SEBI INVESTOR SURVEY 2015

Securities and Exchange Board of India

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Foreword

With the progress of the Indian economy, especially when the focus is on the achievement of sustainable development, there has been an ongoing attempt to include maximum number of participation from all the sections of the society. A host of innovative and dedicated measures have been undertaken by the Government of India to drive forward the financial inclusion agenda. However, research has shown that the development of securities markets has a distinctly unique effect on the development and growth of an economy, beyond the role played by the banking sector. Additionally, securities markets instruments provide higher risk adjusted returns and has significant positive effects on individual portfolios due to diversification. Thus, developing financial markets through high retail market penetration has both social and individual benefits, calling out for a financial markets inclusion as a narrower but arguably as effective goal as financial inclusion alone.

SEBI Investor Survey 2015 (SIS 2015) is the fourth in a series of periodic studies conducted or sponsored by SEBI to quantify actions and perceptions of retail investors. This iteration of the study has the largest breadth and depth, covering more than 200,000 households in the listings exercise and more than 50,000 households in the final survey across cities and villages in all states and union territories (except Lakshadweep). Another unique aspect of SIS 2015 is the inclusion of a Market Participants' Survey – a detailed study of the business and behavior of financial intermediaries covering more than 1000 brokers, depository participants, agents of mutual funds, sub-brokers and authorized persons.

The global financial crisis and its effect were felt in India since the last survey (held in 2008-09) and it was imperative for policy makers to understand the change in investor behavior as an effect of it. The detailed main survey has been informed by state-of-the-art research in behavioral finance (the overlap of finance and psychology) to provide insights into not just the actions of investors but also their perceptions which lead to action. While some insights received from the surveys have been expected, others have been surprising. However, that is the purpose of these studies – to gain the insights and to act upon them. For example, SEBI has taken multiple steps to ease the IPO process– an area of apprehension for some investors in SIS 2015 – validating our efforts in that space.

The survey team at SEBI was led by Dr. Sarat Kumar Malik with support from Mr. Prateek. The team at Nielsen, headed by Mr. Tathagata Dasgupta along with his team members, Dr. Akshaya Patro, Mr. Gunjan Rohatgi and Mr. Dipyaman Sanyal (Consultant to Nielsen) did a commendable job of running such a detailed survey

across every corner of the country and then analyzing the data and creating this insightful report.

Mr. Prashant Saran, Whole Time Member, SEBI and Mr. SV Muralidhar Rao, Executive Director, SEBI have provided constant support and encouragement throughout the study. A special word of thanks to Mr. Sudhakar Khairnar and Ms. Suvidha Nagpal for providing assistance to the project. I would like to express appreciation to all the members of the committees who have been associated from the beginning of the project to its finalisation. However, the most important players in this entire process are the financial decision makers in the households who voluntarily spent their time to respond to this questionnaire. Without their support and patience we would not have been able to conduct this extremely important survey.

I hope that the findings of the present study will be useful to SEBI, stakeholders in the securities market, policy makers, members of the academia and the financial sector as a whole.

U.K. Sinha
Chairman, SEBI

01 INTRODUCTION

One of the key mandates of securities markets regulators[1], which extend beyond their supervisory function, is to inspire confidence, strengthen infrastructure and improve participation rates in the securities markets[2]. To widen the reach, bolster awareness of the securities markets and to underline its significance in a country's economic growth, it is vital to re-examine the limiting definition of financial inclusion itself, which has so far centred on bank accounts. Despite the unpredictability commonly associated with stocks and related instruments in comparison to other methods of savings and capital formation (i.e., real estate, gold, savings accounts, post office savings, etc.), risk-adjusted returns from equities tend to outperform other asset classes in the long run[3]. To socialize the gains from corporate profits and mobilize dormant household savings, the government and government-supported bodies need to reach out and educate a wider populace about options available in the securities markets.

Additionally, smoothly functioning securities markets significantly aid economic development and its consequences go far beyond the positive effects seen from an improved banking system alone. According to a recent World Bank policy research paper, "as economies develop, the marginal increase in economic activity associated with an increase in bank development falls, while the marginal boost to economic activity associated with an increase in securities market development rises"[4]. A number of studies and surveys indicate that a very small proportion of Indian population invests in securities market while countries with matured stock markets have participation rates of around 50 percent[5]. To examine, rationalize and potentially bridge this gap, SEBI Investor Survey 2015 (SIS 2015) attempts to not only measure investor behaviour and preferences but also methodically scrutinize non-participation in the security markets.

1.International Organization of Securities Commissions (IOSCO), IOSCO Website: About Us: IOSCO Objectives, last accessed March 20, 2016, https://www.iosco.org/about/?subsection=about_iosco
2.Securities and Exchange Board of India Act, 1992, last accessed November 16, 2015, http://www.sebi.gov.in/cms/sebi_data/attachdocs/1456380272563.pdf
3.Jeremy J. Siegel, Stocks for the Long Run 5/E: The Definitive Guide to Financial Market Returns & Long-Term Investment Strategies, McGraw- Hill Education, 2014
4.Asli Demirguc-Kunt, Erik Feyen and Ross Levine, "The Evolving Importance of Banks and Securities Markets", World Bank, 2011, last accessed November 16, 2015, http://siteresources.worldbank.org/EXTFINANCIALSECTOR/Resources/Banks_and_SecuritiesWP5805.pdf
5. See similar surveys conducted by the Hong Kong Stock Exchange (Retail Investor Survey, 2014) or Gallup US Annual Economic and Financial Survey: Stock Markets (April 2015)

SEBI Investor Survey 2015

To develop and regulate the fast growing securities markets in India, especially following the economic reforms of 1991, the Securities and Exchange Board of India Act, 1992, established the Securities and Exchange Board of India (SEBI) on April 12 of that year. Through comprehensive monitoring, supervision, and policy development, SEBI continued to showcase its keenness to promote and develop the Indian securities markets and protect investors' interest. The primary mandate of SEBI according to its preamble is, "...to protect the interests of investors in securities and to promote the development of, and to regulate the securities market"[6]. Since risk-adjusted returns from equities tend to outperform other asset classes in the long run, participation in securities markets is imperative not only for the development of the economy as a whole but also to socialize the gains from corporate profits. Jeremy Siegel's seminal text on the subject of long- term, risk-adjusted returns of equities markets uses data from the United States (US) to prove that stocks have the highest risk-adjusted returns due to the mean reverting properties of equities returns[7]. In a cross-sectional study of emerging markets, Spierdijk and Umar (2014) also find that domestic investors benefit from stock markets in the long run[8].

Thus, an equally important mandate of SEBI is to ensure efficient functioning & promoting these markets by providing various investible instruments to the existing as well as potential investors.

SEBI Investor Survey (SIS) 2015, conducted by Nielsen India Pvt. Ltd., is the fourth iteration of a periodic SEBI-sponsored investor survey, which primarily focuses on research questions most critical to policy makers. The survey was developed to identify and understand investor perceptions regarding investment choices and savings instruments and to probe further into the decision-making processes of non-investors, particularly by attempting to understand their non-participation in market instruments and their approaches to saving. In addition to a broader coverage in the survey's geographic scope and a substantially larger sample size than the previous survey, SIS 2015 also provides a robust estimation of investors in the country. Although the sample is right- skewed in income to capture more investors, no areas (urban or rural) were dropped following the listings exercise in order to avoid a bias in the estimates of key variables like total investor households or securities markets participation rate.

6. Securities and Exchange Board of India Act, 1992, last accessed December 20, 2016, http://www.sebi.gov.in/cms/sebi_data/attachdocs/1456380272563.pdf,
7. Jeremy J. Siegel, Stocks for the Long Run 5/E: The Definitive Guide to Financial Market Returns & Long-Term Investment Strategies, McGraw-Hill Education, 2014
8. Laura Spierdijk and Zaghum Umar, "Stocks for the Long Run? Evidence from Emerging Markets", Journal of International Money and Finance, Vol. 47, October 2014, pp. 217–238

Since the data requires a significant number of investors to create rigorous analyses and estimates, it was recognized that random sampling would not be effective for this investor-focused survey. However, it was also apparent that ignoring certain States or socio-economic groups would lead to a statistical bias, and the sample would not then be a true visual of the broader population. The methodology is unique and is one of the key strengths of this survey. While details of the sampling techniques are provided in Chapter 3, the breadth of the survey (with over 50,000 responses across all States and Union Territories except Lakshadweep), its additional focus on rural respondents (1/3rd of the sample) and the depth of the questionnaire (from perceptions on risk, returns, and liquidity to actual investment behaviour; from risk mitigating strategies to demographic details) makes this survey distinctive – even in the global arena[9].

Another key element of the report is a detailed survey of market participants, including Depository Participants (DP), Mutual Fund Agents (MFA), Brokers, Authorized Persons (AP) and Sub-Brokers (SB). With falling commissions and tightening margins, higher Internet penetration and online trading, lower volumes in some businesses and larger institutional players entering the market, market participants' businesses have undergone a sea change in the last five years. SIS 2015 is arguably the sole attempt to rationalize the perceptions and sentiments of the many participants in this fast- evolving market.

SIS 2015, while focusing on securities markets, is primarily a survey of retail consumers of investment instruments. Thus, the securities markets expertise of SEBI and the consumer focus of Nielsen have formed a unique and valuable partnership to help create not only a deeper understanding of the choices and the psyche of the Indian investor but also of the potential investors who can but choose not to participate in the markets.

9. See similar surveys conducted by the Hong Kong Stock Exchange (Retail Investor Survey, 2014) or Gallup US Annual Economic and Financial Survey: Stock Markets (April 2015)

Key Objectives

The list below highlights the aspects that are more crucial from a policy design perspective and the key objectives that underline the SIS's questionnaire design rationale and framework, the survey methodology and the comprehensive analysis:

Household Investors

- To understand the socio-economic characteristics of households
- To study the financial savings/investment behaviour of households
- To determine the risk profile of investors and relate it to their investment behaviour
- To estimate the concentration and distribution of household investors in the securities market
- To find out the reasons for non-investment in securities market and also response to equity public issues
- To understand the interface between investors and market participants and the impact of regulatory policies
- To find out the impact of investor education/financial literacy programs on investments, investor grievances and awareness of redressal mechanisms
- To compare the results of the previous survey with the current survey to find out changes in the investor population (growth/decline), investment behaviour/patterns, etc.

Survey of Market Participants

- To understand market participants' responses to dynamic market situations, their perspective on investor awareness and behaviour, penetration of securities market, business environment, views on regulatory aspects, etc.

Design Rationale

While a sizeable portion of the report is designed to collect socio-economic, demographic and investment data, the survey questionnaire's rationale and structure is grounded on the tenets of behavioural finance, a field that enmeshes psychology with traditional efficient market economic theory. An overlap between traditional finance and investor psychology, which is used in both academic and practitioner finance, behavioural finance recognizes that investor sentiment is fraught with heuristics (mental shortcuts) and biases. While conventional financial models expect unbounded rationality in investor conduct, behavioural finance acknowledges that human rationality is constrained by the cognitive inadequacies of the brain[10]. With reference to the current survey, it is crucial to keep in mind that investors may possibly be biased against certain instruments due to their higher perceived risks and on the other hand, may be more tolerant of other instruments simply grounded on random name recognition. To make certain that the outreach programs of government organizations and SEBI are cognizant of these biases and thus, subsequent steps are taken to educate investors in these areas, perceived risks have been analysed in detail. Apart from simply quantifying investor choices, the survey's objective is to understand exactly what underlies the difference between those who do and those who do not invest and additionally, to underline and rationalize survey outcomes that showcase the anomaly between the perceived risk of an instrument and its actual risk.

The SIS report uses data collected from the extensive survey, from multiple economic data sources, and additionally, also makes use of a variety of related academic research to ascertain causal relationships between respondent characteristics and their investment choices and risk perceptions. Data visualization tools (like maps, graphs and plots) and statistical analysis (like correlations, chi-squares and cross-tabulations) are utilized throughout the report to generate insights from the rich dataset collected by the Nielsen team from all 29 States, 5 Union Territories and the National Capital Region.

10. Andrei Shleifer, Inefficient Markets: An Introduction to Behavioral Finance, Clarendon Lecture Series, Oxford University Press, 2000

Box I – Estimating Total Investors in India

SEBI Investor Survey 2015 (SIS 2015) attempts to generate a deep understanding of retail investors and to also gain insight into why so many of those households who can potentially invest in the securities markets, do not. To support this key objective, a random sample would obviously not provide the desired investor and non-investor mix. Thus, the initial listings sample and the final survey sample use a detailed and unique targeted sampling process, which is skewed towards localities with a higher number of demat accounts. This ensures that the survey's sampling technique is exclusive and directed at generating accurate insights. Consequently, incomes in the listings exercise are, on an average, three times the city average and this survey cannot be compared to either earlier investor surveys or with other surveys that use random samples.

As a first step in the SIS data collection effort, a set of 2,04,694 households were listed and basic information about demographics, income, savings and investments were collected. In the second step, a subset of 50,453 amongst these listed households were chosen to conduct the final survey. In light of the statistical law of large numbers, the listings data was used to create an estimate of the total number of investing households in India at the end of the 2015. Using a bootstrapping methodology to project the total investor households using distinct projection values for rural and urban surveys, by state, it was estimated that there were a total of 3.37 crore investor households in India. Of these, 70 percent (2.37 crore) reside in urban areas while the other 1 crore were rural households. Among these, mutual funds were the most popular investment instrument and nearly 66 percent (or 2.2 crore households) were investors. There were an estimated 1.9 crore households which invested in equities and 77 lakh households which invested in bonds (public, private and PSU). Among derivative instruments, there were 30 lakh equity and currency derivatives investors and 21 lakh investors in commodity futures. Amongst the equity investors, about 18 percent (or 33 lakh) had invested in the primary (IPO) markets.

It is obvious that since the last survey was conducted in 2008-09, the effects of the financial crisis have been felt in India and many investors opted to leave the markets in the height of the crisis. However, with a rise in consumer confidence, investor expectations and the indices, the retail investor has returned with percentage figures reaching back to levels seen in the last survey. This is also supported by the SIS data, which observes that 50 percent of the securities markets investors have started investing in the last five years. Additionally, due to a rise in the number of households, the total number of investing household has increased significantly.

While these estimates can throw some light upon the total number of investors, these are approximations from a survey, which uses targeted sampling (essential for the purposes of this survey, as mentioned above) and thus, cannot be considered a perfect representation of ground realities. To answer that question and quantify the exact number of investors in India, SEBI is undertaking a large scale de-duplication of demat accounts and mutual fund folios across depositories, linking these accounts back to the unique PAN numbers of investors. This will allow for a definitive and complete investor count. However, an estimate is also being provided here to provide an indication of the breadth and trends in investing.

Comparison with the Previous Investor Survey

In 2011, the NCAER published the Investor Survey for SEBI, which was conducted in 2008-09. This section compiles some key results from that survey, contrasts those with the findings of the current survey and additionally, highlights the crucial differences between the two in terms of survey, sample and motivation. While a number of key findings are similar between the 2011 and 2015 surveys, there are some crucial differences in investment awareness and behaviour. Using the 2011 survey as a point of reference, the current survey's questionnaire and sampling frame have been redesigned to account for broader objectives that are essential to regulators and policy makers. The objective of SIS 2015 was broader by design and more comprehensive than the previous survey. It was meant to encompass a vast array of investor behaviour and actions (as enumerated above) and additionally include:

- Reasons for non-investment in securities markets.
- Understanding the interface between investors and market participants.
- Finding out the impact of investor education/ financial literacy programs on investments, investor grievances and awareness of redressal mechanisms.

The previous investor survey sampled 38,412 households from 44 cities and 40 villages. The survey encompassed 25 States/Union Territories (UTs) and did not include Jammu & Kashmir, Arunachal Pradesh, Nagaland, Manipur, Mizoram, Tripura, Andaman & Nicobar Islands, Daman and Diu, Dadra and Nagar Haveli and Lakshadweep.

In comparison, the SIS 2015 includes all States and Union Territories of India except Lakshadweep and has a total sample size of 50,453. SIS 2015 covers 488 villages and 74 towns and cities. This has created a more holistic view of the country's investors and also allows for a significantly more robust estimation of the number of investing households.

To help understand and analyse the broader objectives of SIS 2015, the survey methodology used in the current survey was distinct from the previous study (and is unique amongst such studies). SIS 2015 uses a purposive sampling technique based on demat account data. The objective of using such data is to increase the incidence of selecting investors in the total population to get a comprehensive view of their characteristics, behaviour and investment patterns. The previous study used a focused sampling for the listings exercise by selecting blocks within cities/ towns and then used a stratified sampling technique by creating bands of 'investors', 'savers' and 'none' to choose households accordingly for the final survey. Details are provided in Chapter 3 of this survey report. While the previous survey had listed 70,159 households as the sampling population, the SIS 2015 has a listing of 2,04,694 households from across the country. This allows for a broader pool of survey participants to choose from.

In both the earlier and SIS 2015 surveys, there is a vast regional disparity in the proclivity to invest in securities markets. For instance, in the previous survey, 55 percent of investors were from the West zone while in the current survey, 51 percent of investors are from the West.

According to the previous survey, the estimated number of investor households in India was 2.45 crore (about 11 percent of total households). That implied that 92.7 lakh households (or 6 percent) in rural India invest in the securities markets. The 2011 survey stated that, "… after repeated listing in more than 50 villages across the country, it was found that the extent of participation in securities markets was extremely low. Hence it was decided to present the findings of investments and savings separately for rural households based on a carefully selected sample of 40 villages". In contrast, the SIS 2015 data uses a pan-India survey of large rural sample for analysis and estimation. Probability Proportional to Size (PPS) sampling methodology has been used for the rural sampling in the current survey and the villages covered during the survey have not been restricted to those that have a close proximity to

urban clusters. To get a true representation of the rural population, most of the selected villages are far from cities Though, as stated earlier, the estimated number of households may not be comparable across the two surveys but at a broad level, the estimated number of investor households in India as per SIS 2015 are 3.37 crore (2.36 crore urban and 100.3 lakh rural households) as compared to 2.45 crore (1.52 crore urban and 92.7 lakh rural households) estimated in the previous survey.

There are multiple areas where the 2015 survey findings closely align with the 2011 findings. The most important amongst these is the education-investment relationship. According to the 2011 survey, "Education plays a significant role in influencing risk preferences. The risk appetite was the highest among investors with more than 15 years of schooling" and "26 percent of HH (households) with 15 years of educations in NCAER invest in secondary markets". The SIS 2015 data found analogous results with 25 percent of the highest educated group (15+ years of education) invested in securities markets.

In 2011, the preferred mode of investments was mutual funds, followed closely by equities. This pattern still holds true with very few investors engaging in bonds or derivatives in either survey. Additionally, the dependence on traditional media like newspapers and the importance of financial intermediaries has remained consistent despite rising Internet penetration and changes in the brokerage industry.

However, SEBI website, which was not often visited by investors (according to the 2011 survey) is now a key source of information for investors.

Report Structure and Short Summary of Chapters

- Chapter 2 (Indian and Global Economic Backdrop) analyses both local and global external events and their potential implications on investment and savings behaviour. Investor sentiments are inextricably linked to and affected by internal factors, like income, age, occupation, and risk tolerance as well as several wide-ranging external influences. To analyse and rationalize investor sentiment, it is essential to study the market environment (with a special focus on stock markets), economic growth, the condition of businesses, the Indian political and social situation as well as the global market place scenario.

- Chapter 3 (Survey Methodology and Sample Selection) provides details on the survey methodology and sampling techniques. Between September and November 2015, SEBI Investor Survey encompassed a total of 50,453 households across virtually every corner of rural and urban India, the seventh largest country in the world with an area of 32.9 lakh square kilometres and a population of 125 crore. The SIS 2015 includes all 29 States, 5 Union Territories (excluding Lakshadweep) and the National Capital Region of Delhi. This is the first time that a survey of this depth and magnitude has been undertaken in all the North Eastern States of India. This chapter details not just the exact processes involved in covering this vast country and its population but also the methodology utilized to procure a representative sampling of the diverse population.

- Chapter 4 (Urban Households: Investments and Savings Behaviour) is the survey's core, which endeavours to identify and characterize the Indian urban investor – the majority of Indian investors. The primary focus of the analysis is to identify the fundamental choices of investors and their awareness concerning various investment and savings vehicles, financial instruments, investments patterns, household savings and debt; more specifically, the survey probes further to gauge the essential ethos of an investor. To help rationalize the central questions that this survey attempts to answer, the urban investors' responses are analysed in detail.

- Chapter 5 (Rural Savers: An Untapped Investor Base) is a key chapter for policy makers as it provides information and analysis of the rural saver and investor and discusses the key roadblocks that hamper investment in these markets. Despite the fast urbanization in the country, 65 percent of the Indian population lives in villages and yet, investments in market instruments are still relatively rare in these rural markets. Rural respondents constitute nearly 1/3rd of the SIS 2015 sample.

