15th FICCI Annual Capital Market Conference (CAPAM) 2018

"Blueprint for Capital Market in New India 2022"

September 11, 2018

Trident, Nariman Point, Mumbai

1. Ladies and Gentlemen, it gives me great pleasure to address this august gathering today.

A. <u>Economic Outlook</u>

2. During the April-June quarter of the current year, GDP of India grew by 8.2%. This is the highest growth in two years and strongest since the first quarter of 2016. This was achieved, inter alia, by 13.5% growth in manufacturing, 5.3% in agriculture and 10% growth in investments. Robust corporate earnings figure and the Purchasing Managers' Index (PMI) also indicate that the economy is in a recovery mode.

3. IMF also projects an overall favorable macroeconomic outlook for India and expects economic growth to rise to 7.3% in FY2018/19 and 7.5% in FY2019/20, on strengthening investment and robust private consumption. With concerted measures being taken to address the twin balance sheet problems of the corporate and banking sector, the outlook is expected to improve further.

4. As far as economic risks are concerned, increase in international oil prices, tighter global financial conditions, spillover risks from a global trade conflict, and rising regional geopolitical tensions are some of the potential risks.

B. <u>Fund Raising Activities</u>

5. Let me now give an overview of the fund raising activity happening in the capital market and the interesting trends that I see with regard to IPO market.

6. A record amount of Rs. 8.8 trillion was raised from Indian capital market during 2017-18 (through equity and debt) against Rs. 7.7 trillion during 2016-17. Rs. 2.3 trillion has already been raised in the first quarter of this financial year. This kind of sustained fund raising from capital market is very encouraging. It definitely signals increased economic activity.

7. Apart from an increase in aggregate amount of funds raised, the individual <u>size</u> of offerings has also increased over time, thereby indicating increased capacity of the market to finance larger issues. Average size of IPO has increased more than three times from Rs 640 cr. in 2015-16 to Rs 1,900 cr. in 2017-18 and median offer size increased from Rs 490 cr. in 2015 -16 to Rs 780 crore in 2017-18.

8. One comforting feature of the IPO market is that companies with a certain degree of maturity only are accessing the market, where as for their early stage funding, companies are relying on financing from private and institutional sources. The median age of companies coming out with IPOs during last two years was about 17 years. In contrast, the median age of companies coming out with IPO in US is about 10 years.

9. Over 70% of the IPOs during last 3-4 years consisted of Offer for Sale, signaling exit by early stage investors like PE/VCF. This is also an indication of maturing of Indian capital market as early stage investors are able to

successfully exit from their existing investments so as to be able to channelize their investments for other productive economic activities.

10. A look at the sectoral composition of benchmark indices, particularly SENSEX, shows that the index is predominantly dominated by the financial sector. The weightage of financial sector in SENSEX increased from 21% in March 2008 to 41% in March 2018 followed by IT sector with a weightage of 12%. During the same decade, the weightage of industrial sector in SENSEX declined from 13.5% to 8%. A look at the top 100 companies by market capitalization shows that the share of financial sector has increased from 15% in March 2008 to 23% in March 2018 and that of industrial sector has declined from 14% to 12%.

11. To a casual observer, this may indicate a diminishing role of industrial/ manufacturing sector. However, if we look at the sectoral composition of IPOs over time, we discern a different picture. For instance, the share of industrial sector in IPOs has increased from 15% in 2012-13 to 36% in 2017-18. In contrast, the share of consumer discretionary goods and services sector and financial sector in IPOs has declined, respectively, from 44% to 23% and 13% to 11% during the same time period. The IPO market, therefore, appears to be indicating a trend which probably will get reflected in the benchmark indices at a later stage.

12. Added to this, the number of SME IPOs has gone up from 38 in 2015-16 to 80 in 2016-17. This number further increased to 151 in 2017-18. This is yet another indicator of the increasing role of financial disintermediation that capital market is facilitating.

13. Data on returns generated by IPOs reflects that price discovery in primary market is probably becoming more fair, reinforcing the fact that better quality companies with reasonably longer duration of track record are accessing the market. During 2016-17, 60% of the IPOs, over a period of 1 year from listing, generated a return exceeding the 19% return generated by NIFTY during the same time period.

C. Important measures by SEBI pertaining to Corporates

14. During my address at this FICCI event last year, I had articulated that, if public markets have to sustain the current and enhanced capital raising efforts, it is important that markets continue to satisfy some broad conditions.
    i. The standard of conduct in the market for all stakeholders (intermediaries, merchant bankers, issuers, auditors, etc.) has to further strengthen and be benchmarked to the best in the world.
    ii. Secondly integrity of the markets should be non-negotiable so that it gives a high degree of comfort and confidence to investors.
    iii. Lastly, there should be adequate competition with frictionless ease of doing business for all stakeholders

15. In light of these views, let me now talk broadly about the direction of reforms undertaken by SEBI during the last one year.

16. Corporate governance standards are foremost for enhanced standards of conduct by corporates. Keeping in view the recommendations of the Committee headed by Shri. Uday Kotak, along with the public comments thereon, SEBI has taken decisions on several measures to further improve corporate governance in India.

17. For instance, SEBI, inter alia, enhanced the focus on independent directors, prescribed separation of posts of CEO/ MD and Chairperson; enhanced role of the Audit Committee, Nomination and Remuneration Committee and Risk Management Committee; strengthened approval and disclosure of related party transactions (RPTs) and mandated mandatory consolidated quarterly results w.e.f. from FY 2019-20 and mandatory secretarial audit for listed entities and their material unlisted subsidiaries.

