The Journey to 100 Million Investors

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As widely anticipated, the pandemic had far-reaching impact on the global economy. Jobs were lost at record rates and income plummeted, as restrictions forced the wheels of the economy to slow down or intermittently grind to a halt. Stark images of suffering induced by this economic hardship will remain with us for a long time.

Perhaps, the unexpected outcome was some of the positive trends that have emerged over this period. The pandemic seems to have brought millions of new investors into the country's capital markets. Demat account additions jumped by an all-time high of 10.7 million between April 2020 and January 2021, more than double the accounts opened in the entire financial year 2019-20 at 4.7 million.

Soaring internet penetration, growing financial awareness, adoption of digital payments, a convenient onboarding process enabled by e-KYC and the emergence of technology-led platforms providing integrated access to various investment avenues may have already prepared the ground for this transition. The resultant ability to invest or trade remotely from the comfort and privacy of one's home during the pandemic seems to have catalyzed the rapidly growing tech-savvy generation to make this shift.

The Mutual fund (MF) industry also saw considerable folio additions. Over 8.1 million investor folios were added in 2020-21, as against 7.3 million folios in 2019-20 as per data from the Association of Mutual Funds in India (AMFI). Growing investor awareness aided by the industry's successful 'Mutual Fund Sahi Hai' campaign as well as the expanding reach of distribution and advisory services – both physical and digital – are helping widen the reach of mutual funds.

This may lead us to a few questions. Is this recent surge in accounts and folios a temporary blip, or will it sustain? Are investors acknowledging the importance of investing in meeting their financial goals? With the domestic MF industry coming a long way with AUM crossing the Rs 34 trillion mark, is there further headroom for growth?

India's Mutual Fund AUM as a percentage of our GDP is currently estimated at 12%. This makes it a fraction of the global average of 63%. In comparison, this ratio for developed markets like the US and Canada is 120% and 80% respectively. Some of the other emerging markets such as Brazil (68%) and South Africa (48%) boast of a better penetration. This would certainly point to a lot of potential headroom for AUM growth in this industry. Interestingly, industry research on the experience of some of these countries also indicates that MF AUM in developed, as well as emerging markets, witnessed faster growth after crossing the AUM to GDP threshold of 10%-12%. Many countries witnessed a compounded annual growth rate of over 15% for the next 10 years once they went past this threshold.

India's ratio of AUM to Bank Deposits also conveys a similar picture. India's MF AUM reached 21% of Bank Deposits in FY21. In comparison, this ratio for the US stood at 161%, while despite the more recent growth in MF AUM, China is already above 46%.

Looking at individual participation rates, a mere 2% of Indians currently invest in mutual funds, with MFs forming just 3% of gross household financial savings. For the broader capital markets, less than 5% of our 1.3 billion-plus population is estimated to participate, with only a fraction of these numbers being regularly active. Trading volumes in the Indian capital market are significantly lower than markets such as the United States, United Kingdom, Germany and China.

Similarly, the overall exposure of Indian households to equity assets on their financial balance sheet is among the lowest amongst the major markets in the world at 14%. Notably, the risk appetite of the American household is at 45%, followed by other major economies like Canada and Spain at 42% and 38% respectively.

While the steady growth in the number of PANs is a positive sign indicating growing formalization of the economy, only a small fraction of the 420 million PANs in India currently have any meaningful exposure to the capital markets.

The glass is half full. All these data points indicate a massive opportunity ahead. Productive channelization of savings into financial assets will continue to be a huge growth area over the next decade. Crossing the 100 million active investors mark is well within reach.

So, what can be done? What steps need to be taken to accelerate this further?

There are several powerful enablers already in place – including a responsive regulatory framework, resilient markets infrastructure and progressive industry participants. Yet, several additional opportunities will further enable this transition. These include the continued need to widen and deepen financial awareness; expanding quality distribution and advice; the effective leverage of technology; and improving service while lowering costs through economies of scale - to name a few. Let us examine a few of these ahead.

Awareness, it is said, is the greatest agent for change. The transformation ahead will need to build further on the good work underway with financial literacy. Awareness drives by regulators like SEBI, industry associations like AMFI as well as individual industry players have helped dispel many of the myths and fears associated with investing. They have also increased the visibility of the industry over the years. The role of the media in aiding this effort is also salutary. Conditions are now ripe for taking the next leap. Accelerating information flow propelled by digital reach offers unprecedented new opportunities in this area. With the wider variety of popular new digital mediums being available across languages, traditionally complex messages can be simplified and made more relatable. Combining learning from new-age consumer marketing techniques and microfinance that have already penetrated deep into hitherto unaddressed areas - can help percolate the message of sensible investing to a much wider audience now.

Sustained participation in this process will also need first-time investors to have a reasonable – if not an outstanding – experience. Critical here will be the role of the distributor or advisor. Irrespective of the model chosen – physical, digital or 'phygital' – distributors and advisors will need to be responsible in their communication and service, ensuring that long term investing is not relegated to a speculative 'make-a-quick-buck' scheme by simply highlighting spectacular recent performance. Well-established practices of understanding investor needs and goals, risk appetite, cash flows, experience etc. remain relevant, and highlighting 'inconvenient' topics like the potential loss of capital must be covered effectively, and not just be a 'tick-in-the-box'.

Technology has already made information and access available at an investor's fingertips, helping more and more first-time investors test equity investing. Investment managers as well as intermediaries including distributors and advisory firms will need to continue to adapt and enhance their tech capabilities further. Investments in cloud computing, artificial intelligence, machine learning and data analytics are rapidly changing the world of capital markets. Cost reduction from the scale benefits of these emerging technologies will be critical to compete in an environment of reducing margins, effectively transferring the benefit of this growth to the end investor.

The role of overall customer experience - across all interfaces - is now well established as the critical success factor in today's startups. Individuals quickly benchmark service levels to the latest and the best. Firms that are comparable in terms of products will have to differentiate in terms of service to compete and win. Digital support, quick grievance resolutions, 24x7 access, moving to proactive support from the erstwhile reactive response, online capabilities - to name a few – will enable firms and advisors to reach out to their target audience, and benefit from their share from this pie of growing investors.

Finally, the self-reinforcing cycle of happy investment outcomes will rely not only on good products and processes but as much on good investment behaviour. The discipline of regular, long term investing has already benefitted millions of Indian investors through the MF industry's successful drive to promote Systematic Investment Plans (SIPs). With over 40 million investors contributing over Rs. 9,000 crores every month, SIPs now contribute almost 15% of industry AUM. Helping investors navigate during periods of uncertainty, SIPs have proven to be an ideal route for new investors to gradually enter equity funds, avoiding the worries of market timing while befitting from cost averaging.

In conclusion, capital markets play a pivotal role in the growth of an economy, and in meeting the country's socio-economic aspirations. They provide the financial resources required for the long-term sustainable development of the economy. Indian capital markets are no exception. Its various segments have witnessed notable growth over the years. Yet, this growth may still be the proverbial tip of the iceberg. A much larger opportunity ahead is evident. Building on the strong foundation already established, a confluence of recent factors may well act as the tipping point to propel the industry towards crossing the 100 million investor mark much earlier than we can currently envisage. Look out for more surprises!

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Mutual Fund investments are subject to market risks, read all scheme related documents carefully