- Chapter 6 (Investor Response to Initial Public Offerings) details one of the key areas of interest not only for SEBI but also for securities markets in general: the response to new public issues – either, Initial Public Offerings (IPO) of equities or New Fund Offerings (NFO) of mutual funds. Since primary markets are the key to liquidity for corporations and a well-functioning primary market provides the grease for a smooth functioning economy, this chapter is grounded on the survey participants' detailed answers concerning their experiences while applying for new issues.

- Chapter 7 (Mutual Funds: Investor Behaviour and Investment Patterns) studies investor behaviour and key developments in the mutual fund (MF) industry. Due to the ease of investing in mutual funds through SIPs (Systematic Investment Plan) along with its diversification benefits, most investors prefer this instrument to equities or bonds. Additionally, the publicity of SIPs and the MF industry over the past ten years has seen an enormous increase in total Assets under Management (AUM) of MFs.

- Chapter 8 (Investors and Market Participants) introduces the various Indian market participants and focuses particularly on the broker-investor relationship. The survey finds that although online trading and investments is gaining popularity, brokers and market participants continue to be the mainstay of the securities market functions. The investor-broker interdependence, especially the particularities of the changing structure of the brokerage business, is discussed in depth.

- Chapter 9 (Household Perceptions of Financial Markets) analyses investors' perceptions vis-à-vis specific investment instruments. The survey reasons that a comparison of perceived and actual risk metrics and especially, the need to bridge the fissures between the two, may help provide guidelines to encourage more participants to enter the securities markets. A decrease in prejudiced risk aversion will certainly increase participation and this, in turn, will enhance liquidity and the possibility of productively utilizing the money 'trapped' in non-investment vehicles (like gold, precious metals, unused land etc.).

- Chapter 10 (Awareness of Regulatory Policies, SEBI and Investor Literacy Programs) focuses on awareness levels of regulatory policies, the various investor literacy programs and specifically, on SEBI's role in the investor community. This analysis not only provides policy makers with a metric to measure the success of past programs but also helps in creating a road map for potential outreach planning.

- Chapter 11 (Geographic Snapshots of Investor Behaviour) slices, dices and analyzes the SIS 2015 data by geographic areas. From regional zones to sets of large cities and states, this chapter covers the disparities in patterns and behavior across geographies to rationalize and understand why some of the wealthier and higher educated groups do not participate in the securities markets.

- Chapter 12 (Market Participants' Survey) is a separate survey on market participants (financial intermediaries) that received 1,016 completed questionnaires from brokers, sub-brokers,

depository participants and authorized persons across the country. This is an extremely valuable resource that helps assess particular market participants, the condition of that business, their perception and take on investor sentiments and also their feedback on policies and taxes. This chapter also allows a comparison between the supply side (the intermediaries) and the demand side (the investors) and clarifies their differing stances on similar questions regarding investment behaviour and perceptions.

02 INDIAN AND GLOBAL ECONOMIC BACKDROP

Investor sentiments are not engendered in isolation. They are inextricably linked to and affected by both internal factors, like income, age, occupation, and risk tolerance as well as several wide-ranging external factors. To analyse and rationalize investor behaviour and sentiment, it is essential to conduct a detailed study of the business environment (with a special focus on stock markets), economic growth, the Indian political and social conditions as well as the global market place scenario. The SIS 2015 household survey transpired between September and November 2015, whereas the survey's last iteration took place in 2008–09 (published in 2011). In the interim five to six years, the stock markets, the condition of the economy, the political scenario and the confidence in securities market amongst the population have altered considerably. To provide a substantial backdrop that accurately senses the nation's pulse, the survey needs to scrupulously consider the potential implications of various external factors on investment and savings.

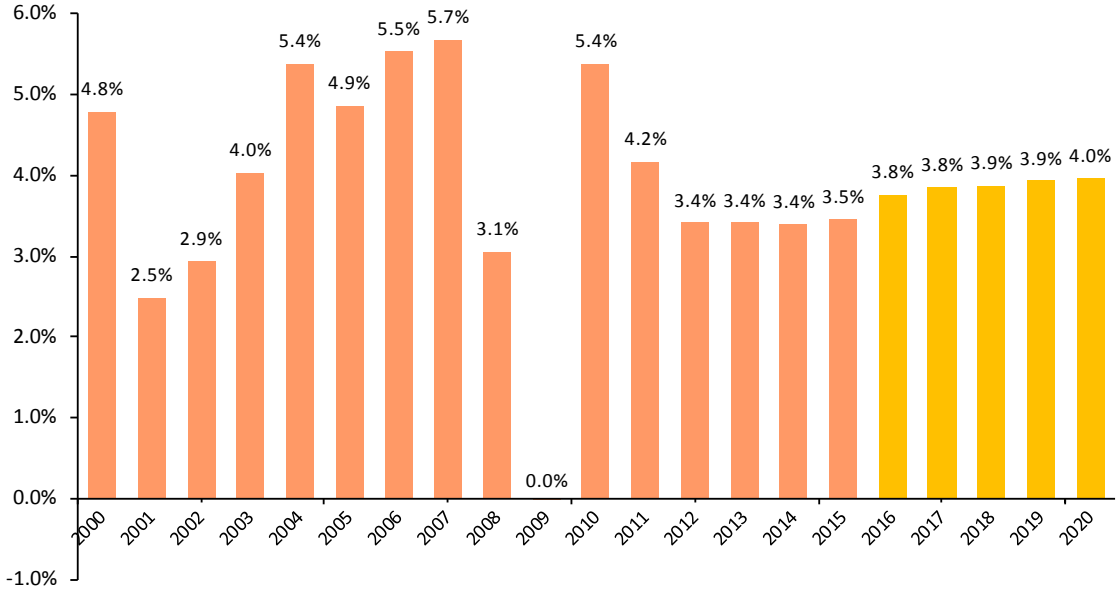
The Global Financial Crisis and its Repercussions

The US economy (the largest economy of the world and the centre of global consumption) is now out of the turmoil observed during and in the aftermath of the 2008 Global Financial Crisis (GFC). For the first time in nearly a decade since the financial turmoil, the US Federal Reserve Bank (Fed) raised its interest rates on 15th December, 2015, to avoid the risk of potentially overheating the economy. The US and other developed markets' Zero Interest Rates Policy (ZIRP) and Quantitative Easing (QE) have been essential to counter the effects of the low growth-low confidence-low inflation-high unemployment cycle in the GFC's wake. These measures created large-scale liquidity in the market and eased the credit flowing into the real economy[11]. As an effect of these policies, unemployment rates in the US are now stabilizing at 5 percent (from a peak of 10 percent in October 2009)[12].

11. International Organization of Securities Commissions (IOSCO) Research Department, "Securities Markets Risk Outlook, 2016", IOSCO, last accessed March 3, 2016, https://www.iosco.org/library/pubdocs/pdf/IOSCOPD527.pdf
12. Bureau of Labor Statistics, "Unemployment Rate", Labor Force Statistics from the Current Population Survey, last accessed January 6, 2016,

Nonetheless, the recovery from the GFC is far more muted than the sharp upturn in the global economy following the last recession of 2000–01 (the dot com bubble and its aftershocks). The global GDP growth rate was 4.8 percent in 2000, which then dropped to 2.5 percent at the height of the dot-com bubble, and then rebounded sharply to 5.4 percent in three years. However, during the GFC, global growth rates went down from 5.7 percent in 2007 to -0.009 percent in 2009 and are yet to reach those levels of growth again. The IMF's growth expectations[13] (as seen in Figure 2.1) show the muted recovery in global growth.

Figure 2.1: Global Real GDP Growth Rates and IMF Forecast



Source: IMF, The Yellow Bars indicates forecast and projections while amber indicate real values.

While it is indisputable that the global economy has a significant effect on the Indian economy and that the country's development agenda may receive some support from global economies in the current and coming year, to sustainably reinvigorate their post-GFC development paths, growth in emerging markets (EM) has to primarily originate from within and not without the economy[14]. Factors like internal consumption and

13. International Monetary Fund, "Gross Domestic Product, Constant Prices, World", World Economic Outlook Database March 2015, last accessed 22 November, 2015, http://www.imf.org/external/pubs/ft/weo/2015/02/weodata/weorept.aspx?pr.x=33&pr.y=9&sy=2000&ey=2020&scsm=1&ssd=1&sort=country&ds=.&br=1&c=001&s=NGDP_RPCH&grp=1&a=1

14. United Nations Economic and Social Commission for Asia Pacific, Reinvigorate Domestic Demand to Revive Growth & Support Sustainable Development, UNESCAP, January 14, 2016, last accessed March 15, 2016, http://www.unescap.org/op-ed/reinvigorate-domestic-demand-revive- growth-support-sustainable-development

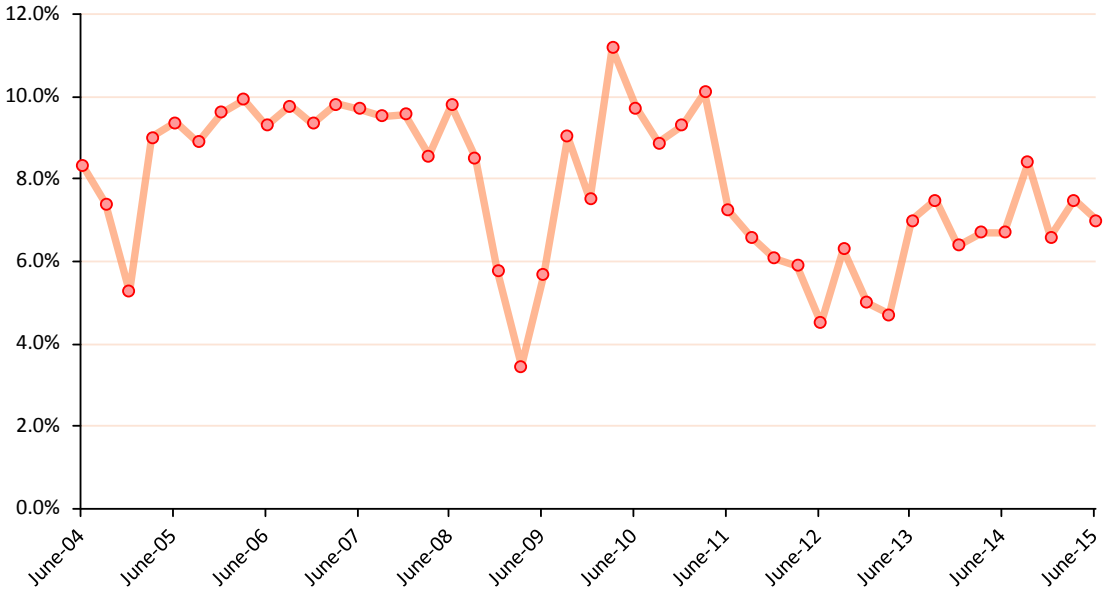
domestic retail investments are major drivers that spur real economic growth. At the same time, consumption and investments are vastly dependent on both the securities markets and investor sentiments. This is commonly known as the "wealth effect" [15] of stock markets, which is not only seen in developed markets like the US but recent research has also found a significant wealth effect in cross-country emerging market studies[16]. The wealth effect from securities markets affects consumption and domestic demand and that, in turn, supports a stable economic growth.Consequently, SIS 2015 attempts to identify and understand investor behaviour and perceptions regarding investment choices and savings instruments in order to probe further into the decision-making processes of non-investors, especially by attempting to understand their non- participation in market instruments and their approaches to saving.

The Current Indian Economic Climate

India is now (December 2015) the fastest growing large economy in the world. The year-over-year quarterly real GDP growth rate is at 7 percent, indicating a moderate recovery in a shaky global economy (Figure 2.2). Subsequent to the rapid decline of growth rates during the GFC, the economy recovered in 2010–11, only to suffer some setbacks from mid-2012 to mid-2014. Over the past year, economic growth has again started gaining some teeth, especially in comparison to the slow growth in the global economy. However, it is far from the heady continuous high growth rates seen between mid 2004 to mid-2009. India's burgeoning middle class[17], a robust consumption expenditure growth (see Figure 2.7), the proposed policy changes and infrastructural investment plans from the government[18] should help it to remain one of the fastest growing global economies in the near future, attracting significant investments from yield-focused investors across the globe.

15. James M. Poterba, "Stock Market Wealth and Consumption", The Journal of Economic Perspectives, Vol. 14, No. 2, Spring 2000, pp. 99–118
16. Tuomas A. Peltonen, Ricardo M. Sousa, and Isabel S. Vansteenkiste, "Wealth Effects in Emerging Market Economies", International Review of Economics & Finance, Vol. 24, October 2012, pp. 155–166
17. Homi J. Kharas, "The Emerging Middle Class in Developing Countries", OECD Development Center Working Paper No. 285, Global Development Outlook, OECD, January 2010, last accessed March 15, 2016
https://www.oecd.org/dev/44457738.pdf
18. Key Features of Budget 2016-2017, Government of India, March 2016, last accessed February 23, 2016, http://indiabudget.nic.in/ub2016- 17/bh/bh1.pdf

Figure 2.2: Quarterly Indian Real GDP Growth Rates



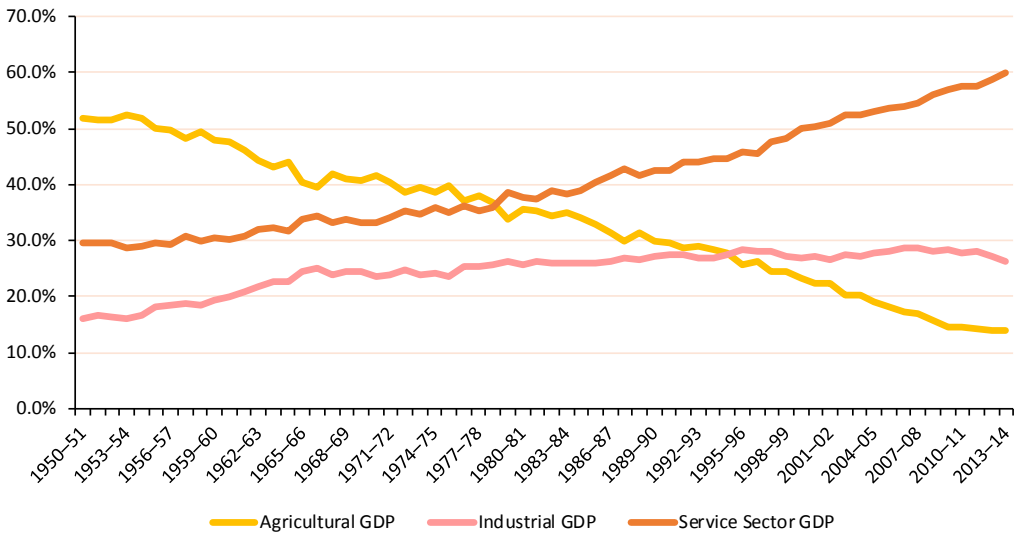
Source: Ministry of Statistics and Programme Implementation (MOSPI)

Indian Financial Markets: Primary Drivers

Urbanization and socio economic growth are two interconnected significant drivers, which are expected to drive investment growth and an increased penetration in securities markets. According to the SIS data (see Chapter 4 and Chapter 5), households with similar education and income (the two primary drivers of socioeconomic growth) in urban areas tend to invest significantly more in the markets than those in rural areas. 7.1 crore people were added to India's cities between 2001 and 2011 and the urban population rose from 27.8 percent to 30 percent of the total population. By 2026, the urban population is expected to increase to over 50 crore people, which will constitute 38 percent

of the total Indian population. In conjunction with this rapid urbanization, the GDP growth rate in India has strong sectoral differences, some of which may support the development and growth of stock markets. Figure 2.3 corroborates the sectoral evolution in the economy since Independence. The service sector has doubled (as a percentage of GDP) from less than 30 percent of GDP (constant prices) in 1950-51 to nearly 60 percent in 2013-14. The related concepts of urbanization and service sector growth in the economy bode well for broader participation in the securities markets. This, in turn, is an essential component for financial stability and economic growth in emerging markets. According to the IMF's analysis regarding emerging markets[19], "Financial development increases a country's resilience and boosts economic growth. It mobilizes savings, promotes information sharing, improves resource allocation, and facilitates diversification and management of risk. It also promotes financial stability to the extent that deep and liquid financial systems with diverse instruments help dampen the impact of shocks." Policy makers and governments need to be cognizant of this essential facet in a country's development paradigm as they create their roadmaps for economic growth.

Figure 2.3: Sectoral Distributions of Indian Economy as a Percentage of GDP



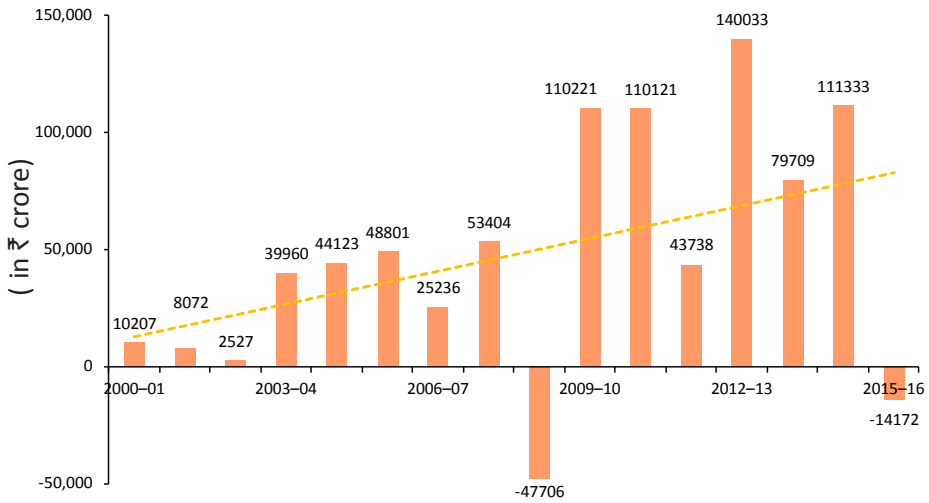
Source: MOSPI

19. IMF Staff Discussion Note, Rethinking Financial Deepening: Stability and Growth in Emerging Markets, May 2015, last accessed December 2, 2015, https://www.imf.org/external/pubs/ft/sdn/2015/sdn1508.pdf

Indian and Global Stock Markets: A Comparative Evaluation

The Indian equity market has grown in size and value since the economic liberalization in 1991. Despite the post-GFC muted global growth, there has been an increasing interest in the stock markets, both from retail investors looking for yields and companies looking to raise capital. As the economic slowdown in China has compelled most global central banks to keep interest rates artificially low, commodity prices have been plummeting. Thus, yield-chasing investors (both retail and institutional) have started moving into equity markets (including emerging economies), fuelling a sharp upturn in the securities markets. The S&P 500 is up more than 200 percent since its 9th March, 2009 lows while the BSE Sensex is up 220 percent in the same time period (as of 31st December, 2015). According to data from the National Securities Depository Limited (NSDL), Foreign Portfolio Investors (FPI)/Foreign Institutional Investors (FII) have invested ₹7,55,400 crore since 2000–01 and ₹5,80,983 crore in the post-GFC period (since 2009–10), and this number increases by about 50 percent when debt is included. Despite negative growth in 2008–09 at the peak of the GFC and in the last fiscal year, the trend line in Figure 2.4 shows the steady and significant rise in foreign investments.

