Increasing the Base of Retail Investors

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India's equity market after the economic reforms of 1991, showcase one of the greatest achievements of India's liberalization policies. The Sensex, which stayed well short of the 5,000 mark for most of the 1990s, has since then risen to cross 20,000 in 2008 and more than 30,000 recently, with an associated climb in market capitalization.

Across the world, equity culture is considered to be widespread and retail investor presence is substantial. As per the latest Survey of Consumer Finances conducted by the Federal Reserve in 2013 about 49% of United States' families were direct or indirect owners of publicly traded stock in 2013. The essential principle followed by the Securities and Exchange Commission in the USA, for example, is to encourage retail investor activity by, in the first instance, seeking to make markets fair and safe.

Thereby, regulators are paying special attention to the retail investor, whose exposure to the market either through direct investments or through instruments issued by intermediaries like mutual and pension funds has been increasing. However, unlike many of the world's stock markets, most trades on the Chinese stock market are made by individual retail investors, rather than institutional investors. Regulators in charge of stock markets have both promoted retail investor interest in market investments and put in place means to protect them once they have entered the market.

The Indian stock market is expanding in scope, size and scale day-by-day and so is the number of investors as in the recent past India, has seen a move in the positive trajectory as Indian households are warming up to financial products by putting a larger part of their financial savings into shares and bonds.

The improvement in performance of equity markets over the years depicted rising confidence of investors in Indian equity markets on account of strong growth prospects of the Indian economy. However it is very unfortunate to realize that very few Indians actually use this progress to their advantage, as less than 1.5 per cent of the total population invests in securities.

Needless to mention, Investors are the backbone of any securities market as they are the prime constituents and the key players in the financial system and an investor predominantly looks at safety, liquidity and return on investment as once the investors are sure of meeting of above-said three objectives; they invest their money without worry.

Evolution of policy scenario of retail investors in India

In order to understand the expanding base it is important to clarify the policy scenario of retail investors in India. The definition of the retail investor in India has changed over time. Till August 2003, under the SEBI (Disclosure and Investor Protection) Guidelines,2000, a retail investor was defined as an individual investor applying for allotment of 10 or less marketable lots in a fixed issue or up to 1000 units in a book built issue.

Since the prices of share values in IPOs from different firms can vary, definition based on number of shares applied for does not take into account the volume of investment made in any particular IPO by the investor concerned, though that is an important factor distinguishing the character of different investors.

To take account of investment size, the retail investor was subsequently redefined to reflect his/her choice of stock by value. In August 2003 the definition was amended to include all individual investors applying for securities worth Rs. 50,000 or less, with that value being subsequently revised to Rs. 1,00,000 in March 2005 and incorporated in the SEBI-Issue of Capital and Disclosure Requirements Regulations, 2009 and then to Rs. 2,00,000 in November 2010.

The increases were partly in order to adjust for inflation. While such definitions have been used to target concessions to the retail investor, analysing the behaviour of investors demarcated on the basis of these definitions is difficult, because comprehensive information on retail investors identified in this manner is hard to come by.

Thereby, retail domestic investors should be seen as a major component which can promote a degree of stability in the market but because of low retail-investor base, the benefit of the stock market boom is not known to have unleashed a wave of prosperity among ordinary urban class that such increase in corporate earnings and their share values bring as a rule, in more developed world.

Retail investment participation: the Indian Scenario

A survey of household saving and investment behavior conducted in 2011 by NCAER found that households investing in bonds, debentures, equity instruments, mutual funds and derivatives totaled 24.5 million and constituted 10.74 per cent of all households in the country. The proportion of investor households was nearly 21 per cent in urban areas and 6 per cent in rural areas; the differential in the proportion can be directly linked to financial literacy.

However, the question that remains is the degree to which households in India have chosen to park their financial savings in instruments directly or indirectly linked to the stock market. Data reflections show clear evidence of the pragmatic risk averse nature of Indian investors since despite the net financial saving rate increased to 7.7 per cent of gross national disposable income (GNDI) in 2015-16 from 7.5 per cent in 2014-15 and 7.4 per cent in 2013-14, the total share of savings in shares and debentures was only 0.7 % of the Gross financial saving. The fact is the household's savings are majorly in physical holdings i.e. 50% and there's a need for channelization of physical savings towards financial savings.

Socio economic structure in favor of increasing the base of retail investors

Favourable consumer demographics: The demographic transition will drive retail finance to flourish in the coming years. It is estimated that the proportion of population in the working age group of 15-64 years will be expanding significantly by ~27% (167mn) over the next 10 years. Currently (2009 estimates) an average Indian is 35 years old, however, in 2020, the average Indian will be only 29 years old as compared with 37 years in China and the US, 45 years in West Europe and 48 years in Japan.

