Indian Capital Market-2025

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India's capital markets which chiefly comprise equity, debt, foreign exchange, derivative markets and commodity derivatives have come a long way since activities first commenced in 1875. The story of India's capital markets is unfolding at a rapid pace. Aided by disruptive innovation in the execution aspects, regulatory changes in the supervisory disciplines, and an increase in the overall participation rate, the growth momentum will continue even as India occupies a more sizable portion of global capital flows and global investor attention given its untapped demographic dividend. The government has set a target of making India a USD 5 trillion economy by 2025. Predicting the state of our capital markets industry in 2025 is challenging but we can attempt to imagine where we will be 7 years hence, given the USD 5 trillion target, by first noting where we are currently, then by recognizing the economic and business drivers that would shape India and finally attempt to imagine some business characteristics of the industry around 2025.

A) Recent Trends and Statistics

The growth momentum continued across most of the sectors of India's capital markets:

- Primary Market: In 2017-18, a total of around ? 8.4 trillion was raised from the capital market representing a CAGR of around 15% over the previous 7 years[1]. There was a significant jump in the amount mobilized through public and rights of equities, qualified institutional placements and preferential allotment issues. The amount raised via private placement of corporate debt however was lower as compared to the previous year.
- Secondary Securities Market: The average market capitalization of BSE and NSE has increased at a CAGR of around 11% over the past 7 years.
- Corporate Debt: The industry is gradually expanding its reach towards the corporate bond market and reducing its reliance on bank credit. The amount mobilized via issuance of bonds has been rising continually over the last 7 years. At ? 18 trillion, money raised through corporate bonds in 2017-18 represents a healthy 16.8% growth over the previous 7 years. While bank credit offtake may have suffered of late due to high NPAs and stringent capital requirements under Basel norms, tailwinds like better transmission of policy rate, structural bond market changes, increased transparency and price discovery have been responsible for the spike in bond market issuances.
- Mutual Funds: The net resources garnered by mutual funds fell by 21% in 2017-18 as compared to the previous year. Even as the momentum in MFs waned last year, the industry did process a significant net investment of ? 2.7 trillion. The investments of MFs in equities and debts have emerged as an effective force in containing market volatility by counterbalancing the impact of Foreign Portfolio Investors.
- Alternative investment funds (AIFs): Funds raised by AIFs have consistently increased since their inception in 2012. In calendar year 2017, AIFs raised ? 182.65 billion, a 38% increase over previous calendar year.
- Foreign Portfolio Investments: The money invested by overseas investors in debt markets increased drastically to ? 1.2 trillion in 2017-18 as compared to a net outflow of ? 73 billion in the previous year. The equity segment however, witnessed a more than halving of investment in 2017-18 to ? 26,0 billion. It is likely that these flows will continue to be volatile in the future as well given global cues, which is why the stability provided by the money raised by mutual funds and alternative funds is critical.
- Insurance: The life insurance industry has also seen its first year premiums at ? 1.94 billion surge by a CAGR of 6.4% over the previous 7 years[2]. At ? 1.5 billion for FY18, the gross direct premiums collected by general insurance companies has grown at a rate of 18% over the same period[3].

B) Drivers for Change

India will seek to monetize its demographic dividend by ensuring that wealth creation opportunities become more democratic and wealth thus created moves to financial saving venues as opposed to the traditional gold and real estate options. This will create a multiplier effect thus making the financial sector both the primary driver as well as a big beneficiary of India's economic expansion. I have listed below the important drivers for change that are expected to shape the Indian economy in the years to come:

- Generation of Growth Capital:
    - o Financialization of Savings: The average percentage of financial assets in a balance sheet of a representative Indian household is around 20% today. This ratio has been increasing in recent times due to the investor education initiatives of the government, regulators and other industry participants.
    - o Democratization of Credit: More and more net new borrowers are now able to avail loans thus spreading

out the outstanding across a wider borrower base. Even as this "diversification" spreads the risk out, the momentum of the trend will continue to increase driven by macro and structural developments like better information sharing of borrowers' data, technology platforms for distribution of credit and increase in financialization of savings.