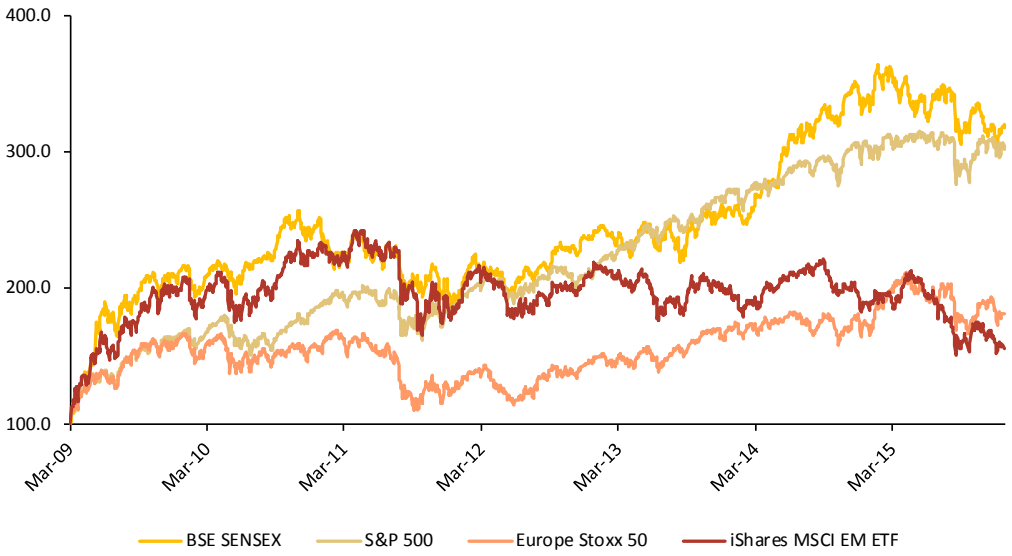
Figure 2.4: Foreign Portfolio Investments/Foreign Institutional Investments (FII) in Indian Equities Market (in ₹ crore)



Source: National Securities Depository Limited (NSDL)

An analysis of S&P BSE Sensex's long-term data provides a persuasive rationale that can help clarify India's investment success story (as observed in Figure 2.5), especially among other emerging economies. The 1991 financial liberalization and the ensuing development of an open market-based economy led to widespread growth in all sectors of the economy. In fifteen years, the Sensex increased by 386 percent—from 5,205 in early January 2000 to 26,117 on December 31st, 2015—despite the largest global financial crisis and a correction in the current year. Correspondingly, the MSCI Emerging Markets Index (a broad measure of performance for EM equities) has also moved up 178 percent. On the other hand, developed markets like the US or Europe have significantly underperformed emerging economies during this phase. For example, the US' Dow Jones Industrial Average is up 60 percent while the Stocks 50 Index for Europe is down 31 percent in the same time period.

Figure 2.5: Comparative Performance of Indian and Global Stock Market Indices



Source: Bloomberg

In spite of this documented long-term positive growth, which reflects fundamental economic growth, short-term movements in the equities market are driven by investor sentiments or in Shleifer and Summers' words: "noise traders" (1990). In the long run, arbitrageurs stabilize market inefficiencies[20].

Since this survey was last conducted in 2008–09 (published in 2011), the Sensex has moved up more than 44 percent in value (Figure 2.5) while developed markets have significantly outperformed India or the EM Indices. This is primarily due to the effects of the Global Financial Crisis (GFC) of 2008–10. During this time period, EM stocks (and economies) did not face the complete rout seen by US or European markets. The recent short-term performance of the Indian markets, which sometimes tends to have an outsized effect on survey responses due to the salience of immediate events, has been bleak. The Sensex was down 6.8 percent in 2015, which might have affected the answers of some respondents of SIS 2015.

20. Andrei Shleifer and Lawrence H. Summers, "The Noise Trader Approach to Finance", The Journal of Economic Perspectives, Vol. 4, No. 2 (Spring, 1990), pp. 19–33

The Sentiment-Stock Market-Real Economy Relationship

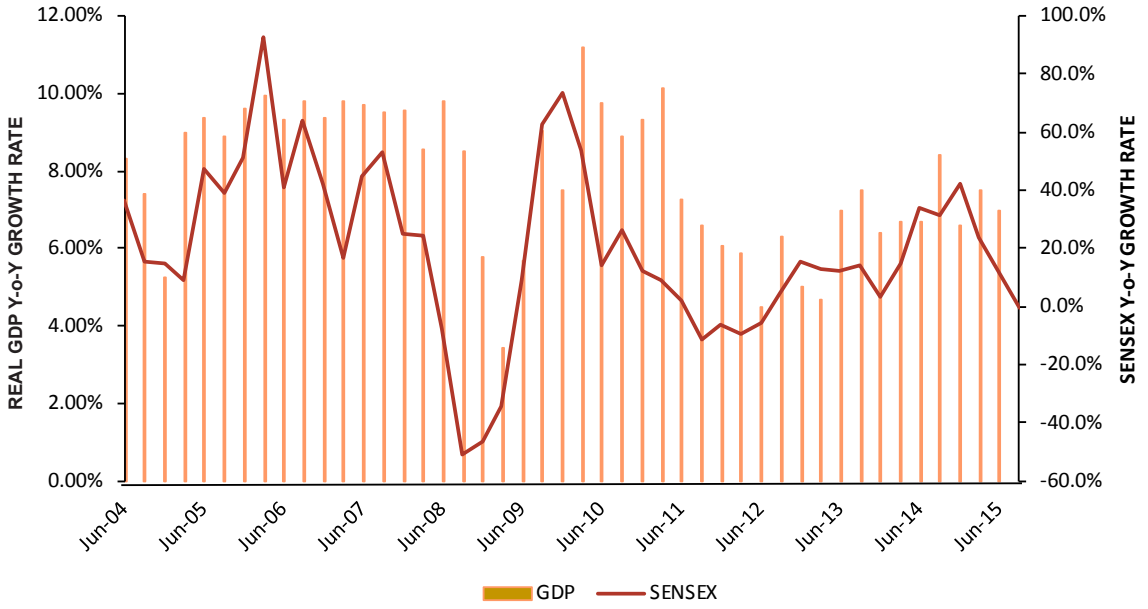
Significant component of the SIS 2015 is to collect and analyse data on investor perceptions and sentiments. To gauge the relationship between stock markets and economic growth, especially whether a growth in stock markets directly translates to a growth in the economy and to figure out whether sentiments and confidence correspondingly leads to a growth of the markets or the economy, the correlation between a broad equities market index (in this case, the Sensex) and the real GDP growth of the economy is essential.

US Federal Reserve Bank's Maria Ward Otoo[21] attempts to answer a more profound chicken-egg question vis-à-vis the relation between markets and growth. Her paper's abstract asks a crucial question: "Does an increase in stock prices raise aggregate sentiment because people are wealthier or because they use movements in stock prices as an indicator of future economic activity and potential labour income growth [21]?" While Otoo eventually concludes that a rise in stock prices leads to the well-documented "wealth effect" amongst investors, she also finds that people use equity price movements as a leading indicator of economic and wage growth.

Figure 2.6 establishes that benchmark index Sensex and GDP are positively correlated and index performance is used an indicator to guage the real GDP growth rates. This is a global phenomenon that is not limited to the Indian scenario. Stock markets' performance is also a crucial component in the Conference Board Leading Indicators series[22], which is used by economists and securities markets professionals across the globe.

21. Maria Ward Otoo, Consumer Sentiment and the Stock Market, Board of Governors of the Federal Reserve System, November 1999, last accessed March 16, 2016, https://www.federalreserve.gov/pubs/feds/1999/199960/199960pap.pdf
22. The Conference Board, "Global Business Cycle Indicators", last accessed March 20, 2016, https://www.conference-board.org/data/bci.cfm

Figure 2.6: The Sensex-Real GDP Relationship

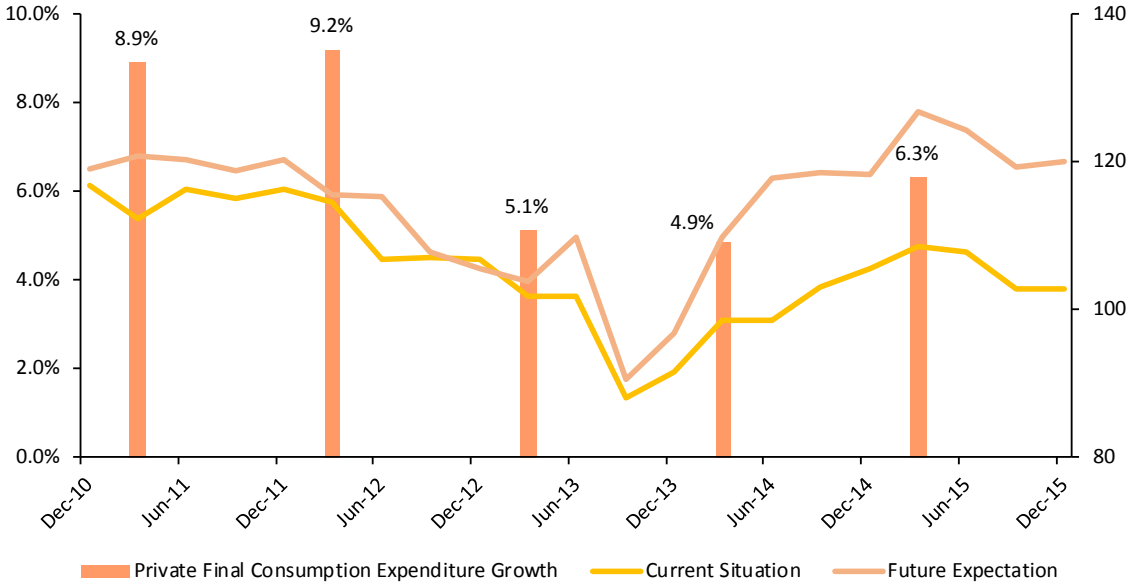


Source: MOSPI, Bloomberg

Although Figure 2.6 confirms the relationship between stock markets (which is often driven by sentiments and expectations) and the real economy, it does not verify the direct effect of sentiments on the real economy. On the other hand, Figure 2.7 uses data from the Consumer Confidence Index series (current and future expectations series) from the Reserve Bank of India (RBI) Surveys and data on growth of personal consumption expenditure of Indian households to showcase the effects of sentiment on actual consumption expenditure.

According to Figure 2.7, a deteriorating confidence in 2012 led to significantly lower growth in personal consumption expenditure in that year whereas a rise in confidence in 2013 was visible in the actual consumption data of the same year. Looking at 2014's data, it is obvious that since the current and future expectations from the economy are on the rise, the growth rates in India reflecting this confidence are on the upswing too (7 percent in the last quarter).

Figure 2.7: Consumer Confidence and Personal Consumption Expenditure



Source: RBI Consumer Confidence Survey, MOSPI

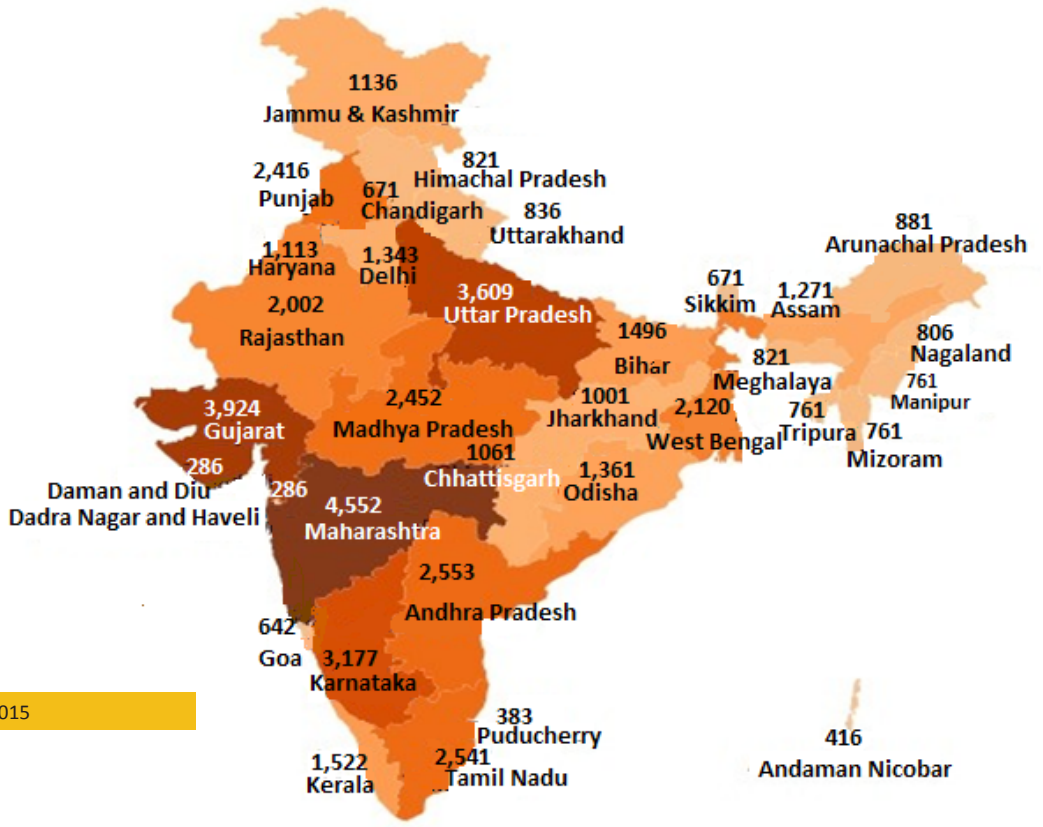
From King and Levine's (1993)[23] seminal paper to the IMF's[24] recent, extensive research, the relationship between the development of financial systems and its effect on economic growth are gradually becoming recognized by academic researchers and policy makers across the globe. The vast research on behavioural economics (for which the psychologist Daniel Kahneman won the Nobel Memorial Prize in Economics) unmistakably demonstrates that individual psychology (driven habitually by its biases and mental shortcuts) primarily drives the growth of securities markets[25]. Thus, it is imperative for regulators and governments to initiate measures for deepning and broadening of the securities market which will contribute to the economic growth.

23. Robert G. King and Ross Levine, "Finance and Growth: Schumpeter Might Be Right", Quarterly Journal of Economics, 1993, Vol. 108, Issue 3, pp. 717–737
24. IMF Staff Discussion Note, Rethinking Financial Deepening: Stability and Growth in Emerging Markets, May 2015, last accessed December 20, 2015, https://www.imf.org/external/pubs/ft/sdn/2015/sdn1508.pdf
25. Daniel Kahneman, Maps Of Bounded Rationality: A Perspective On Intuitive Judgment And Choice, Prize Lecture, December 8, 2002, last accessed December 31, 2015, http://www.nobelprize.org/nobel_prizes/economic-sciences/laureates/2002/kahnemann-lecture.pdf

03 SURVEY METHODOLOGY AND SAMPLE SELECTION

The survey manages to encompass nearly every corner of India, the seventh largest country in the world with an area of 32.9 lakh square kilometres and a population of 125 crore. Figure 3.1 demonstrates the breadth of the SIS 2015. The scale is significantly larger than the previous SEBI-sponsored investor survey, which was held in 25 States and Union Territories (excluding Jammu & Kashmir, Arunachal Pradesh, Nagaland, Manipur, Mizoram, Tripura, Andaman & Nicobar Islands, Daman and Diu, Dadra and Nagar Haveli and Lakshadweep). All 29 states, 5 Union Territories (excluding Lakshadweep) and the National Capital Region of Delhi are included in the SIS 2015 and this is the first time that a survey of this depth and magnitude has been undertaken in all the North-Eastern states of India.

Figure 3.1: Indian States and Survey Responses



Darker Shade indicates higher sample size while lighter shade indicates smaller sample sizes.

Source: SIS 2015

Note on the Survey Process

Grounded on the key objectives of the survey, the SIS 2015 contains two types of questionnaires. The operational methodology followed was:

- More than 2 lakh (2,04,694) households across urban and rural India responded to the first questionnaire: the households listing exercise. This survey primarily concentrates on demographic and basic household investment information profiles that help create the foundation list and thus, a survey 'population'. The sample is then selected from this population.

- Over 50, 000 (50,453) Indian households, Including 36,756 urban and 13,697 rural households, were then randomly identified to participate in the main survey, which subsequently formed the main survey's bedrock. It contains comprehensive information on household investments, awareness of investment options, investments tenures, expected returns, risk-taking capacity and other such minutiae. Furthermore, to know the investors' perception and regulator's role, the respondents were asked questions about their level of awreness and understanding of SEBI regulations related to IPOs, mutual funds etc.
- The listing exercise used Paper and Pencil Interviews (PAPI), whereas the main survey made use of a tablet with Computer Assisted Personal Interviews (CAPI). It is essential to keep in mind that the survey's sampling plan is specifically designed to enable the selection of a larger pool of investors so that the sample size is sizeable enough to create robust estimations of investment patterns and perceptions. This survey's sampling methodology is unique since it is skewed towards amassing a broader investor population data. The primary financial decision maker of the household answered the survey questions.

Executives and consultants at Nielsen in co- ordination with SEBI have developed both the questionnaires. Subsequent to SEBI's final approval, the pilot was initiated. In order to avoid translation losses as much as possible, English and Hindi were the primary languages used. However, to ensure easier accessibility that would help widen the survey's scope, the main survey

application was made available in multiple languages.

SEBI officials provided technical briefings on investment terminologies and conferred with the field survey teams at various locations including Delhi, Mumbai, and Bangalore. Following these briefings, the pilot was conducted in Gurgaon and Jaipur to test the flow of questions, the questionnaire application on the tablets, the skip patterns as well as the enumerators' skill in uploading the data on the server.

In mid-August, both the tablet-aided main survey demo as well as the main survey sampling from the listing population was complete. Initially, the survey was launched in Northern and Western India and subsequently, in Bangalore and the rest of Southern India. In mid-September, it commenced in Eastern India.

The Market Participants' survey was separately conducted online. A total of 1,016 market participants, such as brokers, sub-brokers, mutual funds agents and depository participants completed the survey questionnaire.

Note on Sample Design

To ensure that data from a sufficient number of investing households was captured, a mixed sampling method was proposed in which certain cities and localities with higher income levels were given a greater weightage. Similarly, a greater weightage was given to urban households that were likely to have a higher proportion of investors. Additionally, to achieve a robust estimate of the rural population across states, the sample was spread across rural and urban areas in the ratio of 30:70.

The survey adopted a three-stage stratified sample design in which the first two stages used a readymade frame while the third one made use of a sampling frame. For the rural sample selection, districts, villages and households formed the first, second and third stages of sampling, respectively. For the urban sample selection, cities/towns, urban blocks and households were the three stages. Within each state and UT, rural and urban sampling was independently carried out.

Sampling Frame: The rural survey-sampling frame utilized the 2011 census districts and villages list while the 2011 census cities/towns list was used for the urban survey sampling. In the absence of a definitive list of

households (sampling frame), information on various auxiliary variables was collected via specially designed listing pro forma that listed households in the selected villages and urban blocks. For larger villages/urban blocks, a proportion of households were listed based on 'sampling fraction'.

Sample size: The survey covers a total of 50,453 households. The rural sampling encompasses about 27 percent, i.e., 13,697 households spread across 488 villages in 164 districts while the urban sampling comprises 36,756 households across 1,839 pin code areas in 74 cities and towns

Rural Sampling

Stage 1: Selection of Districts

Within each state, 25 percent of the districts were selected. To select these specific districts, the housing listings data from the 2011 census was used as a base to create an economic development index. The key markers used to construct this index were assets ownership and households possessing bank accounts. To ensure a fair representation and yet ensure a skew towards higher income districts, the index's average value was used as a benchmark and 70 percent of the proposed sample districts above the State average and 30 percent of the proposed sample districts below the State average were then selected.

Stage 2: Selection of Villages

PPS sampling helped select three villages per district in each large state and two villages per district in each of the smaller states. After arranging the villages in ascending order of population, the required number of villages was selected.

Stage 3: Selection of Households

Listing Exercise and Sampling Frame Construction:

In each selected village, the listing required approximately 150 households. Hence, 457 villages generated data from 68,663 households.

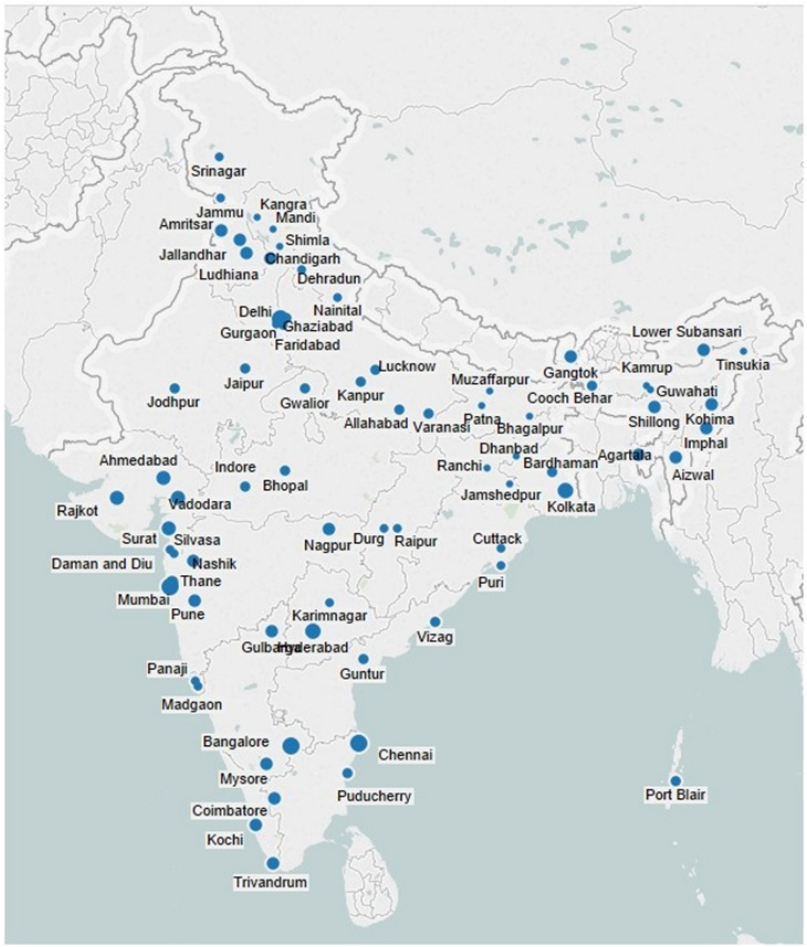
Selection of Households:

Since the listing frame required 30 households from each village, a 68,663 households sampling frame generated 13,697 households' data.

