Capital Market Outlook

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"Like tiny seeds with potent power to push through tough ground and become mighty trees, we hold innate reserves of unimaginable strength. We are resilient" – Catherine DeVrye, The Gift of Nature

The current global economic landscape is characterized by an era of change and the world economy is gripped by an economic turmoil - high inflation, higher interest rates, geopolitical turbulence, volatility in asset prices, uncertainty in market cycles. A looming recession is anticipated, nevertheless, the Indian equity capital market is once again outperforming its international counterparts, thanks to our resilient and growing economy.

Similar to other global markets, the Indian market experienced its fair share of ups and downs. Since the beginning of last year, central banks worldwide have gradually increased interest rates in an attempt to curb inflation. Consequently, foreign investors withdrew their funds from equity markets and sought safer alternatives such as debt instruments.

While on one hand, calendar year 2022 and early 2023 was extremely tough for global investors, most of them were surprised how well Indian markets ended up performing. After all, Indian equity markets had the seventh year of positive equity market return and the World Bank increased its forecasted growth rate to 6.3% fiscal year 2023-24.

In plain and simple terms, it is evident that India has sustained its growth trajectory. Although the pace of growth may not have been uniform, it is remarkable that a better-than-expected growth was witnessed. India's GDP expanded by 6.1% in the most recent quarter, surpassing the 4.4% growth recorded in the previous quarter. While there has been a deceleration in the growth rate from 9.5% in the FY22 to 7.2% in the FY23, it is worth highlighting that India's growth rate has exceeded initial expectations.

India's economic growth trajectory is currently witnessing a transformation from a GDP per capita of \$2,500 to \$5,000, a significant development that should captivate the attention of investors over the next 5-10 years. We have seen this with China in 2007. This significant rise in per capita wealth holds immense potential for various discretionary sectors and businesses that can strategically position themselves to leverage this trend. By capitalizing on this opportunity, such businesses stand to reap substantial benefits, as this transformative shift has the capacity to be truly life-changing for many.

The growth of the market infrastructure over the years has played a pivotal role in facilitating this economic expansion. While it widely acknowledged that domestic and foreign capital flows exhibit a certain degree of cyclicality, the overall trend and direction remain discernible. As India's economy continues to grow, there is a clear expectation of an increase in both absolute savings and the percentage of funds allocated to financial assets and equity. This can be observed particularly through the significant increase in the quantum of deal sizes, both in primary and secondary markets. For a 5-year period between April 2013 and March 2018, INR 1,27,967 crore was raised through IPOs in India. In the next 5-year period from April 2018 to March 2023, this number has increased almost 80% to INR 2,30,000 crore. Five years ago, an Indian IPO of over INR 10,000 Crores was almost impossible or limited to exceptional companies. However, post pandemic, we have witnessed successful execution of 3 IPOs exceeding the INR 10,000 Crore mark. This upward trend reflects the growing appetite of investors in the market. Robust inflows from foreign portfolio investors to the tune of US$ 8 billion in the first half of CY23 and phenomenal investments by domestic institutional investors to the tune of US$ 11 billion during the same period is very encouraging. Strong monthly SIP inflows into Mutual Funds to the tune of INR 15,000 crore per month, increasing consistently month on month with deeper penetration and larger number of folios getting added is a trend that will continue. This will lead to significant inflows into capital markets leading to buoyant primary as well as secondary markets.

A remarkable feature of the India capital markets has been the continuous improvement of market infrastructure. The recent implementation of the T+1 settlement cycle for secondary markets is a case in point. This seamless transition to T+1 settlement cycle has been a big feather in the cap for India. This strategic move facilitates a faster circulation of funds, eliminating the need for an additional day's wait and will foster increased investment. While most global markets operate on a T+2 basis or longer settlement cycles, India's adoption of the T+1 settlement cycle positions it even ahead of the United States and makes the Indian markets most efficient in terms of secondary market infrastructure.

SEBI has recently finalised the timelines for implementation of reduction in settlement cycles for primary markets too, transitioning from T+6 regime to a more efficient T+3 regime, which is half of the current settlement cycle. This anticipated reduction will benefit both issuers and investors as issuers will have faster access to the capital raised which will further enhance the ease of doing business and investors will reap the benefits of having early credit and liquidity concerning their investment. SEBI has continuously been evolving the regulatory processes to shorten settlement cycle timelines across capital market products, underscoring the consistent enhancement of India's equity capital market infrastructure. These endeavours serve to improve liquidity levels and foster greater financial participation among all categories of investors.

Considering India's projected growth rate of approximately 7%, it is reasonable to expect that quality companies can surpass these figures and achieve better growth rates. This is leading to a renewed emphasis on recognising these trends and valuing high-quality businesses, both in the public and private sectors. Additionally, improvements in governance and disclosure norms have led to greater accessibility for minority investors.

Indian markets are also observing a significant trend among Indian entrepreneurs who are successfully establishing and monetising their businesses. The emergence of such an ecosystem is clearly evident and real. Private equity firms have emerged as prominent acquirers, going beyond traditional approaches and actively embracing the role of promoters while assuming control. These firms have consistently engaged in the acquisition of businesses, facilitating them to scale rapidly and eventually selling them for further monetisation. This trend is reflected in the sustained growth of private equity and venture capital investments in India, which have surpassed $60 billion for the third consecutive year. As of the end of 2022, India recorded Private Equity and Venture Capital investments exceeding $61.6 billion across more than 2,000 deals. India's share of investments in the Asia-Pacific region has also increased from approximately 15% in 2021 to around 20% in 2022, as global investors increasingly adopt a "China+1" strategy.

Additionally, the Indian equity capital markets have experienced a growing demand for stable cash flow generating assets. In recent years, there has been a prominent increase in the interest among yield investors in newly introduced investment products such as Real Estate Investment Trusts (REITs) and Infrastructure Investment Trusts (INVITs). If numbers are anything to go by, there has been a significant uptick in mutual fund investments in REITs and INVITs, particularly post the pandemic. The value of holdings in these assets, which amounted to just INR 734 Crore as of March 31, 2020, has soared to INR 5,200 Crore as of March 31, 2023. Furthermore, the number of asset management companies and fund houses investing in REITs and INVITs has surged from 7 in 2020 to 18 in 2023, spanning a mere three-year period. It is worth noting that Mutual Fund investments in REITs and INVITs currently represent a modest 0.13% of the INR 40 trillion total assets under management. Hence, we are likely to see greater demand for these products in the near future as they not only help sponsors unlock the massive value of real estate and infrastructure assets but also enable retail investors to participate.

The Indian government too has actively participated in disinvestment activities and is anticipated to continue doing so, with plans to raise INR 51,000 Crore through stake sales in various state-run companies throughout the year. There have been many examples of capital market-linked disinvestment include the likes of LIC, Coal India, IRCTC, amongst others.

The Indian economy remains highly appealing to both global and local investors and the markets have both widened as well as deepened. Indian Capital Markets will continue to rise and shine.