and Eurozone markets are yet to move to the T+1 system.

The benefits of T+1-

- **In the T+1 format, if an investor sells a share, she will get the money within a day,** and the buyer will get the shares in her demat account also within a day.
- This will also **help investors in reducing the overall capital requirements with the margins getting released on T+1 day,** and in getting the funds in the bank account within 24 hours of the sale of shares.
- The shift will boost operational efficiency as the

rolling of funds and stocks will be faster.

- According to a paper published by the Securities and Exchange Board of India (SEBI), **a T+1 settlement cycle not only reduces the timeframe but also reduces and frees up capital required to collateralise that risk.**
- A shortened settlement cycle **also reduces the number of outstanding unsettled trades at any point of time,** and thus **decreases the unsettled exposure to Clearing Corporation by 50 per cent.**
- The narrower the settlement cycle, the narrower the time window for a counterparty insolvency/ bankruptcy to impact the settlement of a trade.
- Further, the capital blocked in the system to cover the risk of trades will get proportionately reduced with the number of outstanding unsettled trades at any point of time.
- Systemic risk depends on the number of outstanding trades and concentration of risk at critical institutions such as CCPs, and becomes critical when this magnitude of outstanding transactions increases.
- Thus, in this era of increasing trade volumes, a shortened settlement cycle will help in reducing systemic risk.

Why are foreign investors opposed?

- Foreign investors were against SEBI’s T+1 proposal. **Among the issues raised by them were time zone differences, information flow processes, and foreign exchange problems.**
- Foreign investors said they would also find it **difficult to hedge their net India exposure in dollar terms at the end of the day under the T+1 system.**
- In 2020, SEBI deferred the plan to halve the trade settlement cycle to one day (T+1) following opposition from foreign investors.