Urban Sampling

SIS 2015 includes sentiment and behaviour data from all of the top-50 cities of India (by population) and also encompasses 24 additional cities. The scale of the circles in figure 3.2 denotes the number of participants from that city.

Figure 3.2: SIS 2015: Urban Coverage



Source: SIS 2015

Larger circle size indicates higher sample size while smaller circle size indicates smaller sample sizes.

Stage 1: Selection of Towns

Using active demat accounts data, 1 to 5 towns were chosen from each of the 35 States/UTs. In each State, towns were then arranged in descending order according to the number of active demat accounts. All towns that contributed to create a sum total of 50–60 percent demat accounts in the State have been included in the survey. In smaller States, a single town may alone contribute 50–60 percent (or more) demat accounts while in large States, about 4 to 5 Cities accounted for 50–60 percent of the demat accounts.

Stage 2: Selection of Pin Code Areas

From each city/town, 20 pin code areas with the maximum concentration of demat accounts and 5 pin code areas with a low concentration of demat accounts were chosen.

Stage 3: Selection of Households

Listing Exercise and Sampling Frame Construction:

Each pin code area was divided into blocks /clusters comprising of 100 to 125 households. The survey team then identified the block likely to have the maximum concentration of investors. Within the selected block/ cluster, about 75 households were then chosen.

Selection of Households:

From each of the above blocks, 20 households were selected at random. Following the urban sampling design, a 1,36,031 households sampling frame generated 36,756 households' data.

Table 3.1 displays state-level data on the rural and urban survey including data on number of districts, sample districts and villages, and households' listings and sample data.

Table 3.1: All India State-Level Rural and Urban Listings and Samples

State Code	No of State and UTs	RURAL					URBAN					ALL INDIA	
		No. of Districts	Sample Districts	Sample Villages	Listed Households	Sample Households	No. of Towns	Sample Towns	Pin-Code Area	Listed Households	Sample Households	Listed Households	Sample Households
1	Jammu & Kashmir	22	6	17	2475	495	132	2	50	3750	641	6225	1136
2	Himachal Pradesh	12	3	6	900	180	61	3	75	5625	641	6525	821
3	Punjab	22	6	17	2475	495	236	3	75	5625	1922	8100	2417
4	Chandigarh	1	1	1	150	30	7	1	25	1875	641	2025	671
5	Uttrakhand	13	3	7	975	195	121	2	50	3750	641	4725	836
6	Haryana	21	5	16	2363	473	165	2	50	3750	641	6113	1114
7	Delhi	11	3	6	825	165	145	1	25	1875	1179	2700	1344
8	Rajasthan	33	8	24	3600	720	320	3	75	5625	1282	9225	2002
9	Uttar Pradesh	75	19	56	8438	1688	937	5	125	9375	1922	17813	3610
10	Bihar	38	10	29	4275	855	203	3	75	5625	641	9900	1496
11	Sikkim	4	1	1	150	30	9	1	25	1875	641	2025	671
12	Arunachal Pradesh	17	4	8	1200	240	27	1	25	1875	641	3075	881
13	Nagaland	11	3	6	825	165	26	1	25	1875	641	2700	806
14	Manipur	9	2	4	600	120	58	1	25	1875	641	2475	761
15	Mizoram	8	2	4	600	120	23	1	25	1875	641	2475	761
16	Tripura	8	2	4	600	120	42	1	25	1875	641	2475	761
17	Meghalaya	11	3	6	900	180	22	1	25	1875	641	2775	821
18	Assam	27	7	21	3150	630	226	3	75	5625	641	8775	1271
19	West Bengal	19	5	10	1500	300	921	3	75	5625	1820	7125	2120
20	Jharkhand	24	6	12	1800	360	229	3	75	5625	641	7425	1001
21	Orissa	30	8	24	3600	720	238	2	50	3750	641	7350	1361
22	Chhattisgarh	27	7	14	2100	420	205	2	50	3750	641	5850	1061
23	Madhya Pradesh	51	13	39	5850	1170	509	3	75	5625	1282	11475	2452
24	Gujarat	33	8	24	3600	720	385	4	100	7500	3204	11100	3924
25	Daman & Diu	2	1	1	150	30	8	1	25	1875	256	2025	286
26	Dadra and Nagar Haveli	1	1	1	150	30	6	1	25	1875	256	2025	286
27	Maharashtra	36	9	27	4050	810	537	5	125	9375	3742	13425	4552
28	Andhra Pradesh	13	3	10	1463	293	240	3	75	5625	1820	7088	2113
29	Karnataka	30	8	24	3600	720	371	3	75	5625	2461	9225	3181
30	Goa	2	1	1	150	30	71	2	50	3750	641	3900	671
31	Kerala	14	4	8	1200	240	532	2	50	3750	1282	4950	1522
32	Tamil Nadu	32	8	24	3600	720	1109	2	50	3750	1820	7350	2540
33	Pondicherry	4	1	1	150	30	11	1	14	1031	353	1181	383
34	Andaman and Nicobar	3	1	1	150	30	5	1	25	1875	384	2025	414
35	Telengana	10	3	6	900	180	248	1	25	1875	256	2775	436
ALL INDIA		674	175	460	68514	13704	8385	74	1839	137906	36779	206420	50483
Achieved Sample		674	169	457	68513	13703	8385	73	1839	136031	36779	204544	50482

Table 3.2 drills down further to the city level for the urban survey, which constitutes more than 70 percent of the data.

Table 3.2: All India City-Level Sample Size Data

State/City	Coverage	State/City	Coverage	State/City	Coverage
Andaman Nicobar	**384**	**Jharkhand**	**641**	**Rajasthan**	**1282**
Port Blair	384	Dhanbad	213	Jaipur	428
Andhra Pradesh	**854**	Jamshedpur	214	Jodhpur	427
Guntur	427	Ranchi	214	Udaipur	427
Vizag	427	**Karnataka**	**2463**	**Sikkim**	**641**
Arunachal Pradesh	**641**	Bangalore	1179	Gangtok	641
Lower Subansari	641	Gulbarga	641	**Tamil Nadu**	**1825**
Assam	**641**	Mysore	643	Chennai	1183
Guwahati	214	**Kerala**	**1282**	Coimbatore	642
Kamrup	214	Kochi	641	**Telangana**	**1225**
Tinsukia	213	Trivandrum	641	Hyderabad	967
Bihar	**641**	**Madhya Pradesh**	**1282**	Karimnagar	258
Bhagalpur	214	Bhopal	428	**Tripura**	**641**
Muzaffarpur	213	Gwalior	427	Agartala	641
Patna	214	Indore	427	**Uttar Pradesh**	**1921**
Chandigarh	**641**	**Maharashtra**	**3742**	Allahabad	384
Chandigarh	641	Mumbai	1178	Ghaziabad	385
Chhattisgarh	**641**	Nagpur	641	Kanpur	384
Durg	320	Nashik	641	Lucknow	384
Raipur	321	Pune	641	Varanasi	384
Delhi	**1178**	Thane	641	**Uttarakhand**	**641**
Delhi	1178	**Manipur**	**641**	Dehradun	321
Goa	**612**	Imphal	641	Nainital	320
Madgaon	306	**Meghalaya**	**641**	**West Bengal**	**1820**
Panaji	306	Shillong	641	Bardhaman	427
Gujarat	**3204**	**Mizoram**	**641**	Cooch Behar	427
Ahmedabad	801	Aizwal	641	Kolkata	966
Rajkot	801	**Nagaland**	**641**	**Daman and Diu**	**256**
Surat	801	Kohima	641	Daman and Diu	256
Vadodara	801	**Odisha**	**641**	**Dadra and Nagar Haveli**	**256**
Haryana	**640**	Cuttack	320	Silvasa	256
Faridabad	320	Puri	321	**Jammu and Kashmir**	**641**
Gurgaon	320	**Puducherry**	**353**	Jammu	321
Himachal Pradesh	**641**	Puducherry	353	Srinagar	320
Kangra	213	**Punjab**	**1921**		
Mandi	214	Amritsar	640		
Shimla	214	Jallandhar	641		
		Ludhiana	640		

Source: All urban data, SIS 2015

Market Participants' Survey

Over the past few years, there has been a marked change in the business of Market Participants. A large number of brokers and sub-brokers have shut down in a short time frame. In contrast, a large number of Authorized Persons (AP) have registered in the same period, arguably taking over some of the roles of the sub-broker. As the regulator of securities markets, it is imperative that SEBI attempts to understand in detail the reason for the changes in the industry. Additionally, market participants play a crucial role in bringing new investors into the securities market, which SEBI encourages. To capture insights from the supply side, market participants are included in a separate survey. All groups of financial intermediaries including Sub-Brokers, Mutual Funds Agents, Brokers, Depository Participants and Authorized Persons responded to the survey and provided some key insights.

Sample Size Determination

A sample size of 1,000 provides robust estimates at 95 percent confidence level (CL) with 2.8 percent error. The sample size has been calculated using the formula n = p (1-p) z2/e2, where p is the proportion of the occurrence of variable of interest (considered as 0.5), z is the alpha value of level of significance at 95 percent confidence level (1.96) and e is the level of error (.02). Using the above formula, a sample of 1,000 provides estimates at 95 percent CL with 2.8 percent error. Since online surveys have a much lower 'hit rate' than pen and paper or traditional survey methods, 5,000 e-mails were sent to allow for an 80 percent failure rate.

Table 3.3: Sample Size Target Distribution

Category	Total Population	Sample Proportion	Sample Size (Email)
Sub-Brokers	65535	32.2%	1611
Mutual Funds Agents	53785	26.4%	1322
Brokers	10023	4.9%	246
DPs	850	0.4%	21
Authorized Persons	73487	36.1%	1807
Total	203385	100.0%	5000

Source: Market Participants Survey, SIS 2015

Stage 1 – Distribution of Sample across Target Groups

The 5,000 e-mails were targeted to various financial intermediaries based on PPS sampling guidelines.

Stage 2 – Sample Selection

For each of the categories, the sample was selected using Systematic Sampling. The financial intermediary Population was divided by the required sample size to get the sampling interval (I). The target group was sorted alphabetically after selecting the respondents by their valid e-mail IDs. The first sample was selected using a random number(R) within the sampling interval. The corresponding samples were selected by adding the sampling Interval I with the Random number … R + I, R + 2I, R + 3I…. till the required sample was achieved. The sampling interval was 41 for all the categories.

Table 3.4: Sample Selection and Sampling Distribution

Category	Total Population	Sample Proportion	Sample Size	Sampling Interval
Sub-Brokers	65535	32.2%	1611	41
MFAs	53785	26.4%	1322	41
Brokers	10023	4.9%	246	41
DPs	850	0.4%	21	41
Authorized Persons	73487	36.1%	1807	41
Total	203385	100.0%	5000	

Source: Market Participants Survey, SIS 2015

The actual sample size achieved is 1,016, which will provide robust estimates at 95 percent CL with about 2.89 percent error level. The distribution between the types of financial intermediaries in this sample is shown in Table 3.5.

Table 3.5: Distribution of Actual Sample

Category	Achieved Sample
Sub-Brokers	311
Mutual Fund Agents	210
Brokers	100
DPs	90
Authorized Persons	305
Total	1016

Source: Market Participants Survey, SIS 2015

Chapter 12 analyses the data provided by the Market Participants' survey and provides not only details about the business of financial intermediaries but also a distinct perspective of the markets and the retail investor's behaviour.

The Listings Exercise, the Final Survey and the Market Participants' Survey together provides a vast trove of information on the Indian retail investor and the securities market, which is analysed in the rest of this survey report. The uniqueness and robust statistical basis of the sampling is the core of this analysis. The data from the listings exercise is additionally used to estimate the total number of investors based on a bootstrapping methodology, using the urban and rural data separately at the state level (See Box I Page - 6).

04 URBAN HOUSEHOLDS: INVESTMENTS AND SAVINGS BEHAVIOUR

KEY FINDINGS

- **Household awareness of savings schemes is significantly higher than a cognizance of investment instruments.**
- **Primary motivation for investing is capital gains, closely followed by lifestyle improvement plans.**
- **About 15 Percent of survey respondents participate in securities markets.**
- **Middle-income groups save more as a percentage of their annual income than the highest income groups.**
- **Clear inverse linear relationship between income and debt levels;that is, as income levels increase, debt (as percentage of income) falls.**
- **The SIS data finds that even among households that invest, it is education and occupation and not factors such as age, household size or marital status that are primary drivers.**
- **Successful outreach efforts have created improved awareness and thus, most investors (66 Percent) invest in mutual funds rather than equities (55 Percent).**
- **There is a direct linear correlation between higher education levels and superior porfolio diversification**

Chapter Rationale

With a savings rate of 31 percent (savings as percentage of GDP), the 2014 World Bank data[26] situates India among the top-20 saver nations in the world. However, most of these savings accumulate in bank deposits, physical assets and currency. According to the "Changes in Financial Assets/Liabilities of the Household Sector" data from the Handbook of Statistics on Indian Economy 2014–15 of the Reserve Bank of India (RBI)[27], investments in shares (including mutual funds) and debentures is ₹57,000 crore for that year, which is 4.6 percent of all household asset growth. While this is a sharp increase from ₹32,300 crore, which is 2.5 percent of all household asset growth from the previous year, it still remains at muted levels. Supporting this RBI finding, the SIS data also discovers that even though just 15 percent of the survey respondents are investors, household awareness of savings schemes is significantly higher than a cognizance of investment instruments. A detailed analysis of the SIS data shows that the primary motivation for investing is capital gains, closely followed by lifestyle improvement plans and that, surprisingly, middle income groups save more as a percentage of their annual income than the highest income groups in the survey; thus, creating a non-linear relationship between savings and income. Conversely, on the debt side, there is a clear inverse linear relationship between income and debt levels. In spite of new sources of credit availability (like credit cards) and an easier access to traditional loans (like personal, car and student loans or mortgages),wealthier households have lower debt. Probing further into investment instruments preferences, the SIS data shows that there is no relationship between household income and the choice of investments instruments like equity or mutual funds; however, lower-income groups tend to invest more in debt instruments, which are low risk.

Furthermore, the SIS data finds that it is education and occupation and not factors such as age, household size or marital status that are primary drivers of investment. It seems that the Government of India (GoI) and SEBI's successful outreach efforts have also created improved awareness for certain instruments (like mutual funds) and consequently, most investors (66 percent) invest in mutual funds that are diversified and thus, safer and more reliable than equities (55 percent). In fact, there is a direct linear correlation between higher education levels and superior portfolio diversification.

26. World Bank, Data: Gross Savings (% of GDP), Washington DC: World Bank, last accessed 30 December, 2015, http://data.worldbank.org/indicator/NY.GNS.ICTR.ZS
27. Reserve Bank of India, Table 12: Changes in Financial Assets/ Liabilities of the Household Sector (At Current Prices), New Delhi: Reserve Bank of India, 16 September, 2015, last accessed 30 December, 2015, https://www.rbi.org.in/scripts/PublicationsView.aspx?id=16453

Introduction

The SIS 2015 has a forward-looking agenda that focuses on investor sentiments and perceptions and, at the same time, meticulously records data on investment patterns and behaviour. Comparably, to understand the investment and savings behaviour of Indian households, the National Statistical Survey Organization (NSSO) has been conducting the All India Debt and Investment Survey (AIDIS); the key findings from the latest (70th) round was published in December 2014[28]. Nevertheless, the NSSO survey's coverage, while analogous to the current survey, does not aim to generate a profound understanding of investor attitude– it is primarily a data collection tool.

Investments and Savings: Awareness and Preferences

While a significant portion of this survey focuses primarily on investors, the current section attempts to analyse the awareness of financial and non- financial instruments – both for savings and investments. Investors are survey respondents who have participated in the securities markets (namely, in Mutual Funds, Equities, Derivatives, Debentures/Bonds or Commodity Futures). Of the SIS's total 36,756 urban sample size, 14.57 percent (5,356) are investors. Table 4.1 provides a list of all the investment and savings instruments that respondents were specifically asked about in the survey.

Table 4.1: List of instruments provided to Survey Respondents

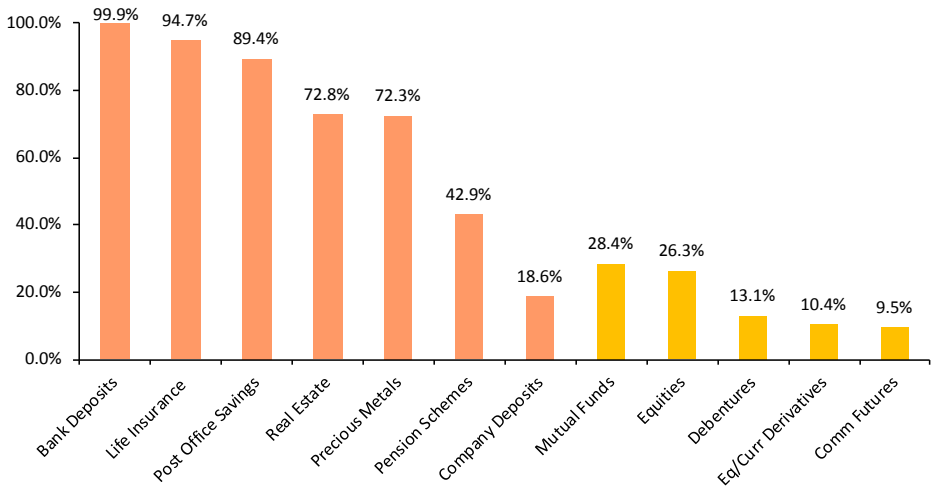
List of Instruments		
Bank Deposits (Fixed/Recurring/ Savings)	Company Deposits	Post Office Savings Schemes e.g., NSS, KVP etc.
Life Insurance	Pension Schemes	
Real Estate	Precious Metals (Gold/Silver/Platinum)	
Equities/Stocks/Shares	Mutual Funds/SIPs	Debentures/Bonds
Commodities Futures	Derivatives (Equity/Currency)	

Legend: Investment Instruments highlighted in yellow

28. National Sample Survey Office, Key Indicators of Debt and Investment in India NSS 70th Round, 2013, New Delhi: Ministry of Statistics Programme Implementation, last accessed December 30, 2015, http://mospi.nic.in/Mospi_New/upload/KI_70_18.2_19dec14.pdf

To help quantify the number and the behaviour of potential investors and savers who did not participate in the securities markets, respondents were specifically asked about non-investment instruments of savings or capital formation. As Figure 4.1 clearly demonstrates, there is a sharp distinction in the awareness levels between savings schemes and investment instruments; cognizance about savings schemes is significantly higher. While awareness concerning company deposits is lower than that of mutual funds or equities, a familiarity with every other savings schemes and non-market instruments is significantly higher than that of any of the market instruments.

Figure 4.1: Awareness Levels of Financial and Investment Instruments



N = 36,756 (all urban respondents, SIS 2015)

Additionally, although nearly all the survey participants are staggeringly aware of Bank Deposits (99.9 percent),Life Insurance (94.7 percent) and Post Office Savings (89.4 percent), familiarity with Mutual Funds and Equities is just 28.4 percent and 26.3 percent, respectively (Table 4.2). On the other hand, awareness of Derivatives (10.4 percent) and Futures (9.5 percent) is even lower and surprisingly, Debentures (13.1 percent), despite being higher in the capital stack and having a declared interest rate, ranks low too. Correspondingly, in 2003, Senetal[29] observe that the secondary corporate bond market in India is practically non-existent and in March 2015, Gwalani and Bharati[30]. also find that awareness and investments in the corporate bond markets remain abysmally low.