The significant increase in younger population will offers a huge market for retail finance like consumer loans—personal, housing, and education etc. and other financial products like--insurance, mutual funds and wealth management etc. and thereby, the structural opportunity for enormous growth of retail finance in the coming years is evident.

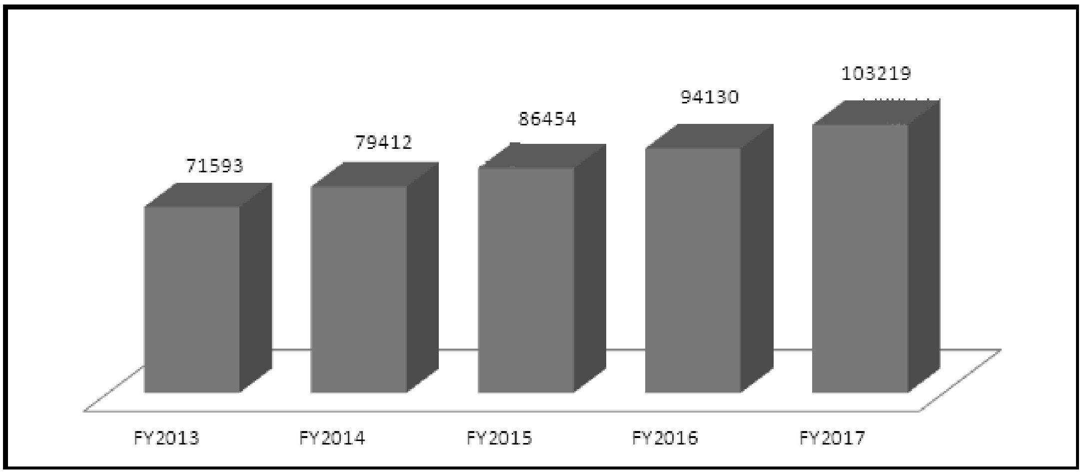
India's population projections **(in mn)**

Year	2001	2011	2021
Total	1,029	1,193	1,340
Below 15 years	364 (35.4%)	347 (29%)	337 (25%)
15-64 years	613 (59.6%)	780 (65.4%)	908 (68%)
Above 65 years	49 (4.8%)	66 (5.5%)	95 (7%)

Source: PHD Research Bureau, compiled from the report of the technical group on population projections constituted by the National Commission on Population

Rising income and consumption levels: Most importantly, the per capita disposable income--the spending and saving capacity of individuals have also grown steadily during the recent years. India's per capita disposable income increased significantly (i.e. a percentage increase of 44 %) from Rs. 71593 in FY2013 to Rs 103219 in FY17.

Spectacular rise in India's per capita disposable income (in Rs.)



Source: PHD Research Bureau, compiled from CSO. Note: Per capita disposable income is per capita Net National Income at current prices released by CSO.

Thus, given the strong income effect -- the spectacular rise in per capita disposable income, expanding middle class, and rapid urbanization, we believe opportunities in retail finance will grow manifold in the coming years.

However, in India, even presence cannot be taken for granted. Retail investor presence is likely to increase as per capita income in a country rises, since at any given level of inequality that would increase incomes and surpluses in the hands of those in the middle and upper-middle of the income distribution from where retail investors can be expected to come. But, this relationship does not seem to be exactly the same across contexts and time, with some middle income countries now reflecting a much greater presence of retail investors than the present day developed did when they were at the same level of development. So, if retail investor presence is considered important, intervention may be necessary.

Interestingly, Retail participation in the Indian stock markets has seen slight progress. Retail investors' holding in NSE-listed companies hit a six-year high of 21.35 per cent at the end of March 31, 2015, while Bombay Stock Exchange has saw a 34 % jump during the same period which it had attributed to several government initiatives such as financial inclusion and fall in inflation.

The improvement in performance of equity markets over the years depicted rising confidence of investors in Indian equity markets on account of strong growth prospects of the Indian economy. In addition, capital pumping in Indian equity markets by foreign institutional investors, combined with investments made by domestic financial institutions, corporates and high net worth individuals, has been largely responsible for increases in the volume and value of transactions and, therefore, in market indices and capitalisation.

The last five year pattern of the financial saving of household sector in India can be seen as follows:

(Per cent of GNDI)

Item/Year	2011-12	2012-13	2013-14	2014-15	2015-16
Gross Financial Savings (of which)					
1. Currency	1.2	1.1	0.9	1.1	1.4
2. Deposits	6.0	6.0	5.8	4.9	4.7
3. Shares and Debentures	0.2	0.2	0.4	0.4	0.7
4. Claims on Government	-0.2	-0.1	0.1	0.0	0.4
5. Insurance Funds	2.2	1.8	1.6	1.9	2.0
6. Provident and Pension Funds	1.1	1.5	1.6	1.9	2.0

*As per the latest estimates of Reserve Bank of India; GNDI: Gross National Disposable Income

Note: Figures may not add up due to rounding of; **Source**: PHD Research Bureau, Compiled from various sources

Overall, households parking a large part of their savings, outside of insurance and pension funds, in short maturity and highly liquid financial assets, do not seem to operate with long time horizons, being influenced more by returns registered in much shorter periods.

