

Capital Markets – The Path to the Indian Growth Story



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BSE, commonly known as Bombay Stock Exchange, has been in existence for close to 140 years.

It was set up in 1875 as Native Share and Stock Brokers despite the British who were ruling India then. The Articles of Association of the Exchange then, restricted membership to Indian nationals only.

BSE is the oldest exchange in Asia and

is also the largest exchange in the world by number of companies listed, more than twice as big as its nearest competitor. Currently, more than 5400 companies are listed on BSE with market capitalisation (wealth) in the vicinity of INR 90 lakh crore (~US \$1.5 trillion). BSE has more than 2.57 crore investors registered with it making it amongst the largest exchanges in the world in terms of number of users.

Today, BSE's name is synonymous with investments in India due to its consistent services over all these 140 years across the country.

Over last 140 years, BSE has acted as a catalyst and a first line regulator for corporates to raise necessary funds from small investors and provide adequate returns to the investors in a fair, efficient and transparent manner. Today, market capitalisation of INR 90 lakh crore is very similar in size to the entire banking system's asset base of INR 80-85 lakh crore.

Stock market's ability to efficiently allocate capital and provide superior returns will always make it a platform of choice for smart savers vis a vis other alternatives for savings such as bank deposits etc. BSE Sensex which was started in 1984-85 with a base of 1979-80 as 100, has breached 25000 levels recently. What it indicates is that, if you had invested INR 100 in 1979-80, today, in 2014, you would have got INR 25,000 in terms of asset value, a return of 25,000% in 35 years. No other asset class in India would have given such returns on a consistent basis. Looking at the importance of investment and savings through stock market, Government of India has exempted the profit from stock sale from capital gains, if you hold the shares for more than 1 year. In contrast, if you keep savings in bank deposits or any other assets class, on sale of these assets, the profit derived will attract capital gains. Effectively, which ever way one looks at, investment in

stock markets provides better returns with lowest tax incidence to investors making it quite an attractive avenue for savings.

In addition to capital gains, the stocks also provide dividend out of the profits to shareholders. The returns therefore are even higher than 25000% in 35 years.

The money investor invests in stock markets through IPO goes to companies for them to finance their need for funds to set up additional projects, upgradation of facilities, working capital needs and various other needs. In essence, investment in stock markets go for productive purposes and create jobs. In modern India, most jobs are created by corporates in IT, Manufacturing, Pharma, Defence, Services, Retail, Mining, Ports, Roads, Electricity Generation, etc. All these companies need funds to invest and create jobs. The investments in stock markets create these jobs in addition to giving the investors superior returns. In my opinion, India's job for next 20 years is to create jobs. India needs to create 1.5 crore new jobs each year for next 20 years making it 30 crore jobs creation in next 20 years. It is a huge task. It has to be accomplished in the most efficient way. BSE is the only vehicle through which this is possible. India has been fortunate to have a well functioning stock market system over all these 140 years which has provided superior returns to all class of shareholders with excellent standards of corporate governance and a strong impartial regulator in the form of SEBI.

Banking system is considered more important due to variety of reasons including its ability to provide targeted lending to suit policies. Investors in Stock markets may not allocate funds in the sector in which policy maker want them to as numerous investors make their own decisions every day, every moment unlike banking system. However, due to the same, stock markets are also able to provide each person a choice of where he wants to invest in making it quite efficient. Banking system is considered more safe and robust. Most of the policy making and protection in financial markets relates to banking system. However, stock markets have become almost the same size in the wealth they represent. Why did this happen? Do people trust banks less despite policy protection? Do people trust stock markets more despite the daily volatility? Perhaps, higher and superior tax free returns have changed the perception of smart investors in favour of stock markets in last decade? We can leave the answers to the experts for further debate.

BSE in last 20 years have completely reformed themselves. BSE became fully automated in 1995. Stock depositories and clearing corporations were set up to make micro structure mechanism efficient and

robust. Derivatives in equities, currency and interest rates have been introduced. Small and Medium sector exchange platform has also been created. IPOs now take place through exchanges. BSE is now present in more than 1700 locations and almost 3 lakh users across cities and town are watching and trading on BSE every day. In addition to broker offices, investors are now able to watch and trade on BSE using internet and mobile facilities also. BSE has the capacity to take more than 5 lakh orders in a second and gives median response time of 200 micro seconds making it the fastest stock exchange in India and puts BSE amongst the fastest and largest stock exchange systems in the world.

India has huge demographic advantage with more than half of its population under the age of 25. On an average, 15 million youths will join the workforce every year, for the next 20 years which gives India a unique competitive advantage – while also is its biggest threat if India fails to create opportunities for its youth population.