29. Pronab Sen, Nikhil Bahel and Shikhar Ranjan, Developing the Indian Debt Capital Markets: Small Investor Perspectives, New Delhi: Planning Commission, Government of India, July 2003, last accessed 18 December, 2015, http://planningcommission.nic.in/reports/wrkpapers/wkpr_debt.pdf

30. Hema P. Gwalani and D. B. Bharati, "An Analytical Study of the Awareness Level of Corporate Bond Market in India Among Retail Investors", IBMRD's Journal of Management and Research, Vol. 4, March 2015, pp. 75–87

For derivatives, on the other hand, it is not the market's novelty but a 1950s government statute that rationalizes the low level of awareness. The Bombay Cotton Traders Association started futures trading in 1875 and by the early 1900s, India had one of the largest futures trading markets in the world[31]. However, cash settlements and trading in options and derivatives were banned in 1952 till (acting on the recommendations of the LC Gupta Committee) SEBI approved derivatives trading from June 2001. In the interim half a century, derivatives remained restricted to the shadow 'badla' markets (banned by SEBI in 2001) and definitely out of reach of retail investors[32]. Since 2008–09, equity derivatives at the NSE have increased from an average daily turnover of ₹45,310 crore to ₹1,93,212 crore in 2015–16[33]. Although a relatively smaller market, currency derivatives has seen a sharper growth, moving from ₹1,167 crore to ₹18,602 crore in daily turnover in the same time period[34]. Furthermore, it is clear from the SIS and RBI data that institutional investors drive almost the entire volume and growth of this market.

Table 4.2: Household Awareness of Investment Instruments

Awareness of Investment Instruments	Mutual Funds	Equities	Debentures	Equity/Currency Derivatives	Commodity Futures
Awareness	28.4%	26.3%	13.1%	10.4%	9.5%
Investor Awareness	84.6%	79.4%	48.2%	33.6%	29.2%
Non-Investor Awareness	18.7%	17.1%	7.0%	2.4%	6.1%

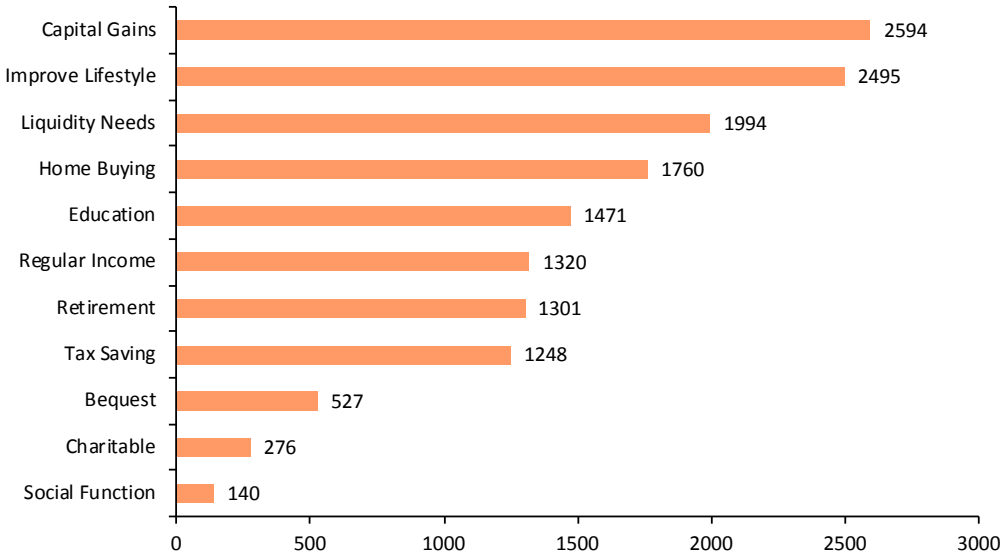
N = 36,756 (all urban respondents, SIS 2015)

According to the SIS 2015 data, the awareness level for savings instruments are almost identical amongst investors and non-investors, whereas (as Figure 4.1 significantly highlights) a familiarity with investment instruments is extremely low amongst non-investors. Awareness of even traditional investments like equities and mutual funds is surprisingly low among non-investors while an awareness of derivatives, bonds and debentures is in the single digits. This data shows that there is a need to reach out and educate a wider populace about options available in the securities markets and additionally, expound the effectiveness of probing more deeply into the benefits of diversification, risk management and returns optimization to create a more efficient household financial portfolio.

31. Asani Sarkar, "Indian Derivatives Markets", The Oxford Companion to Economics in India, Ed: Kaushik Basu, New Delhi: Oxford University Press, 2006, last accessed March 15, 2016, https://www.newyorkfed.org/medialibrary/media/research/economists/sarkar/derivatives_in_india.pdf
32. Ibid.
33. National Stock Exchange, "Business Growth in FO Segment", NSE website, last accessed March 10, 2016, https://www1.nseindia.com/products/content/derivatives/equities/historical_fo_bussinessgrowth.htm
34. National Stock Exchange, "Business Growth in CD Segment", NSE website, last accessed March 10, 2016, http://www.nseindia.com/products/content/derivatives/currency/cd_historical_businessGrowth.htm

To further investigate the specific motivations that govern a household's investing preferences, the SIS 2015 closely scrutinized their decision-making and investment rationale.

Figure 4.2: Why do Households Invest



N = 5,356 (all urban investor, SIS 2015). Optional question answered by 5,313 investors.
Respondents could check multiple options.

According to Figure 4.2, capital gains, which are "… an increase in the value of a capital asset (investment or real estate) that gives it a higher worth than the purchase price"[35], is the primary purpose for household investing. Thus, capital gains closely followed by lifestyle improvement are the key motivations for investing while liquidity needs and home buying also play crucial roles. Additionally, since there are almost no investment opportunities (as opposed to savings schemes) that allow for tax savings, this factors significantly lower in the list. With just 3 percent of Indians paying income taxes[36], the indifference towards tax savings schemes may also be a consequence of the insignificant tax net.

35. Merriam-Webster's Collegiate Dictionary, s.v., "capital gain", last accessed December 11, 2015, http://www.merriam-webster.com/dictionary/capital%20gain
36."Less than 3 percent File Income Tax Return in India", Deccan Herald, December 19, 2012, last accessed December 19, 2015, http://www.deccanherald.com/content/299566/less-3-percent-file-income.html

While investment rationale, that is, "Why do I invest?" is a crucial element of the survey, key drivers of broader financial savings (in both investment and other financial instruments), that is, "What Drives Me to Save?" is also an important question that needs to be explored. Figure 4.3 shows the distribution of savings amongst households by income levels. The economic reasoning behind the linear income-savings hypothesis is logical and derives directly from basic development economics. Since all additional income is expended to supplement basic needs, lower income groups have a higher marginalpropensity to consume[37]. Figure 4.3 backs this claim as the data shows that 85 percent of those in the < ₹20,000 income range have savings less than 40 percent of annual income. Once the threshold of basic needs is crossed, households start saving for future contingencies or for investment returns. The SIS data supports this hypothesis; in urban India, the limit is above or around the ₹20,000 per month level. The data also reveals that middle-class households in the ₹20,000 to ₹50,000 range, followed closely by the ₹50,000 to ₹1 lakh income group, have a higher marginal propensity to save. Unexpectedly, the figures disclose that 80 percent of households with monthly income greater than 1 lakh also have savings less than 40 percent of annual income. While this seems to go against the linear income-savings hypothesis, it is crucial to keep in mind that this high- income segment may have social safety nets (like insurance, family support, etc.) that allow them to have a lower "precautionary demand for savings". Additionally, with just 3 percent of Indians paying income taxes, the top tier of the high-income group are arguably less keen to disclose their incomes and savings.

37. See Chapter 7, Debraj Ray, Development Economics, Princeton, NJ: Princeton University Press, 1998

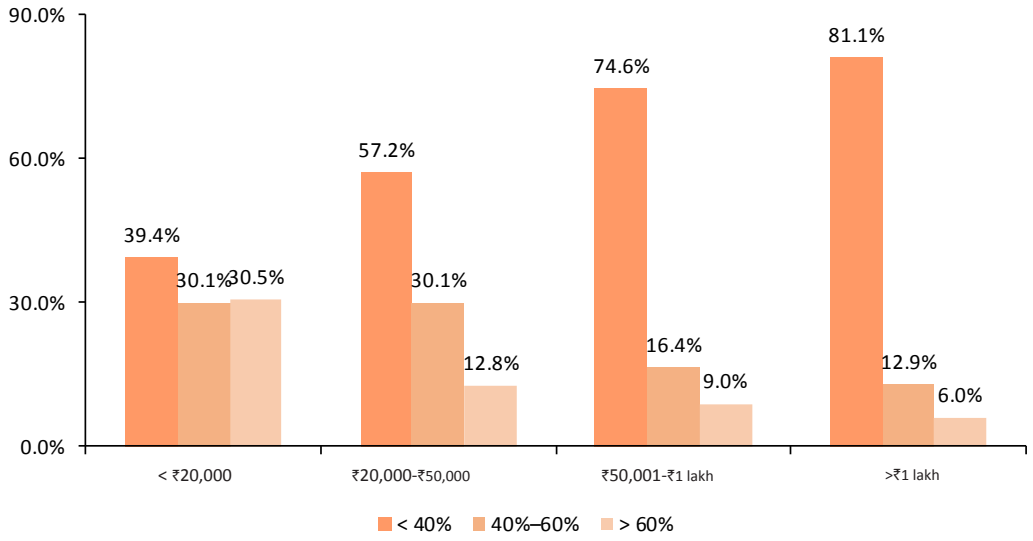
Figure 4.3: Total Household Savings as a Percentage of the Household's Annual Income

Savings	Monthly Income			
	Below ₹20000	₹20000 -₹50000	₹50000 - ₹1 Lakh	Above ₹1 Lakh
< 40% of annual income	10569	8833	2920	5513
40%–60% of annual income	1506	3660	624	843
> 60% of annual income	341	771	143	569
Total	12416	13264	3687	6925

N = 36,756 (all urban respondents, SIS 2015)

To probe further into household indebtedness, the other side of the savings coin, we perform a similar analysis. In this case, the income-debt inverse linear relationship holds true – the higher the household income, the lower the debt levels drop. Figure 4.4 confirms that 31 percent of low-income households (with monthly incomes less than ₹20,000) have debts larger than 60 percent of their annual income, whereas just 6 percent of ₹1 lakh+ households have matching debt levels. However, contrasting the survey findings on savings, the higher income households have lower debts than the mid-income groups. Analogous to the low-income group, nearly a third of the mid-income group households are indebted at the 40 percent to 60 percent of income level. With the rise of indebtedness in the middle class owing to the upsurge of credit instruments like credit cards, easier car loans, student loans and housing loans, this is a foreseeable outcome. While high-income groups also show a comparable increase in the use of credit instruments, their elevated income levels possibly balance and thus, do not significantly affect their indebtedness ratios.

Figure 4.4: Total Debt as Percentage of Annual Income



Debt	Monthly Income			
	Below ₹20000	₹20000 -₹50000	₹50000 - ₹1 Lakh	Above ₹1 Lakh
< 40% of annual income	4892	7580	2751	5619
40%–60% of annual income	3733	3993	605	894
> 60% of annual income	3791	1691	331	412
Total	12416	13264	3687	6925

N = 36,756 (all urban respondents, SIS 2015)

Table 4.3 shows the average household total debt for the entire surveyed population as a percentage of total annual income. While 58 percent of the participants had debt that was less than 40 percent of annual income, 25 percent had debt levels in the 40 percent to 60 percent of annual income range, and a mere 17 percent had debt more than 60 percent of annual income.

This is indeed welcome news for Indian policy makers since it assertively showcases the low indebtedness in the country. For instance, the United States has a $1,185 thousand crore total household debt. With a population of about 30 crore, an average household size of 2.84 people and an annual median income of $51,939, the total US indebtedness number in relation to its annual

38. The Organisation for Economic Co-operation and Development (OECD), "Household Debt: Total % of Net Disposable Income, 2014", National Accounts a t a Glance, l a s t accessed March 30 , 2016 ,
h t t ps : / / data. oecd. o rg/ hha/ household- debt. h tm
39. McKinsey Global Institute, Debt and (Not Much) Deleveraging, London: McKinsey & Company, February, 2015, last accessed December 10, 2015, http://www.mckinsey.com/global-themes/employment-and-growth/debt-and-not-much-deleveraging

income is over 190 percent. Additionally, the Household Debt to Disposable Income statistic for the US[38] stands at 113 percent of its annual income. The SIS 2015 data on debt (Table 4.3) is consistent with McKinsey's 2015 report, "Debt and (Not Much) Deleveraging"[39] in which India's rank just misses the lowest quartile among the 47 nations listed. According to the report, while the Debt-to-GDP ratios for developed economies like Japan (top of the list at 400 percent), the US (16th on the list at 233 percent) and the United Kingdom (13th on the list at 252 percent) have actually been increasing, India's national leverage ratio has essentially remained constant in the past 7 years and stands at 120 percent of GDP (rank 35). The Indian Debt to GDP ratio is significantly lower even when compared to other large developing countries like China (217 percent), South Africa (133 percent) and Brazil (128 percent).

Table 4.3 – Household Total Debt as Percentage of Annual Income

Debt	Frequency	Percentage
< 40% of annual income	21238	57.5%
40% - 60% of annual income	9279	25.0%
> 60% of annual income	6239	16.5%

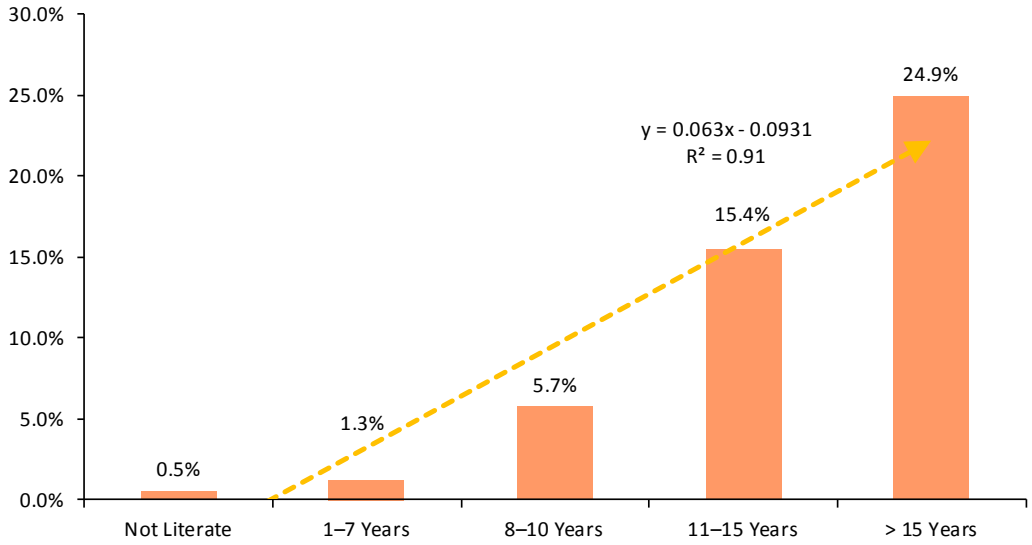
N = 36,756 (all urban respondents, SIS 2015)

The Education-Occupation-Investment Interrelationship

Grable (2000)[40] establishes a relationship between multiple underlying socio-demographic factors (like education, income, age and marital status) and financial risk tolerance. The direct linear relationship between investments and education (Fig. 4.5) may also help further rationalize the survey's unanticipated outcome that clearly ascertains that income is not a primary linear driver of savings and that investor distribution is skewed towards the higher educated groups. According to the SIS data, while 25 percent of the highly educated (15+ years of education) invest in the securities markets, less than 1 percent of those with 1 to 7 years of education do so. This percentage increases to 6 percent and 15 percent for 8-10 years and 11-15 years of education, respectively.

40. John E. Grable, "Financial Risk Tolerance and Additional Factors that Affect Risk Taking in Everyday Money Matters", Journal of Business and Psychology, Vol. 14 (Summer 2000)

Figure 4.5 – The Education-Investment Relationship



N = 5,356 (all urban investors, SIS 2015)

According to the SIS data, income and education significantly influence investment choices while variables like age seem to have a very limited effect on whether a respondent chooses to invest or not. The average age for both investors and non-investors is 41 years. Similarly, marital status and household size show no significant effect on the choice to invest. However, government and private employees show a considerable disparity in their predilection to invest (Table 4.4), which may possibly be an effect of the steady incomes amongst government employees. According to the SIS data, 23 percent of government employees and only 11 percent of private employees are investors and thus, it seems that occupation has an effect on investment behaviour. Additionally, since 17.5 percent business owners are also investors, the data concludes that business owners, too, have a higher likelihood of investing. SIS's Chapter 9 analyses risk tolerance and the various factors affecting it in detail.

Table 4.4 – Investors by Occupation

Occupation	Non-Investor (%)	Investor (%)
Service (Government)	76.9%	23.1%
Business (Shop Owner)	80.7%	19.3%
Other Business	83.7%	16.3%
Service (Private)	89.4%	10.6%
Retired	91.5%	8.5%
Agriculture	95.7%	4.3%
Others (Specify)	96.4%	3.7%
Self Employed	96.8%	3.2%
Total	85.4%	14.6%

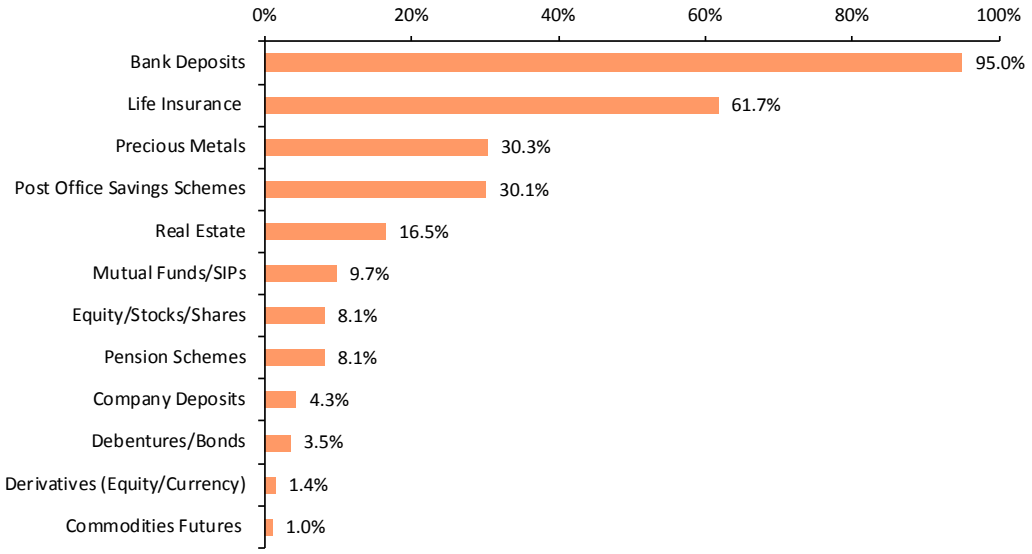
N = 5,356 (all urban investors, SIS 2015)

Savings and Investment Instruments: Household Preferences

Figure 4.6 shows the actual percentage of investors/ savers in each of the instruments discussed in the first half of this chapter. It is apparent that non-market related instruments, including comparatively higher risk assets like precious metals or real estate, are clearly more popular. Long considered a safe, long term, and compulsory savings instrument, India has the highest incidence of life insurance buyers in the world. Predictably, post office savings schemes with their wide reach and network and risk-free schemes are also a crucial savings instrument. However, the chart highlights a crucial bias towards precious metals and real estate. After China, India is the second largest consumer of gold. With over 600 tons being used in jewellery production alone, Indian households are estimated to own 22,000 tons of the metal[41]. While gold prices have corrected significantly over the past few years, more Indians would rather continue to use gold as a savings instruments than invest in mutual funds or equities. Although the Residex Indian Real Estate Index for the top-20 cities has shown flat or marginal growth in nearly all cities over the past 12 to 24 months[42], this sector, too, continues to be a primary instrument of capital formation for Indian households.

41. World Gold Council, "Developing Indian Hallmarking: A Roadmap for Future Growth", July 30, 2015, last accessed April 7, 2016, http://www.gold.org/download/file/4025/Developing-Indian-hallmarking.pdf
42. National Housing Bank, NHB Residex January–March 2015, last accessed 16 December, 2015,

Figure 4.6 – Investment and Savings Vehicles Used by Survey Respondents

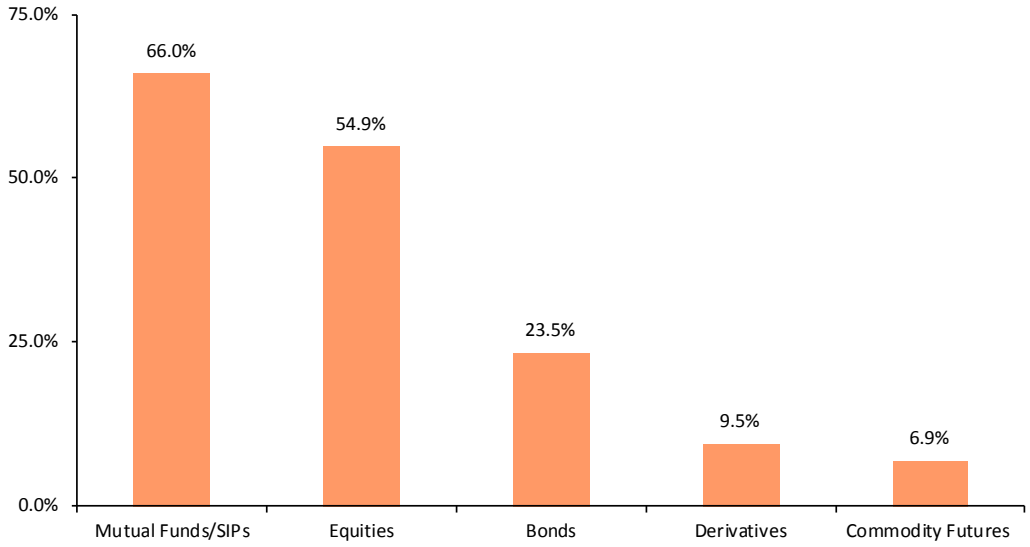


N = 36,756 (all urban respondents, SIS 2015). Respondents could check multiple options.