- Utilization of Capital for Growth
  - o Consumption Growth: In 2025, India's per capita income is likely to reach USD 3,500 from the current USD 2,000 levels. India's middle class will expand rapidly as the country becomes more urbanized. Globally, it has been observed that the moment a country's per capita GDP crosses USD 2,000, the proportion of discretionary expenditure rises dramatically. This will necessitate investments in the supply chain which has implications on ecommerce and consumer credit business volumes.
  - o Infrastructure: The policy focus on improving connectivity and mobility will see investments in industries related to telecom, roads, airports, railways. Mega projects like the Phase I of the Bharatmala project, new dedicated freight corridors, the UDAN scheme, various Metro rail projects will provide new opportunities to capital markets to raise capital in the run up to 2025.
  - o Housing: Rapid urbanization will necessitate increased investments in housing and related urban infrastructure. It is expected that affordable housing presents a ? 6 trillion opportunity over next 5 years making this a very attractive trigger for all around growth.
  - o If India must achieve its goal of reaching USD 5 billion of GDP by 2025, nearly all industries will have to achieve a 2x – 3x growth.

C) Prognosis

We have looked at the current state of our capital markets and the change drivers shaping India. The destination (USD 5 trillion GDP) has been well articulated and there will be many paths to get there. I list below, in brief, some changes which we should prepare for in our capital markets to support this significant journey:

- Credit Markets: The securities market can be a wholesome source of risk capital only in the presence of a liquid and vibrant corporate bond market. Credit market is expected to more than triple over the next 7 years to around ? 350 trillion. Retail and SME credit is expected to grow faster than wholesale credit. The focus on housing will ensure that mortgages will emerge as a significant growth vector within retail credit and are expected to grow at a CAGR of 23%. By 2025, credit markets could be more like equity markets – capital allocation to corporates and individuals will be more market based, flexible and will reach deeper.
- Wealth management: Financialization of savings is expected to boost the industry wealth pool from the current INR 200 trillion to INR 500 trillion. Even as MFs are expected to see their AUMs increase five-fold to INR 80 trillion, AIFs are expected by 10 times to a size of INR 20 trillion.
- Equity Capital Market & Advisory: History shows us that trading volumes grow between 4 to 5 times when the GDP of a country doubles. Average daily institutional equity trading volume is expected to increase from INR 138 billion to INR 500 million. On the investment banking side, the market is projected to grow 7 times by 2025 while the anticipated increase in the number of billion-dollar market cap companies in India will see the advisory market growing rapidly as well.
- Insurance: Growth in life insurance is expected to be led by private insurers with the total industry premium collected reaching INR 11 trillion. The general insurance market will also see similar trends with the annual premium growing by 3 times to reach INR 5 trillion.

Other trends

- Client Experience: Given the themes of democratization and the demographic dividend, the newer participants will be online, more tech literate so the growth in the broader financial markets distribution and communication has to embrace digital technologies. Capital markets participants will benefit from a client first approach. We are likely to see a gradual lowering of client switching cost and unbundling of products and services as client stickiness and consequently profits become intertwined with client experience.
- Pooling of Debtor Data: Credit bureaus will continue to grow in relevance. Borrower data and what firms do with it will become critical to their business success. India's financial system's soundness ratings will rise as credit information becomes more freely available.
- Business Data: Indian capital markets will see business data management and analytics evolve as a strategic function in the coming years. Data prowess of capital market firms will impact their performance across a range of activities like client experience, risk management, trading strategies and regulatory compliance.

Conclusion

I believe that India will make its tryst with its economic destiny by 2025, a measured but eventful 75 years after becoming a republic. While the first trillion USD of India's GDP took 60 years to form, the second trillion took only eight years. It is entirely possible that India adds an additional 3 trillion USD to its GDP in the next 7 – 8 years. India's capital markets industry will thus have to gear up to ensure that it provides the required capital and platforms to the idea that is India.

[1] Recent Trends & Statistics: data sourced from www.sebi.gov.in (unless otherwise noted)
[2] www.irdai.gov.in
[3] Drivers for Change & Prognosis: data represents Edelweiss' view