18. While, globally, India already ranks high on the aspect of protection of minority interests as per the Doing Business Report of the World Bank Group, the recent measures on corporate governance by SEBI would add significantly in enhancing investor confidence by way of further enhancing transparency and accountability in the governance of corporate sector in India.

19. Based on the inputs received from various stakeholders and through wider consultations, SEBI recently reviewed the ICDR, SAST and Buyback regulations. The recent changes to ICDR regulations, inter alia, include rationalization of disclosure requirement, rationalized definition of promoter group and aspects which would further enhance overall ease of doing business.

D. <u>Challenges</u>

20. KPMG report titled *"Ten key global regulatory challenges for 2018 –action to drive effective change in financial services"* outlines - Cyber-security and Data Privacy; Risk Management, Governance and Controls; Conduct and Culture; Compliance Risk Management; Financial Crimes Compliance; Strategic Risk and Disruptions; Fiduciary and Investor Protection; Data and

Analytics; Capital and Liquidity; and Geopolitical Uncertainty as the 10 major regulatory challenges.

21. While the report intends to guide financial services companies in allocating valuable resources and investment to manage risk, the list also has implications for regulatory policies. In this context, let me highlight 3-4 areas where SEBI is focused on at prtesent.

22. Cyber security is clearly an area SEBI is actively involved in. A High Powered Steering Committee on Cyber Security (HPSC-CS) comprising experts is providing overall guidance to SEBI in developing and maintaining cyber security and cyber resilience requirements aligned with Global best practices and Industry standards.

23. Towards enhancing market integrity, SEBI has strengthened the framework for algorithmic trading recently. To further strengthen the rules to deter financial crimes like frauds, market manipulations and insider trading, the Fair Market Conduct Committee constituted by SEBI and headed by Dr.T. K. Viswanathan, Formerly Union Law Secretary has since submitted its recommendations which were also put in public domain seeking comments. A view on these recommendations will be taken soon.

24. With increasing amount of financial transactions, all of us are faced with volumes of data to deal with. The surveillance system of SEBI already has an embedded data warehouse and business intelligence system. Presently, SEBI is focused on further enhancing its in-house analytics capacity to make better use of data analytics for its supervision function. SEBI has recently invited expression of interest from companies for enhancement of analytical

capabilities and setting up of private cloud to provide infrastructure, storage and computing capacity to different upcoming projects of SEBI.

E. Theme of the Conference

25. Year 2022 is a landmark year for all of us as India complete 75 years of Independence.

26. The vision of New India along with its impact on the economy is bound to re-shape our capital markets by 2022. In order to support higher economic growth, there is a need for concerted effort towards further developing the Indian securities market so as to increase market based financing and supply of risk capital. In the coming years, SEBI will continue with its endeavor of providing the right regulatory environment and facilitating development of market infrastructure to meet the financing need of economic activities through the securities market.

27. In furthering market based financing, corporate bond market has to play an increasingly important role. Further development of a liquid corporate bond market through trading of securitized receipts, increased participation of domestic institutional investors and though other relevant policy and operational measures will continue to engage the attention of SEBI going forward.

28. Increasing the role of Indian securities market hinges upon a transformational change in the current allocation of household's savings between physical and financial assets and there is a need to channelize more and more savings to productive financial assets. Policy refinements for enhancing geographical spread of securities market in India will continue. Apart from enhancing

investor awareness and improving access to securities market, technology solutions will be explored to achieve the objective of scaling up of delivery channels in the market.

29. Continued investor confidence is a crucial factor in attracting more investors to securities market. Right governance framework and a transparent and clean market go a long way in meeting these expectations of investors at large. SEBI will continue to focus on further enhancing the overall governance standards in the market, be it for issuers, intermediaries or market infrastructure providers.

30. In the next wave of capital markets growth, apart from the traditional markets i.e. equity, bonds, and currencies, we expect a lot more focus on the commodity markets. In this context, integration of commodities and securities derivative markets and introduction of new products, including option and index products in the commodity derivatives space is an area which have been actively engaging our attention.

31. Technology use in the financial sector is already disrupting the traditional regulatory tools forcing regulators to keep pace with the changes. Going forward, increase in use of machine learning and artificial intelligence among other technologies, in the capital markets is a writing on the wall. The complexities in the capital markets are only going to increase with time. SEBI needs to quickly upgrade its regulatory capacity to properly comprehend the nuances of technological changes with a view to staying ahead of the curve.

32. “Proper level of regulation” is an issue with which a regulator has to constantly grapple with. As for SEBI, the objectives of improving ease of

doing business and maintaining market integrity have to be properly balanced. Any imbalance leads to either over regulation or under regulation. While it may not be always possible to accurately quantify the costs and benefits of making a regulation, it will be our endeavor to keep on improving the processes going forward.

33. Our overall vision is to have bigger, cleaner and safer markets. As of now, India's capital markets are 8th largest in the world in terms of market capitalization. Our market cap to GDP ratio is 86%. SEBI is committed to facilitate further growth of markets. SEBI is equally committed to ensure clean and safe markets. We are duty bound to ensure that the market mechanism is not misused or manipulated by the unscrupulous elements. It is but natural to keep focus on safety issues including systemic risks. In reality, all these issues are inter-related.

34. I wish you all a fruitful and engaging deliberation during this conference.