The SIS 2015 data illustrates that the universe of retail derivatives investors, on the other hand, is very small with less than 10 percent of investors using Currency/ Equity derivatives or Commodity Futures. Amongst investors, mutual funds are the most popular investment instrument (66 percent) while more than half invest in equities (55 percent) and less than a quarter invest in debentures or bonds. The large number of investors in mutual funds are most likely a direct positive result of the GoI's and the mutual fund industry's sustained and extensive outreach efforts[43]. The Association of Mutual Funds in India (AMFI), which is an association of SEBI-registered mutual funds in India and has all the 47 SEBI-registered asset management funds as its members, has been spearheading the effort to publicize the importance of mutual funds to retail investors. According to the AMFI website, between April 2016 and December 2016, there are 185 confirmed investor awareness programs that will be conducted by member firms across the country[44].

43. Shaji Vikraman, "Slow Start, Rapid Growth: Story of India's Mutual Funds Industry", Indian Express, September 17, 2015, last accessed March 15, 2016, http://indianexpress.com/article/explained/slow-start-rapid-growth-story-of-indias-mutual-funds-industry/
44. Association of Mutual Funds in India website, last accessed April 7, 2016, https://www.amfiindia.com/

Figure 4.7 – Prefered Investment Instruments



N = 5,356 (all urban investors, SIS 2015). Respondents could check multiple options

Urban Investment Preferences

In this section, urban investors' choices are analysed in detail whilst carefully differentiating between the socio-economic characteristics of equity, mutual fund and debt investors. Although most income groups invest primarily in mutual funds, the SIS data shows that 70 percent of the top tier middle-income group (₹50,000 to ₹1 lakh) invests in equities (Table 4.5). With reference to equities and mutual funds, no well-defined relationship can be perceived between income and choice of investment instruments whereas debt instruments are noticeably more popular among lower income groups. 30 percent of Range I investors invest in bonds and debentures while only 23 percent of Range II and 11 percent of Range III investors invest in bonds, respectively. However, among Range IV investors, this number increases again to 26 percent. It is unsurprising that lower risk debt instruments appeal to a lower income client base, and yet, this may also be an effect of successful inroads built by retail bond sales executives.

Table 4.5: Investment Instrument Choice, by Income

Range	Income Range	Mutual Fund Investor	Equity Investor	Debt Investor	Total Investors	Total Respondents
I	Less than 20,000	729	665	311	1033	12688
	(% of Total Investors)	70.6%	64.4%	30.1%	100.0%	
II	20,000 to 50,000	2161	1626	732	3236	13403
	(% of Total Investors)	66.8%	50.2%	22.6%	100.0%	
III	50,000 to 1 lakh	195	336	54	478	3721
	(% of Total Investors)	40.8%	70.3%	11.3%	100.0%	
IV	Above 1 lakh	451	314	159	609	6944
	(% of Total Investors)	74.1%	51.6%	26.1%	100.0%	

N = 5,356 (all urban investors, SIS 2015)

As observed earlier, education may have a significant influence on choice of investment instruments. Table 4.6 provides two key insights into education and choice of investment instruments. First, complementing Grable's (2000) argument that higher education leads to a higher financial risk appetite and as equities are higher risk instruments than mutual funds (which are diversified) or bonds (which are higher in the capital stack), the SIS data proves that mutual fund and debt investing are not affected significantly by income levels while higher levels of education lead to an increased appetite for equity investing.

Table 4.6: Education and Investment Instrument Choice

Education	Mutual Fund Investor	Equity Investor	Debt Investor	Total Investors
1 to 7 Years	22	9	0	32
(% of Total Investors)	68.8%	28.1%	0.0%	100.0%
8 to 10 Years	273	108	90	445
(% of Total Investors)	61.3%	24.3%	20.2%	100.0%
11 to 15 Years	1299	1155	470	2324
(% of Total Investors)	55.9%	49.7%	20.2%	100.0%
More than 15 Years	1939	1667	696	2551
(% of Total Investors)	76.0%	65.3%	27.3%	100.0%

N = 5,356 (all urban investors, SIS 2015)

The second interesting outcome shows that investors with more years of education invest in higher number of instruments, which clearly indicates a greater realization of the value of diversification in the securities markets. Among those with 15+ years of education, 76 percent invest in mutual funds, 65 percent invest in equities and 27 percent in debt while among those with 11 to 15 years of education, 56 percent invest in mutual funds, 50 percent in equities and 20 percent in debt. A similar pattern is also seen among those with 8 to 10 and 1 to 7 years of education.

One of the key findings of this report is that although economic and demographic considerations are crucial for investment choices, the cultural aspect is probably the most important driver that determines whether an individual invests in the securities markets or not. While the state-level and zonal-level details of investors, their choice of investment instruments and cross-tabulations used to further analyse their choices are provided in Chapter 10, Table 4.7 shows the investor distribution by zone (including data on investment instruments choices). The West Zone leads not only in the total number of investors but also in awareness of investment instruments. Additional evidence that supports this finding underlines that despite 20 regional exchanges shutting down in the last fiscal year, the volumes in the Bombay Stock Exchange have kept increasing steadily.

Table 4.7: Investors and Investment Instruments used by zone

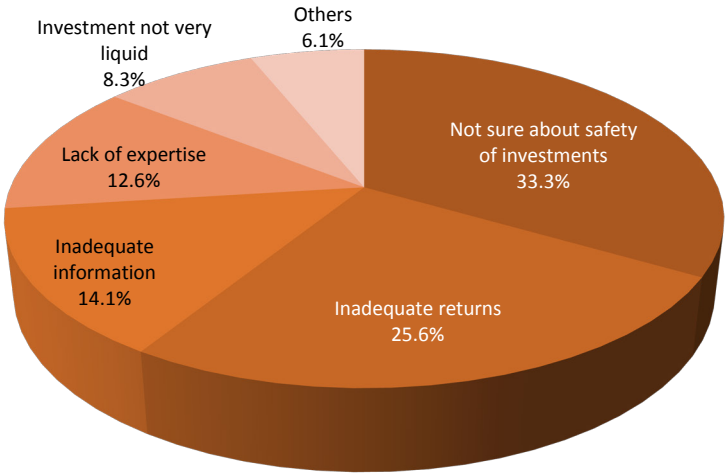
Instrument	East	North	South	West
Mutual Funds	633	859	212	1832
Equities	143	804	157	1837
Debentures	37	218	88	913
Derivatives	0	212	5	294
Commodity Futures	163	143	19	44
Total Investors	812	1419	385	2740

N = 5,356 (all urban investors, SIS 2015)

Why Don't More Households Invest?

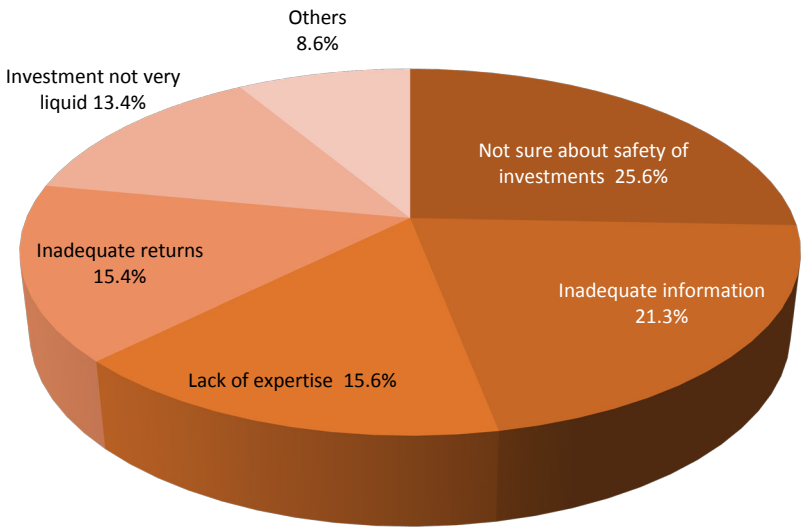
As can be seen from the previous analysis, there exists a large pool of households from a high to mid income group who are educated and who save (in bank accounts, life insurance, or post offices), and yet do not invest. The fundamental rationale behind their non-participation in securities markets is of paramount importance to policy makers and the securities market regulator. While a lack of awareness about key instruments (Figure 4.1) is certainly a primary roadblock, more than 40 percent of households that are aware of investments like mutual funds or equities, do not invest in the markets. To compartmentalize and rationalize this non-participation, Figure 4.8 and Figure 4.9 analyse the data on why households do not invest in specific instruments.

Figure 4.8 – Why Do Households not Invest in Mutual Funds?



Note: Other includes Absence of investment through cash (3%), Limited access (1%), Not sure whom to approach (1%) and Requirements like PAN (0.2%)

Figure 4.9 – Why Do Households Not Invest in Equities?



Note: 'Others' includes not sure whom to approach (4%), inadequate returns (3%), Limited access (1%) and Requirements like PAN (0.2%)

The above figures show that the typical impulse for not investing in securities markets instruments is principally risk aversion (i.e., apprehension concerning the safety of a particular instrument) followed by inadequate returns and lack of information. A sustained and widespread mutual fund information dissemination in India has ensured that information availability is not a concern. Respondents seem more anxious regarding mutual funds returns. On the other hand, investors are not fully cognizant about equities, especially its diversity benefits and comparative returns, especially when compared to mutual funds. Potential investors are also not aware of the superior risk adjusted returns of mutual funds and equities and seem to consider individual savings and investment instruments independently instead of calculating their optimal weights in a diversified portfolio. Moreover, from a regulators' standpoint, the data quite clearly highlights that none of the requirements and restrictions put in place for securities markets investing have become impediments for potential investors. Very few respondents (less than 1 percent) desist from investing due to regulatory issues like KYC requirements, PAN card requirements or restriction on cash investments.

05 RURAL SAVERS: AN UNTAPPED INVESTOR BASE

KEY FINDINGS

- **There are a mere 32 investors (0.234 percent) amongst the 13,697 rural survey respondents.**
- **Of these investors, 21 (66 percent) invest in mutual funds, 4 (12.5 percent) invest in equities and 7 (22 percent) invest in bonds and debentures although none have ever invested in derivatives or futures.**
- **However, 95 percent of rural survey respondents have bank accounts, 47 percent have life insurance, 29 percent have post office deposits and 11 percent save in precious metals.**
- **Although the SIS data showcase a high propensity to save, these potential investors do not participate in the securities markets – possibly, due to a lack of awareness.**
- **Almost all respondents are aware of bank deposits while 88 percent and 76 percent are aware of life insurance and post office savings, respectively. The awareness levels for mutual funds and equities are 1.4 percent although less than 0.5 percent are cognizant of futures, derivatives or debentures.**
- **The SIS data does not find a clear linear relationship between education, income and/or occupation and investments amongst the rural population.**
- **On mapping out the data, the SIS discovers that rural investors tend to reside close to the local district headquarters or urban centres like Delhi, Bangalore and Hyderabad.**

Chapter Rationale

From the earliest available data (1952) it is seen that despite rising rural income and education, improving access to electricity and roads, and the significant growth in financial inclusion, the rate of investments in the securities markets from the rural Indian population has been dismally low. According to SIS 2015, just 0.234 percent of rural survey respondents are investors. Even among these few investors, there is not one engaged in derivatives or futures or invested in more than one asset class while 66 percent invest in mutual funds, 22 percent in bonds and 12.5 percent in equities. However, since 95 percent of rural households have bank savings while 47 percent and 29 percent of respondents use savings instruments from life insurance companies and the post offices, respectively, these low investment numbers are not simply due to a lack of financial inclusion. With merely 1.4 percent of respondents barely familiar with mutual funds or equities and less than 0.5 percent who have scarcely even heard of bonds, futures and derivatives, it appears that there is a complete lack of awareness concerning these securities markets instruments amongst the rural population.

According to the SIS data, nearly 40 percent of the rural respondents earn more than ₹20,000 per month while 24 percent of households have a total savings of 40 percent to 60 percent of their annual income and a further 7 percent have savings higher than 60 percent of their annual income. Although these households, which have the income levels and the tendency to save, can potentially participate in the securities markets, the percentage of investors is as low as that of the broader rural average. Moreover, contrasting the urban survey, the rural SIS data does not find a find a clear linear relationship between education and investments amongst the rural population. Despite 1.2 to 1.5 crore households with comparable education, income and savings propensity, the data estimates that there are one crore rural investors. Arguably, an increase in awareness levels and information accessibility amongst the percentage of rural households who use various non-market instruments for capital formation could directly result in potential investors in the securities markets. Appropriate awareness programs and outreach efforts could certainly help in bringing these potential investor households into the securities markets fold.

Introduction

In 1964, the Economic Weekly (now Economic and Political Weekly)[45] published one of the earliest (post-Independence) research studies on the rural investor. To study the decadal difference in capital formation amongst rural households, this survey compared the data from the all India Rural Debt and Investment Survey (1961-62) with the all India Rural Credit Survey (1951-52) and concluded that, "The relatively small value of capital formation by rural households is thus perhaps the most disturbing finding of the Reserve Bank's Survey". Half a century later, both the All India Debt and Investment Survey (AIDIS) (2013, 70th edition)[46] and the SIS 2015 data also conclude that although savings rates and awareness has significantly increased, the investment in securities markets still remains extremely muted amongst the rural population. According to the AIDIS data, the percentage of shares and other markets-related assets of total value of household assets in rural areas is only 0.07 percent while the SIS 2015 data shows that just 0.23 percent of rural households invest in securities markets assets.

Based on the SIS 2015 findings and utilizing the trends and patterns observed among the larger urban data set, this chapter tries to estimate the number of potential rural investors. This survey should help policy makers and the government to quantify the size of this potential financial consumer base and also aid them to determine the necessity and process of enabling rural savers to become securities markets investors. In the current context of the GoI's Pradhan Mantri Jan Dhan Yojana (PMJDY) and the focus on financial inclusion, this survey with its detailed pan-India rural data can certainly help define a future road map.

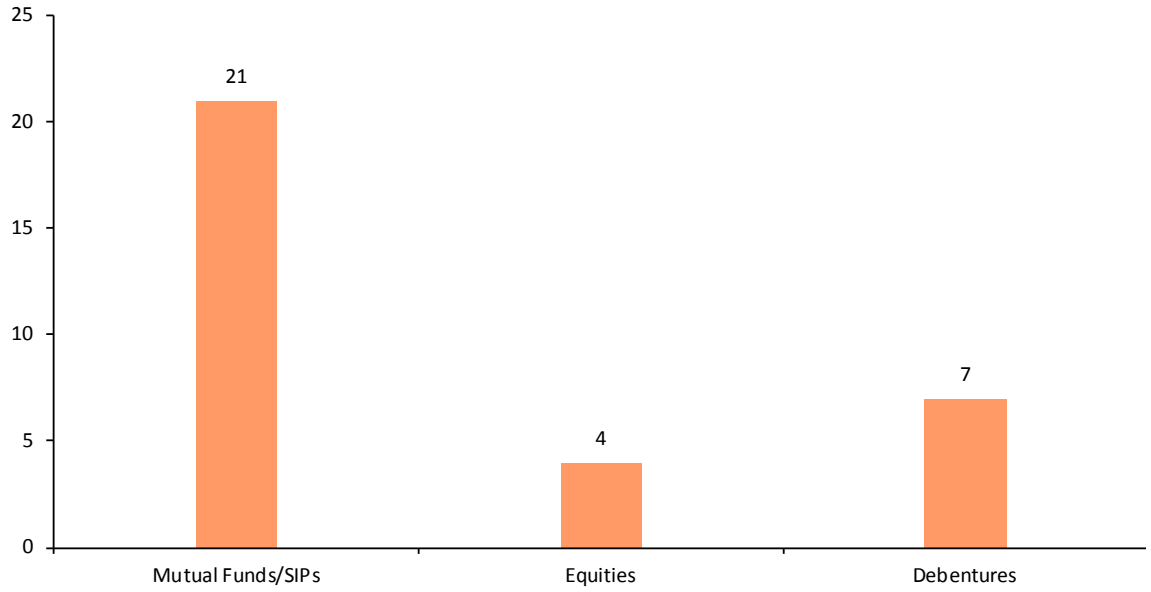
The (Elusive) Rural Investor

In sharp contrast to the 14.5 percent investors in the total urban survey respondents, there are only 32 investors (0.234 percent) amongst the 13,697 rural survey respondents. However, comparable to the urban survey, investments in mutual funds are significantly higher than equities or bonds (Figure 5.1). Of the 32 rural investors, 21 (66 percent) invest in mutual funds, which is almost exactly equal to the percentage of urban

45. Economic Weekly, "Rural Debt and Investment", Vol. 16, Issue 4, January 1964
46. National Sample Survey Office, Key Indicators of Debt and Investment in India NSS 70th Round, 2013, New Delhi: Ministry of Statistics Programme Implementation, last accessed December 30, 2015, http://mospi.nic.in/Mospi_New/upload/KI_70_18.2_19dec14.pdf

respondents who invest in these funds. Only 4 (12.5 percent of investors) and 7 (22 percent of investors) out of the surveyed population invest in equities and bonds/ debentures, respectively, whereas not one respondent has ever invested in derivatives or futures. Since riskier investments like derivatives are completely absent from their portfolios and equities lag behind safer debt investments (unlike in the urban areas), the risk aversion amongst the few rural investors is undeniably palpable.

Figure 5.1: Investments in Different Asset Classes Amongst Rural Investors

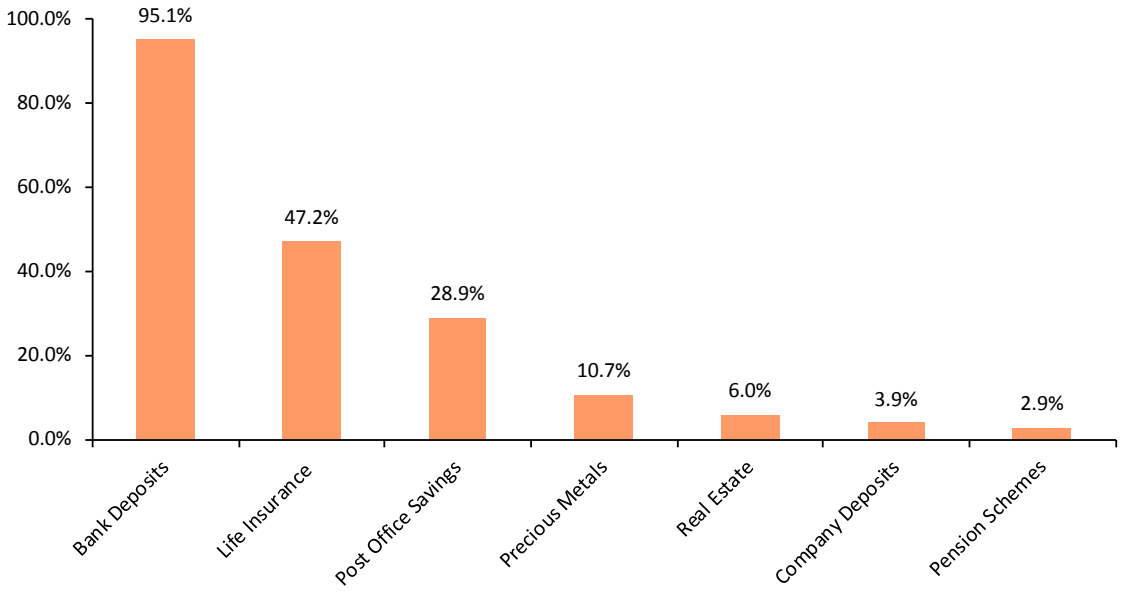


N=32 (all rural investors, SIS 2015)

On the other hand, it is crucial to keep in mind that the reported lack of investments does not automatically translate to a complete absence of financial inclusion in Indian villages. A significant part of the population who possess savings banks accounts or post office deposits certainly participate in the financial system. As Figure 5.2 unmistakably asserts, 95 percent of rural survey respondents have bank accounts, 47 percent own life insurance while 29 percent possess post office savings. Thus, the data confirm that the Indian government's focus on financial inclusion by increasing the number of rural banks and providing outreach messages via mass media in villages to encourage traditional banking habits has been remarkably successful. With 47 percent

of the surveyed rural population owning life insurance policies, the insurance companies have also impressively succeeded in including the rural population in their fold. The Life India Corporation of India (LIC), which was formed in 1956, has relentlessly disseminated information on insurances across the country for the last sixty years. Its widespread success is reflected in both the SIS's urban and rural savings data. With its 1,20,388 employees and an agent base of more than 10 lakhs (11,95,916 as on 31st March 2014)[47], the LIC, alone, is instrumental for the ease with which the general Indian population accepts life insurance as a standard instrument of long-term, regular savings. Comparably, with its reach of 1,54,866 post offices (of which 1,39,080 or nearly 90 percent are in rural areas), post office savings schemes too are an easily accepted method of capital formation. In Chapter 4, the SIS 2015 data confirms that newer forms of investments and savings have limited awareness and thus, lower investments. Since the broader appeal and reach of the securities markets began post-liberalization, it has relatively limited awareness when compared to insurance.