It has been observed that, returns from stock markets seemed to have influenced the trend in household financial savings behavior. Consider the period between 31 March 2005 and 31 March 2017. The Sensex rose from 6493 to 32,000 or by 392 per cent, implying an average return of 32.6 per cent a year, for an investor who bought a Sensex bundle (of shares) on the former date and exited on the latter date.

Turnover data seem to suggest that retail investors are important players in the Indian markets. Turnover data from the NSE indicate that in the years to 2010-11 the turnover recorded in the retail investor segment (as captured by the Average Gross Traded Value) exceeded that in the segments where institutional investors and proprietary traders where active. This could be due to either a larger number of trades by retail investors or the shares traded by retail investors being of higher average value or a combination of the two.

Turnover Analysis				
	Institutional		Retail	
	Average Gross Traded Value (Rs. Cr.)	% Contribution	Average Gross Traded Value (Rs. Cr.)	% Contribution
2009-10	397743	13.53	1493247	54.81
2010-11	618641	12.69	2396870	49.17
2011-12	847559	16.22	2114543	40.47
2012-13	909623	17.31	1929249	36.71
2013-14	1050969	16.5	2279202	35.79
2014-15	1 ,28,47, 080	11.55	4,15,81,358	37.39
2015-16	1 ,38,30, 974	10.67	5,18,76,427	40.01
2016-17	2,67,08,140	14.15%	8,26,35,016	43.78%

Source: NSE Annual Reports

Developing a Conductive Policy Environment

It is this imperative to develop a policy framework which should identify and correct any impediments to retail investor entry and participation, taking into account the need of such investors to invest in small lots and their weakness relative to institutional and high net worth individuals when seeking to acquire shares.

Since mutual fund institutions are important means of market engagement for retail investors, they must be encouraged to develop appropriate, transparent products that serve the asset building goals of smaller investor and build wide distribution networks for them. The distribution of mutual fund products through a wide network of bank branches spread across the country should be promoted in the coming times.

Going ahead, in order to safeguard the interest of investors particularly retail investors, stringent disclosure of information by issuers must be demanded, enhancement in transparency of information, setting policy framework for intermediaries for providing quality financial advice for selling investment products, promoting investor education, financial literacy and availability of affordable and accessible dispute resolution mechanisms for investors who feel aggrieved by the investment process.

Improving the ease and reducing the cost of entry for retail investors and activity in equity markets with the help of incentives by the Government would definitely going to enhance retail investor's participation in equity market, going ahead.

Suggestive Measures for policy framework to expand the investor base

- First, it should identify and correct any impediments to retail investor entry and participation, taking into account the need of such investors to invest in small lots and their weakness relative to institutional and high net worth individuals when seeking to acquire shares.
- Second, it should strengthen regulation aimed at guarding against market manipulation and price rigging since losses sustained by retail investors as a result of such activity makes them withdraw from markets and stay out.
- Third, there is need to ensure that information disclosure by issuers of equity and listed companies is comprehensive and clear so as to allow retail investors to arrive at informed judgements on investment options.
- Fourth, it is necessary to educate investors not only on the potential savings opportunities in the market, but also on an evidence-based, sensible investment strategy.
- And, finally, it is necessary to strengthen the mutual fund distribution network in order to attract retail investors to the Indian Capital Markets.

Conclusions

It is thus evident that even as of today the general assessment is that retail investor interest in India's capital market has been far short of potential despite the continuous efforts made by the government and financial institutions in promoting retail investor activity in the market, by organising investor education activities.

A conducive policy environment must be promoted for enhancing retail investor presence and activity in equity investments. Keeping in view India's growth potential in the coming times the share of retail investors in equity market should be enhanced in the coming times coupled with conducive policy environment.

There is thus a need to ensure that information disclosure by issuers of equity and listed companies is comprehensive and clear so as to allow retail investors to arrive at informed judgments on investment options.

It is also necessary to educate investors not only on the potential savings opportunities in the market, but also on an evidence-based, sensible investment strategy since that in the long run retail investors would in all probability expose themselves to the market largely through institutional devices such as mutual or pension funds. But even this institutional intermediation does not necessarily serve them well, and has on more than one occasion worked against retail investor financial interests.

To conclude, I believe, there is an urgent need to create a platform where Government and Industry associations should jointly organise a number of investor education programmes for enhancing the financial literacy levels of retail investors.