From 1 Crore to 5 Crore Investors

Anup Bagchi
Managing Director & CEO
ICICI Securities Ltd.

Memory of the first investment which I made in the market can fade a bit, but I can not forget the experience which is etched in my mind. We have come far from then and it can be said that a complete transformation has happened in this area and today we are challenging many developed countries.

The journey of Indian financial markets has been of many shades over the last decade. We have seen a lot of progress along with some pauses. Many twists and a few turns. Awe inspiring growth punctuated by its lack of inclusiveness. The fastest free market economy is now face to face with the challenges and opportunities to opt for either slow and steady or fast and furious growth, in the next decade.

Last two decades have been of transformation – of trading systems, dematerialization, settlement guarantee, corporate governance, expansion of markets and many more. This was made possible by efforts of Exchanges, Market participants, Investors and the Regulator which is now widely perceived as a robust institution and a role model for regulators in emerging markets.

The Government, the Regulators and the financial institutions have an important role to play in building a strong and robust capital market. The growth trajectory of a country's capital markets in significantly influenced by the actions of these stakeholders. Concerted efforts of the Government and the Regulators supported by a long-term vision and clarity in action is providing significant helping in fostering a climate that is conducive to growth and investments.

India is one of the five countries classified as big emerging market economies apart from China, Indonesia, Brazil and Russia. A study by World Bank predicts that by 2020 the share of these five biggest emerging markets' in the world output will double to 16.1% from 7.8% in 1992. This surge in growth is supported by an expanding middle-class population, with an increase in public and private investment. India has a strong middle class of 250-300 million expected to double in the next two decades. The country is set to become the fifth largest consumer economy.

Just to give some perspective, it is estimated that India will require capital flows of USD 500 billion merely for developing its infrastructure. The Indian economy's size was approximately USD 1 trillion in 2009-2010 with the savings rate of Indian households of 33.4% in 2009 -2010. In the next decade or so, it is expected that the economy will grow at an average rate of 8%. This translates into incremental savings of USD 5 trillion over the next decade. Comparatively, the US economy's size was around USD 13.22 trillion in 2010. Assuming a savings rate of 5%, it may not be a surprise if the amount of savings of Indian households exceeds savings of US households in absolute terms by 2020.

Also, Indian households have traditionally preferred safety of bank deposits and government saving schemes and much less than 10% of the their investments in financial assets is in shares, debentures and mutual funds, which is low as compared to some of the developed economies. Given the quantum of savings, the need to mobilise savings into productive channels and the opportunity for financial intermediation, the next decade will be an opportunity of a lifetime for Indian capital markets players.

One of the daunting challenges before the Indian capital markets is expanding the investor base and provide them access to high quality financial services.

Indian households invest lesser in equity markets than do their developed market counterparts, particularly in the United States and the United Kingdom. As a result, retail equity ownership (non-promoter) amounts to around 10 percent of total equity ownership. While corporates see markets to raise low cost risk capital, investors seek greater trust through better corporate governance and liquid secondary markets for exit options.

A decade back equity was more of a niche product. But now it has been able to win the mind share of the common man. So the awareness challenge has already been taken care of to a large extent. Moving ahead, the accessibility to markets in terms of reach, processes and economics has to be as simple as a bank account. Also intermediaries need to match the credibility that banks enjoy in terms of transparency and trustworthiness. This will go a long way in increasing the customer base and making the capital markets a beneficiary of the large surplus of investable funds available in the country.

Customer education has always played a key role in expansion of markets. Giving it a form of public and private partnership would make it more acceptable. Regulators can provide the right environment and intermediaries can provide the necessary reach and infrastructure for this. Further deepening of capital markets can be achieved through investor education initiatives, development of quality independent financial advisors and using the Information Technology to reach out across the length and breadth of the country.

We have the right environment for larger markets and catering to higher number of IPOs. This will go a long way in supporting the increase in the number of investors for which growth in the market capitalization also becomes a necessity. This would be facilitated by more number of quality stocks being listed and smaller companies also being able to tap the primary markets for equity capital.

Further simplifying the process of raising equity capital would be a step in the right direction. In the future it has to reach a level where equity raising is as easy as raising debt is today. This will happen with the cost of fund raising coming down along with simplification of the regulations and the process.

Securities and Exchange Board of India (SEBI) is in the process of further simplifying initial public offering (IPO) process for the benefit to increase retail participation. Few measures like availability of IPOs at discount to retail investors have already been taken. Such measures in other areas too will lead to lower costs for the intermediaries and thus better service standards for retail investors. Regulatory reform is required across all dimensions of capital markets, to remove structural bottlenecks. SEBI has also taken several proactive measures to improve the integrity of the secondary as well as primary markets through better governance and disclosure norms.

However going ahead, customer will be more aware & more demanding. Hence the intermediaries will have to create scale of economies to keep the cost low, in order to sustain these higher demands from the customers.

According to a SEBI-NCAER Survey of Indian Investors, almost half of the households are such where the head of the household has studied only up to matriculation. Even though there may be others in the household with higher educational qualifications, it does not automatically follow that every graduate understands the nuances of the market and how a particular company, industry and the economy perform. By the same token, not every office-goer is well equipped to invest in the stock market. At best, most individual investors can be good followers. But the fact remains that market growth will happen due to small investors. A parallel can be seen in the telecom industry, where unprecedented growth has happened. Thus we have to see direct participation and indirect participation together to determine the equity participation by retail investors. Thus MF and Insurance must also be counted as form of participation in the equity markets.

There are additional two issues that needs to be kept in mind. We have alternate fixed income avenues which gives reasonable returns due to administered rates or high interest rate regimes. This coupled with the fact that general populations' ability to weather out volatility or take temporary dip in capital is restricted. Thus innovative offerings can provide the opportunity to tap a larger pool of savings. Innovative products like Capital Protected Structures which offer safety as well as an opportunity to reap the basic benefit of equity markets would certainly find favor with retail investors. Also innovative products catering to various classes of investors, having different risk profiles are required. Thus emphasis is on product innovation within a sound regulatory and supervisory framework.

As the industry moves through the per capita spectrum the cost of delivery has to be kept pace to sustain the economics. It might be necessary to incentive the system to bring in clients across per capita spectrum and work on different incentive structures to create surplus for investments.

The entry of investors below the age of 25 in the market has gone up significantly and this shows that journey to 5 crore investors has begun. We may reach this mark much sooner than latter.

Conclusion

One of the underlying challenges that the banking and financial services sector is dealing with is the issue of increasing the out-reach & enhancing financial inclusion. The huge scale of the drive towards inclusive growth is intimidating, as various stakeholders like banks, insurance companies , asset management companies and broking intermediaries struggle to move a step closer to the untapped areas and newer target consumers. The challenge lies in devising a cost-effective delivery model to reach out to the low income group of society, penetrating the remote areas. Awareness, regulations, product innovation, delivery innovation and higher moving per capita will need to move in tandem to make this happen. The first one crore mark took over two decades, the road to five crore may take less than a decade.