Figure 5.2: Instruments for Savings and Capital Formation used by Rural Households

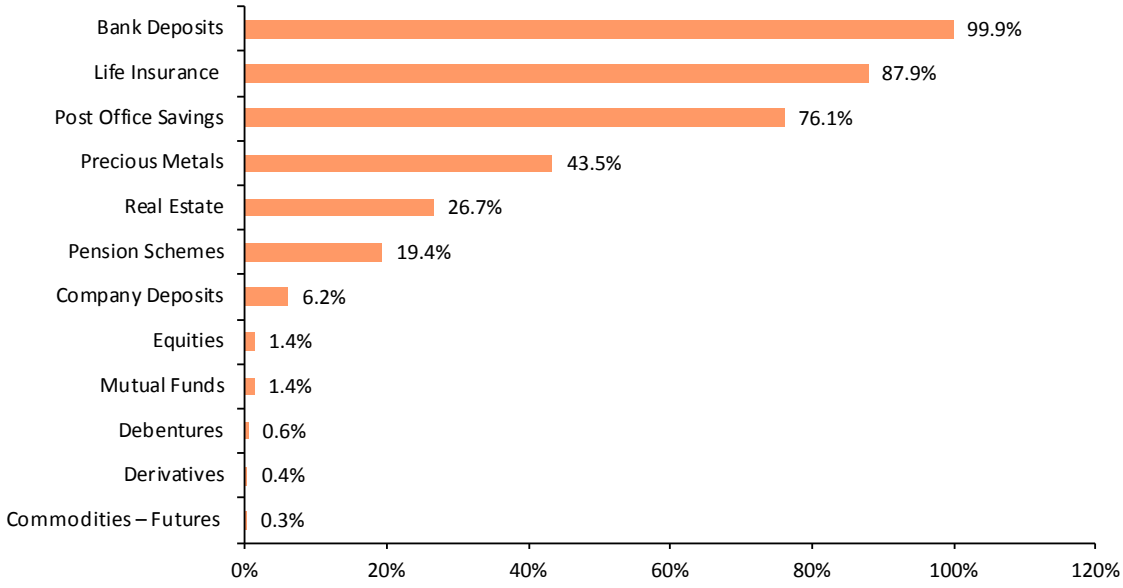


N=13,697 (all rural respondents, SIS 2015)

47. Life Insurance Corporation of India website, last accessed December 30, 2015, http://www.licindia.in/

According to SIS 2015 data, nearly 100 percent of respondents are aware of bank deposits, 88 percent are aware of Life Insurance while 76 percent are cognizant of Post Office savings whereas, the awareness levels for mutual funds and equities are both 1.4 percent while less than 0.5 percent respondents even know about futures, derivatives or debentures. This bleak scenario of investing amongst rural households seems to be a consequence of the lack of awareness about different investment instruments (Figure 5.3).

Figure 5.3: Awareness of Savings, Investment and Capital Formation Instruments



N=13,697 (all rural respondents, SIS 2015)

Potential Rural Investors

Using the analysis on urban household investments (Chapter 4), this section tries to estimate the total number of potential rural investors in India based on income levels, investments and savings. Before scrutinizing the three primary drivers of investments, which are income, education and occupation, it is essential to analyze the savings rates amongst rural households. Table 5.1 demonstrates that while rural savings rates are significantly lower than urban areas (an effect of lower real income in rural areas), nearly a quarter of households have total savings in Range II while more than 7 percent have total savings in Range III. There are more than 22 crore rural households in India and amongst these, 6 crore households are in the former group (Range II) and around 1.5 crore in the latter (Range III). The number of investing households in rural India is significantly lower than these numbers.

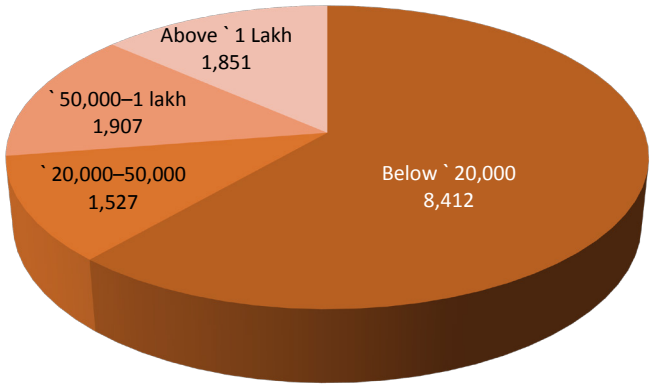
Table 5.1: Total Savings of Household as Percentage of Annual Income

Total Savings as Percentage of Annual Income			
Range I	< 40% of Annual Income	9427	68.8%
Range II	40%–60% of Annual Income	3293	24.0%
Range III	> 60% of Annual Income	977	7.1%

N=13,697 (all rural respondents, SIS 2015)

Figure 5.4 shows that not only do nearly 40 percent of respondents have an income higher than Rs.20,000 per month, 14 percent of these are in the greater than 1 lakh per month income slab. Additionally, it is crucial to remember that baseline expenses in rural areas are significantly lower than in urban India, which significantly increases the potential for capital formation and investments in rural high and middle-income groups. The fact that there are a negligible amount of securities markets investors even among these households displays a singular lack of awareness and dearth of outreach.

Figure 5.4: Income Distribution of Rural Survey Respondents

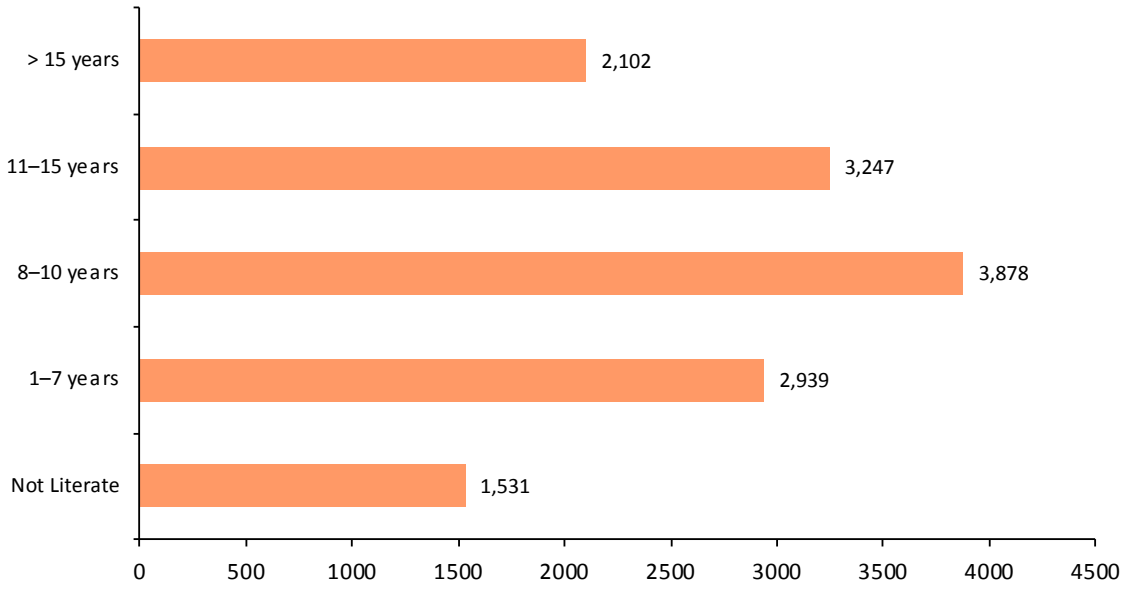


N=13,697 (all rural respondents, SIS 2015)

Analyzing the savings and income data further, it is seen that 31 percent of the above one lakh income households and 28 percent of the ₹50,000 - ₹1,00,000 income households have total savings that are more than 40 percent of their annual household income. Keeping in mind the 22 crore rural households population, the SIS estimates that about 1.5 to 1.8 crore households (controlling for the survey design) possess income and savings rates that will undoubtedly allow them to invest in market-related instruments. However, even among these high-income, high-savings households, investment rates are insignificant and hover around the rural average of 0.23 percent.

In the urban households chapter (Chapter 4), the SIS established a clear linear relationship between education and investments (Figure 4.5). Education not only has a direct linear relationship with investing and savings but an even stronger one with income levels. As Figure 5.5 shows, the right skew in the income data has also significantly affected the education levels of the survey respondents. While the current Indian national literacy is 74 percent, the literacy rate of the SIS 2015 survey respondents is 89 percent (which is closer to the youth literacy rate of 90.2 percent). According to the survey data, 25 percent of urban respondents with more than 15 years of education invest in the securities markets whereas in more educated rural households, this percentage remains equivalent to the national rural average of 0.23 percent.

Figure 5.5: Education Levels amongst Rural Respondents



While it is surprising that investment levels are low even amongst the educated and high-income groups of rural India who also have significantly high savings rate, it distinctly highlights the strong urban-rural divide regarding financial awareness. The significance of these differences have to be noted and outreach from the government and regulators defined, to create awareness and thus, a higher level of financial inclusion that extends beyond basic banking operations.

06 INVESTORS RESPONSE TO INITIAL PUBLIC OFFERINGS (IPOs)

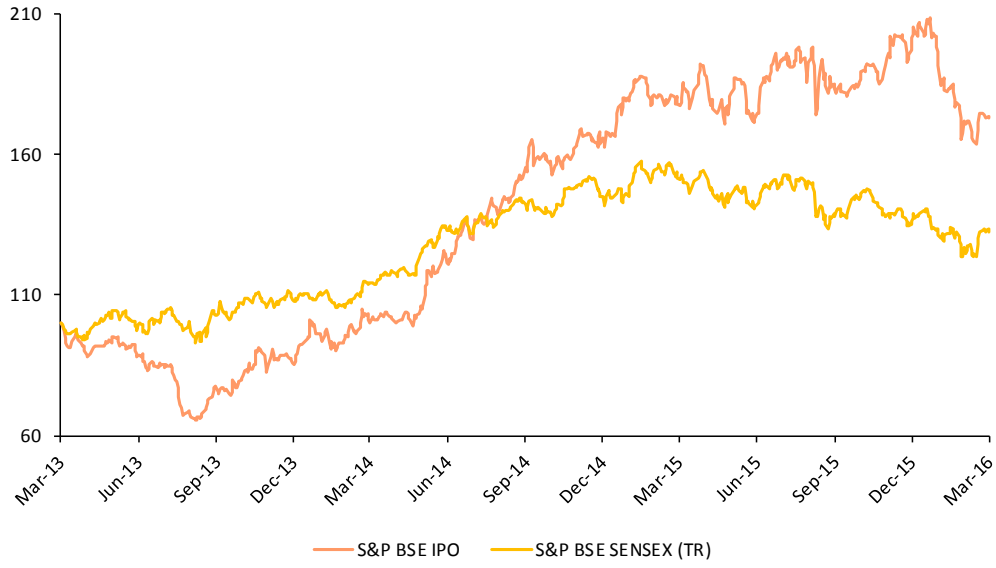
KEY FINDINGS

- **While 15 percent of survey participants are investors, just 18 percent of these have invested in IPOs. Thus, a mere 3 percent of all survey participants have invested in IPOs.**
- **Over 72 percent of regular IPO investors find the IPO process challenging.**
- **The book building process, the time taken for allocation and the handing over of cheques are the most critical roadblocks. Each of these issues has been acted upon by SEBI over the past year.**
- **The median IPO investor participates in one IPO per year.**
- **Despite the large-scale closure of brokerages (detailed in Chapter 8), financial intermediaries play a key role in IPO information dissemination.**
- **Stockbrokers are the largest supplier of IPO application forms.**
- **Notwithstanding the increasing role of the Internet; newspapers and television remain the top two sources of IPO-related news.**
- **Indian investors demonstrate an intuitive wisdom by investing in IPOs for an optimal holding period.**

Chapter Rationale

Reflecting the broader sentiments of the global credit markets, the IPO markets in India have gone through a roller coaster ride in the past decade and are slowly recovering after a lull of over four years. However, according to the 2015 SIS data, most Indian investors perceive the IPO investment processes of book building and cheque clearance together with the protracted time spent on the entire process from application to allotment to be complicated and cumbersome. Consequently, less than 20 percent of investors, which is close to 3 percent of those surveyed-participate in IPOs and even amongst those who do, the investment frequency is just one IPO per year. From the SIS data, we can extrapolate that a reliance on traditional sources of information and advice (i.e., brokerages and newspapers) despite the large-scale closure of brokerages and the Internet's appropriation of information is affecting IPO growth. In spite of these impediments, Indian investors demonstrate an intuitive wisdom by usually investing in IPOs for a holding period that is less than three years. As Figure 6.1 demonstrates, empirically, Indian IPOs have persistently outperformed broader indices in the initial two to three year period.

Figure 6.1 – Comparative Performances: S&P BSE IPO Index and S&P BSE Sensex[48]



Source: Bloomberg

48. S&P Dow Jones Indices, S&P BSE IPO Index and S&P BSE Sensex, last accessed March 10, 2016, http://us.spindices.com/indices/equity/sp- bse-ipo

Introduction

In an initial public offering (colloquially referred to as "going public"), private companies sell their shares in securities exchanges to raise capital and thus, transform into public companies listed in the stock markets. IPOs allow businesses to raise funds for expansion and the broader retail investor community to participate in a firm's growth. Unlike a debt or a loan, which are financial obligations for the company, the money raised through an IPO is equity capital in a company, which reduces a company's leverage and improves its balance sheets. Common shares do not have declared interest rates and consequently, IPOs tend to allow companies to reduce their WACC (Weighted Average Cost of Capital).

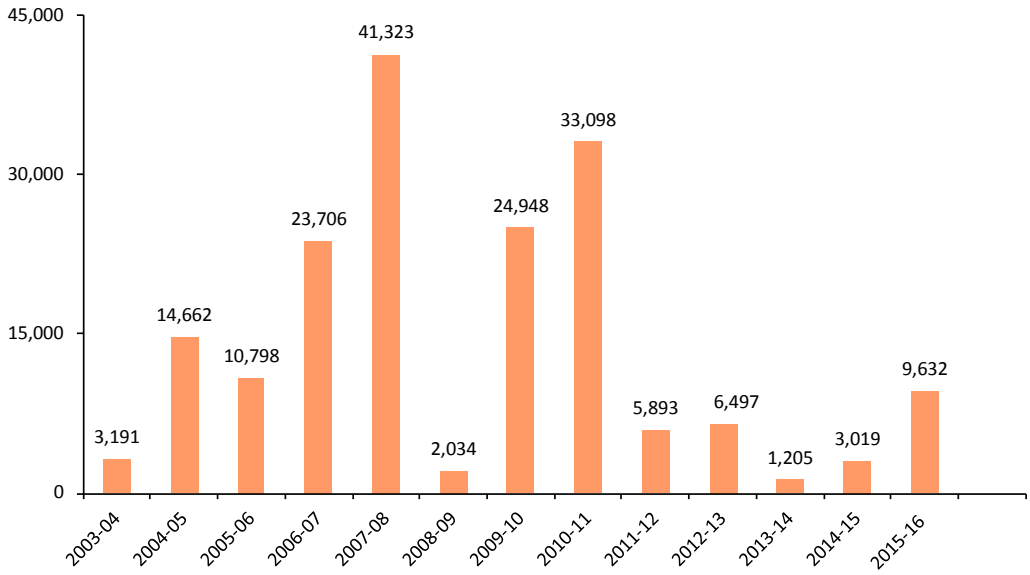
With rising entrepreneurship in India and an emergent start-up ecosystem, a strong IPO market allows venture capitalists and early stage investors to be at ease with their investments. Weaker market sentiments do not allow new shares to be priced at optimal valuations, leading to fall in IPO volumes; thus, as a barometer of investor sentiment, new public issues—either as Initial Public Offerings (IPO) of equities or New Fund Offerings (NFO) of mutual funds—are a key area of interest for SEBI. These primary markets that provide liquidity to corporations and are the key to understanding investor sentiment are crucial for a smooth functioning economy[49].

Indian IPO Markets

Reflecting the broader sentiments of the global credit markets, the IPO markets in India have gone through a roller coaster ride in the past decade. Figure 6.2 shows the trend in IPO issuance since FY 2003-04, by volume. The sharp global economic growth and the subsequent GFC are also echoed in this data[50].

49. NASSCOM and Zinnov, Startup India – Momentous Rise of the Indian Start-up Ecosystem (New Delhi: NASSCOM, 2015), last accessed March 17, 2016, http://www.nasscom.in/startup-india-%E2%80%93-momentous-rise-indian-startup-ecosystem
50. Prime Database, Prime IPO database, last accessed December 31, 2015, http://www.primedatabase.com/

Figure 6.2: IPO Volumes in India since 2003–04 (₹ crore)



Source: SEBI Data in 2015-16 is till November 2015

While the 2003-04 data continues to reflect the after effects of the 2001 dotcom crisis, the IPO markets in India grew sharply during the 2005 to 2008 period. The sharp drop in 2008-09 mirrors the freeze in the global credit markets whereas between 2009 and 2011, India (and some larger emerging markets) seemed immune to the broader crisis in the developed markets. In 2010-11, low interest rates and negative equity market returns in developed countries encouraged both local and foreign funds to invest heavily in the Indian markets and the IPO market showed a surprising resilience by inching closer to its 2007-08 peaks. Nonetheless, between 2011 and 2015, the GFC's prolonged, spillover effects impeded the growth of the Indian markets. The total IPO volume was a meager ₹16,614 crore – significantly lower than the FY 2010-11 total IPO volume of ₹33,097 crore. However, the current fiscal year's data look promising again. Optimism about the new government's policy developments, improving global economy and credit market conditions have resulted in 220 percent increase in IPO volumes by November 30th, 2015.

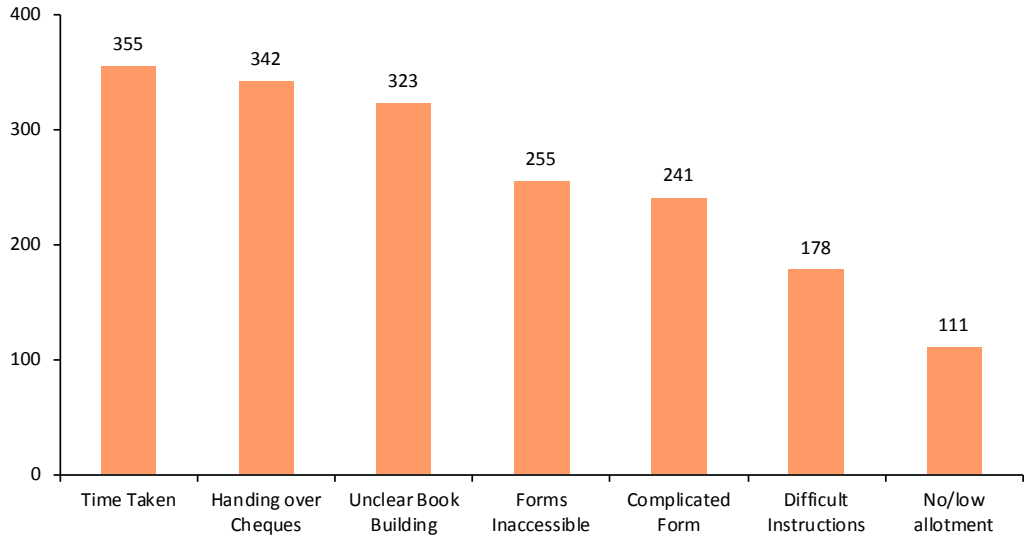
Interest in IPO amongst Investors

A small percentage of the Indian investors participate in the IPO process and this community has never been analyzed in detail[51]. According to the 2015 SIS data, while 15 percent of survey participants are investors and out of these, 18 percent have invested in IPOs, just 17 percent of investors consistently participate in IPOs. Thus, a mere 3 percent of all survey participants have invested in IPOs. The SIS data shows that among survey participants, 948 out of a total 5,356 investors regularly invest in IPOs and 957 have participated in the IPO process at least once. On an average, the median IPO investor invests in one IPO per year.