The biggest challenge and opportunity for the government would be to create jobs – by creating an environment where Indian companies are able to grow and thus create more jobs, where SMEs find it easy to raise funds for their enterprises and where the youth is adequately trained to contribute and participate in the Indian growth story.

India currently ranks 134th in the world on the parameter of “Ease of doing business”. We may disagree to the extent of problems in India, but it is understood that developments are required. We need to create an environment where companies and entrepreneurs don’t fail just because of lack of access to funds; the youth don’t go unemployed due to lack of opportunities or lack of skill training.

These two areas, which actually go hand in hand should be the focus area for the country for the next 5 years. While it is the Government’s role to create policies, the implementation and the benefits we derive of those policies would depend on the Indian institutions. For instance, the Indian banking sector and the Stock Exchanges need to play a major role in addressing the first concern, for enabling the Indian enterprises to grow, compete and succeed. BSE, in the last 2 years, has been able to get 60 SME companies to get listed; listing of SMEs enables them to raise funds from the public, while giving the investors to become part of the success story if these ventures succeed. The SME market cap has already reached USD 1.25 billion in a short period of 2 years. If things go well, we hope to have USD 10 billion of wealth represented on BSE SME segment within the next 5 years. The success of the BSE SME Segment has prompted requests from PEs and new age entrepreneurs to give the segment a new name that would reflect the aspirations of the market from this segment.

The way, name of BSE is synonymous with capital markets over last 140 years, BSE SME segment has become the largest market of its kind in India with more

than 90% market share. Nurturing wealth creation in India for all shareholders – small investors, large investors, PEs, VCs, Angel investors, promoters, non-promoters – has been at the core of BSE philosophy all these years – that of transforming India in to a country where every one can partner with every one else irrespective of how much they want to invest, thus reducing entry barriers to investment. Providing conducive conditions for investments such as E-IPO, market making, etc. have been some of the innovations, the market regulator SEBI has pushed for in recent times. These reforms will make Indian capital markets even more attractive for investors in time to come.

BSE has also set up an Incubation cell to help promote entrepreneurs to develop their business models. We need to help thousands of such SMEs get access to funds and training for them to succeed – for themselves, for their investors and for the employment they would generate if they succeed.

The institutions themselves would have to take the lead in addressing the second issue – training and skill development for the youth. BSE has also taken the leadership in setting up of the BFSI Sector Skill Council, to help train the youth in BFSI Sector. A lot, however, still needs to be done to improve the employability of the youth and to provide them with opportunities of employment.

Stock markets also have their own issues. Although, automation has taken place, more transparency, fairness and efficient have been brought in to market functioning, market capitalisation have grown manifold to compete with the banking system, BSE has not been able to attract more small investors over last 20 years. To some extent, daily price volatility in stocks reduces the interest of many small investors who want consistency of returns. Investors who favour stability in returns might like to invest in G-Secs, corporate bonds, debentures etc on BSE. India needs \$1.3 trillion investment in its infrastructure sector, BSE can play a major role in raising part of this capital requirement; in areas like power, water supply, transport and river projects, etc.

BSE also needs to reduce the dependence of Indian markets on speculative activities. Most of the market activities in Indian markets are now concentrated on futures, options etc. Hedging is a legitimate activity and very useful to the society. Speculation is also a legitimate activity. However, its usefulness to society is limited. When the speculative activities become overwhelming vis a vis primary purpose of channelising savings and investments in to productive asset classes, it starts becoming harmful.

To continue to build on the tremendous transformation that has been brought to the Indian markets over last 20 years and make markets serve the nation in even better and more useful ways, BSE needs to make and market products which are more investment oriented and less speculation oriented. BSE needs to harp on corporate governance so that small investors are at par with owner managers as far as information availability is concerned.

BSE needs to do a lot of investor awareness helping savers across the country understand the importance of investments and BSE in nation building, job creation and also in getting superior returns for their own investments.

BSE has come a long way in service of the nation in last 140 years. It has a longer way to go. The work is still to be done in making India a full employment country. The task is cut out for BSE to work with banks, mutual funds, insurance companies, regulators, micro finance companies, brokers etc to be the most regulatory compliant exchange with the best returns for small investors and at the same time creating environment for good companies to raise funds for their growth and the economic growth of the country.

BSE's vision for 2035 is to have 25 crore investors registered with it up from the current 2.5 crore investors and market capitalisation of \$15 trillion up from the current \$1.5 trillion. BSE's success in these endeavours would also largely depend on the growth of India and Indian corporate world over next 20 years. Policy making and execution to create and sustain an environment conducive to doing business, creating jobs and enabling India to leverage its inherent strengths is a tough task but achievable. BSE would continue to work with all stakeholders of the country to continue to stick to its roots of being primarily an 'Investment Exchange' to the country in times to come.