While it is undeniable that Indian IPOs have expanded phenomenally in 2015 with an IPO growth rate higher than any other large market, it is also true that the market baseline is much lower than that of China or other developed markets[52]. Since primary market is a direct source of liquidity for companies and also act as a barometer for credit flows in the broader economy, it is vital that the regulators ensure the accessibility of these markets. However, according to the SIS data, over 73 percent of the surveyed regular IPO investors perceive the IPO investment processes of book building and cheque clearances together with the protracted time spent on the entire process from application to allotment to be complicated and cumbersome. As detailed in Figure 6.3, investors are not only ambiguous about the process of book building and have significant concerns with the long-drawn-out time the process demands, they are also apprehensive about specific tasks like the handing over of physical cheques to unknown persons and the inaccessibility of forms. Surprisingly, the SIS data confirms that although nearly 84 percent of regular IPO investors and 25 percent of all investors are aware that forms and prospectus are available online; yet, despite rising urban Internet penetration, there seems to be little 'faith' in using the Internet for matters related to IPO investments. It should be noted here that over the past year, during the course of the writing of this report, SEBI has made significant changes in the IPO process and has already addressed many areas that caused concern amongst SIS 2015 participants.

51. Amey Pramodkumar Kansara, "Where are India's Retail Investors?", The Market Mogul, December 15, 2015, last accessed December 30, 2015, http://themarketmogul.com/indias-retail-investors/
52. Ernst and Young, EY Global IPO Trends 2015 4Q, (New York: EY, 2015), last accessed March 17, 2016, http://www.ey.com/Publication/vwLUAssets/EY-global-ipo-trends-2015-q4/$FILE/EY-global-ipo-trends-2015-q4.pdf

Figure 6.3 – Difficulties of Investing in IPOs

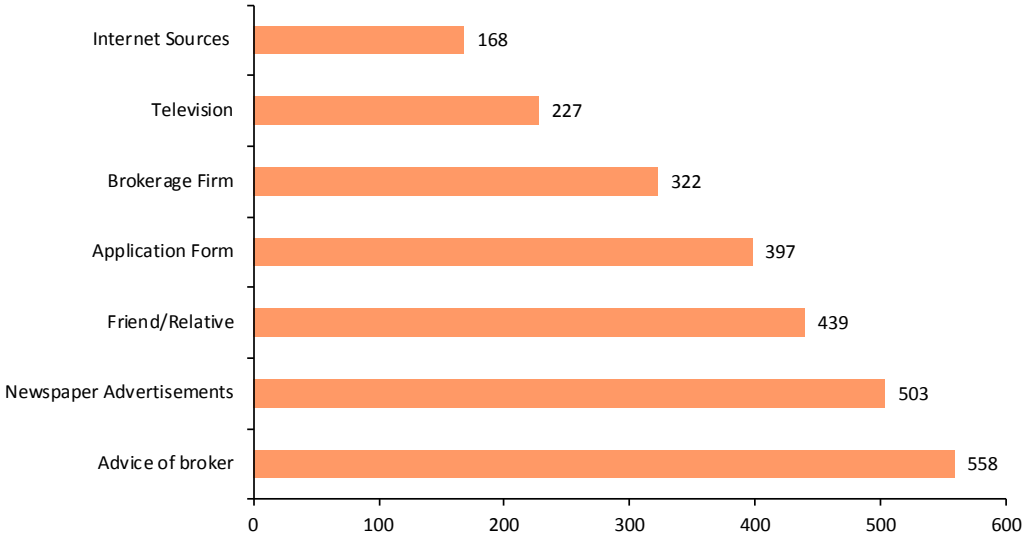


N=948 (regular IPO investors, SIS 2015)

A deeper analysis of the SIS data can lead to the inference that a reliance on traditional sources of information and advice (i.e., brokerages and newspapers) despite the large-scale closure of brokerages and the Internet's appropriation of information is possibly hampering the growth of the IPO markets. A close examination of information accessibility and the difficulties associated with the application process provide clarity on approaches to help expand IPO market participation rate.

According to the SIS data, although new media and television are relevant for information dissemination, newspaper advertisements still remain the most popular source of information. In comparison, a mere one third of investors rely on the Internet while two third of investors depend on the television. Keeping this analysis in mind, outreach efforts to popularize primary markets investments should be optimized. Additionally, as Figure 6.4 clearly illustrates, while a retail investor's personal contacts are an important information source, with 59 percent of investors depending on brokers, it is still the brokerage business that is the primary source of information on IPOs.

Figure 6.4 – IPOs: Information Sources



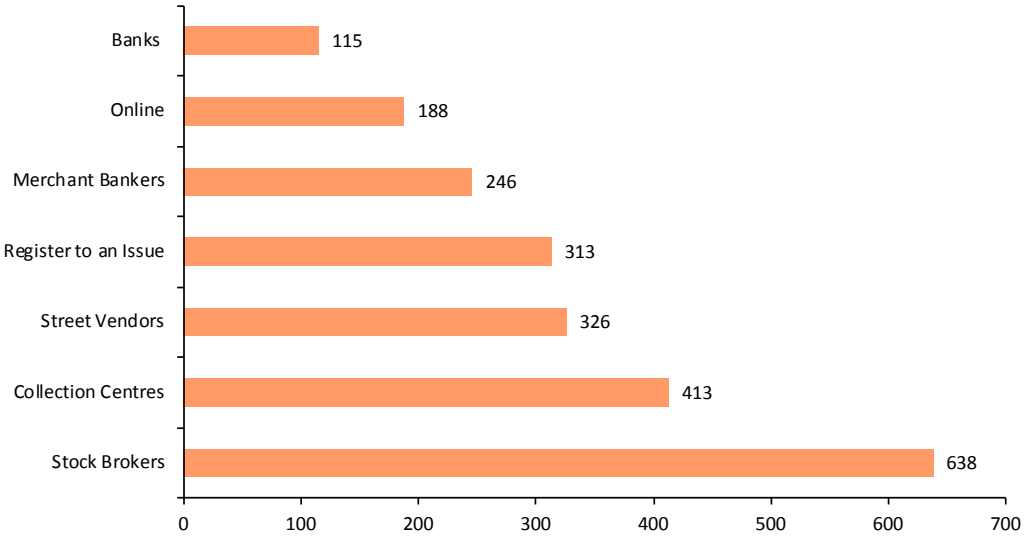
N=948 (regular IPO investors, SIS 2015)

A close analysis of the process by which IPO application forms are sourced and distributed underlines the significance of the financial intermediaries. To encourage transparency and accessibility, online applications of IPO forms have recently been encouraged, and yet, the SIS data confirms that stockbrokers still tenaciously endure as the primary source of these forms to most investors.

Figure 6.5 ratifies that online sources of application forms are amongst the least prevalent access points and it is the brick and mortar sources that are the most widespread. Currently, online forms are used half as frequently as street vendors and virtually every applicant sources the application forms either directly from their broker or from the "registrar of the issue", or through various collection centers.

53. SEBI, Frequently Asked Questions on Application Supported by Block Amount (ASBA) Facility, Mumbai: SEBI, last accessed March 17, 2016, http://www.sebi.gov.in/faq/asbaprocess.pdf

Figure 6.5 – IPO Application Forms: Sources



N=948 (regular IPO investors, SIS 2015)

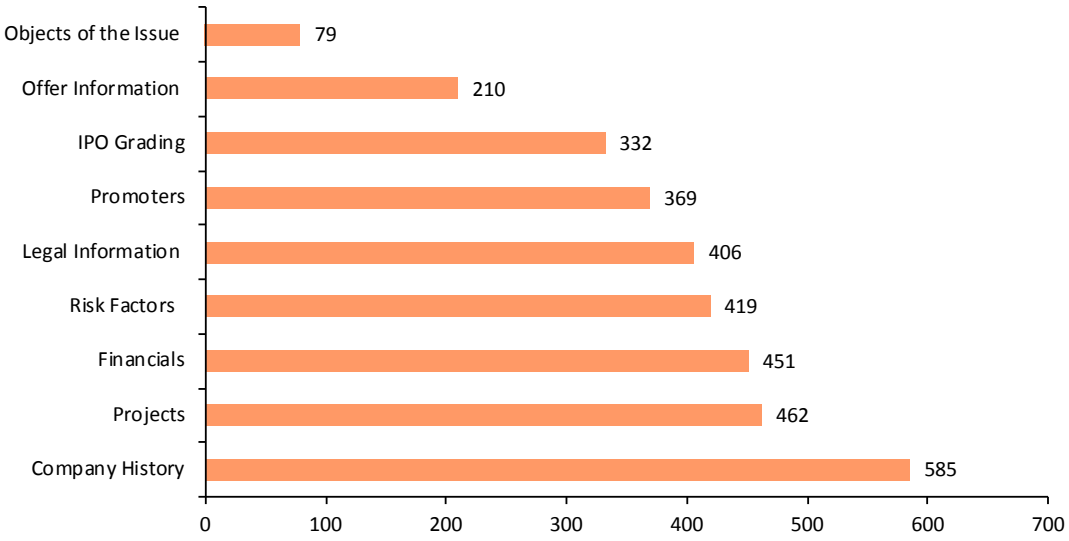
As the SIS 2015 data has previously established, the stockbroker community very closely supports the initial step towards applying for an IPO – the application form. Nonetheless, when questioned closely about the prospectus and its specific sections, although almost all the IPO applicants affirmed that they had reviewed the prospectus, and yet, almost half were unable to recall its sections accurately. This hesitancy may signal that the investors depend primarily on their brokers, not only for the physical copy of the form but also for interpretation and dissemination of the essential information contained in the prospectus itself. Disturbingly, since investors tend to focus more on company's history as opposed to current risk factors, balance sheet strength and growth potential (as Figure 6.6 points out) are thus the broker's inherent biases[54]—rather than the investor's personal assessment of the new issue—may strongly affect the decision-making process.

According to the US Securities and Exchange Commission, "This year's top-performing mutual funds aren't necessarily going to be next year's best performers. It's not uncommon for a fund to have better-than-average performance one year and mediocre or

54. Refer to Chapter 8 for detailed data and analysis regarding investor-broker relationships

below-average performance the following year. That's why the SEC requires funds to tell investors that a fund's past performance does not necessarily predict future results"[55]. Notwithstanding similar disclaimers in India, in their retrograde focus, investors ignore the ubiquitous regulatory caution that past performance is not necessarily a prediction of future outcome. Arguably the easiest heuristic to utilize, investors expect future performance to exactly mirror past successes/failures.

Figure 6.6 – Part of Prospectus read by IPO Investors



N=948 (regular IPO investors, SIS 2015)

According to the SIS 2015 survey, in case of grievances in the IPO process, investors commonly contact their brokers (22 percent) whilst about 9 percent go unreported. The data shows that investors also tend to reach out to SEBI (22 percent) and the Stock Exchanges (18 percent) and just 13 percent of grievances get to the company directly. This showcases a faith in the regulators and exchanges that is essential for market functioning while, yet again, lays emphasis on the role of the financial intermediaries in the urban Indian context. In spite of the impediments discussed above, the SIS data confirms that Indian investors demonstrate an intuitive wisdom by investing in IPOs for a holding period that is less than three years. Table 6.1 showcases

55. Securities and Exchange Commission, Fast Answers: Mutual Funds, Past Performance, July 28, 2010, Washington DC: SEC, last accessed March 26, 2016, https://www.sec.gov/answers/mperf.htm

the varied holding periods of IPOs and highlights the different timelines of investors – in primary markets. Academic research in finance proves that globally, IPOs outperform the broader indices in short-term returns[56]. In the Indian context, an investment horizon of two years is optimal and beyond that, the excess returns from IPOs slowly dissipate[57]. With more than 60 percent of IPO investors exiting their investments in less than one year and more than 90 percent exiting within three years, Indian investors demonstrate an intuitive wisdom by investing in IPOs for a holding period that is less than three years.

Table 6.1 – Holding Period of Equities Purchased through the IPO Process

Holding Period	Frequency	Percent	Cumulative
< 6 Months	226	23.6%	23.6%
6–12 Months	353	36.9%	60.6%
1–3 Years	316	33.1%	93.6%
> 3 Years	61	6.4%	100.0%
Total	956	100.0%	

N=956 (IPO investors, SIS 2015)

56. The seminal paper is Ritter, Jay R, "The Long-Run Performance of Initial Public Offerings", The Journal of Finance 46, no. 1 (1991): 3–27
57. Seshadev Sahoo and Prabina Rajib, "After Market Pricing Performance of Initial Public Offerings (IPOs): Indian IPO Market 2002–2006", Vikalpa, 35, no. 4 (2010): 27

07 MUTUAL FUNDS: INVESTOR BEHAVIOUR AND INVESTMENT PATTERNS

KEY FINDINGS

- **Of the SIS 2015 data's total investor base, 66 percent (or 3,536) have invested in mutual funds (MF), making it the most popular investment instrument amongst Indian investors.**
- **Among the 3,536 mutual fund investors, 1,494 are regular MF investors.**
- **Like other securities markets information sources, MF investors also find out about new offerings or existing mutual funds primarily through newspapers (56 percent).**
- **Although most investors (88 percent) are aware that MFs can be bought online, the Internet is neither a primary soruce of information for MFs (only 24 percent use it) nor it is a primary method of investing in MFs. Additionally, 24 percent of investors use exchanges and exchange plaforms to invest in MFs.**
- **Traditional means of investing like using MF distributors, collection centres or investing directly through the MF remain the most popular.**
- **With nearly 60 percent of regular MF investors using SIPs to invest in MFs, the recent popularity of SIPs is palpable.**
- **Although 58 percent claim that they will hold on to their MF investments in times of market volatility, less than a quarter of investors continue with their MF investments beyond a three-year period.**
- **Almost all MF investors look through the SID - Scheme Information Document. Risk Factors (68 percent) and Scheme Highlights (51 percent) are the most widely read while a mere 31 percent read through the Past Performance details.**
- **The primary problem in the MF investment process is the non-accessibility of forms (35 percent).**
- **In cases of grievance, most investors reach out to SEBI (64 percent).**

Chapter Rationale

Mutual funds, the most popular investment instrument amongst Indian investors, are diversified financial instruments that provide high quality, long-term, risk-adjusted returns for retail investors. Although investors seem to have realized that these funds help optimize their portfolio (66 percent of investors have invested in it) yet a holistic overview of the population that includes all investors and non-investors shows that a meagre 10 percent of urban respondents have invested in mutual funds. Additionally, although most mutual fund investors claim that they will hold on to their investments in times of market volatility, in reality, less than 1 percent of investors continue with that particular MF investment beyond a three-year period.

Whether it is in acquiring information from conventional sources like newspapers (and not the Internet) or in using old-style methods for investing like MF distributors and collection centres or investing directly through the fund itself, mutual fund investors continue to follow traditional paths of investment. In fact, 35 percent of investors believe that the primary problem in the MF investment process is the non-accessibility of forms and yet, 88 percent are aware that the entire MF investment process is available online. However, with nearly 60 percent of regular MF investors using Systematic Investment Plans (SIPs) to invest in MFs, it seems that the modern day, automated investment process has resonated with the investors. Furthermore, almost all MF investors look through the Scheme Information Document (SID) with Risk Factors (68 percent) and Scheme Highlights (51 percent) being the most widely read while a mere 31 percent read through the Past Performance details. MF investors appear savvy enough to realize that past performance of a fund is not a guarantee of future success.

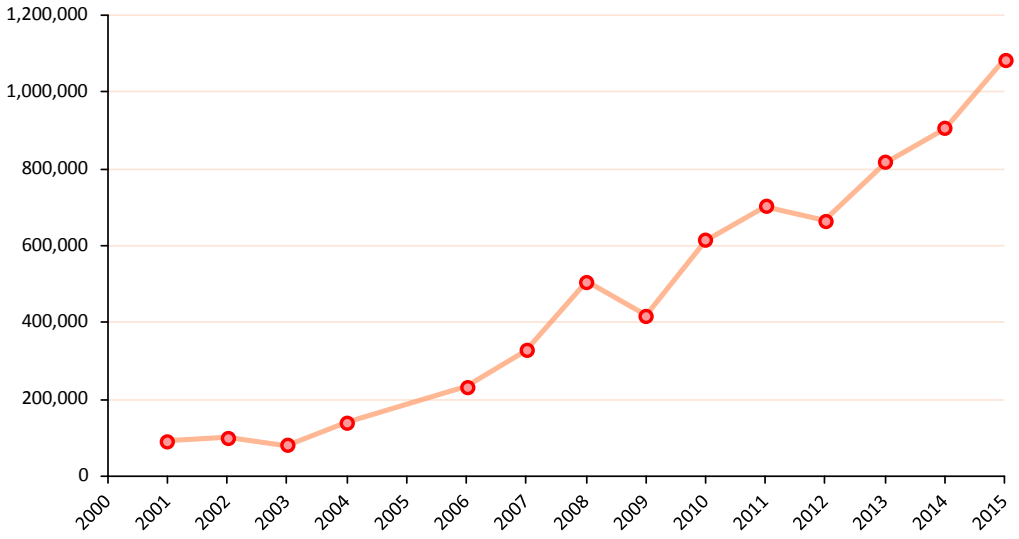
Introduction

The US Securities and Exchange Commission's guide for mutual fund investors enumerates four advantages of investing in MFs: Professional Management, Diversification, Affordability and Liquidity[58]. Among these, diversification offers a crucial and straightforward advantage to a household's portfolio. Unlike a single

58. Securities and Exchange Commission, Office of Investor Education and Advocacy, "Mutual Funds: A Guide for Investors", 2010, last accessed March 30, 2016, https://investor.gov/sites/default/files/mutual-funds.pdf

security/asset portfolio, a portfolio with assets or securities that have limited correlation to each other can lead to higher returns but lower risk[59]. Mutual fund unit holders can participate in multiple underlying assets (stocks, bonds or even commodities) whose returns are not fully correlated, and thus, provide higher risk-adjusted returns[60]. It is encouraging that these benefits have been realized by retail investors and investments in the mutual fund (MF) industry has shot up since liberalization of that market. The Indian MF industry has significantly changed since private sector funds were allowed to enter the market in 1993. In 2002, the 1963 UTI Act was repealed. From February 2003, the market as a whole moved to the next level. The AUM has grown nearly 12 times since then[61] – an increase of 280 percent in the next 10 years.

Figure 7.1: Assets under Management of the Indian Mutual Fund Industry (in ₹Crore)



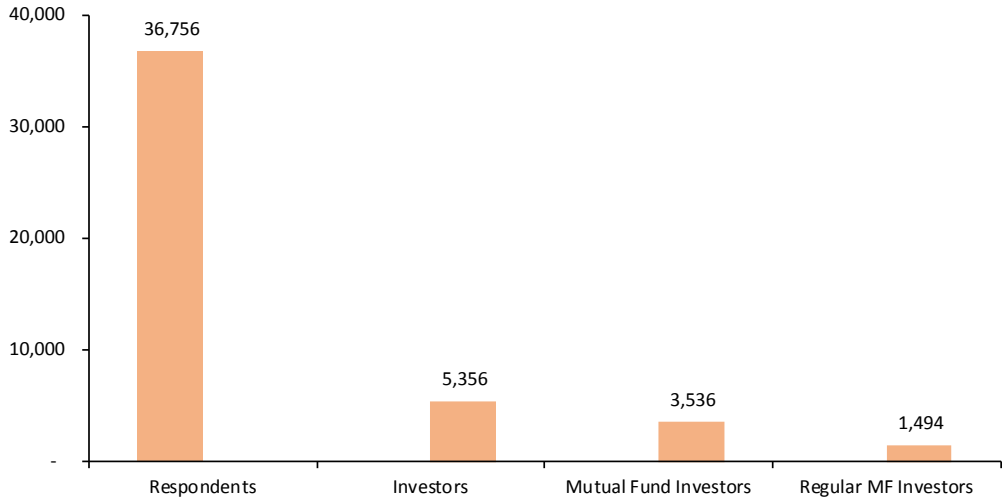
Source: Association of Mutual Funds in India (AMFI)

The SIS 2015 data confirms that the MF industry has grown sharply and that MFs are the most popular investment vehicle among the survey respondents with 66 percent of investors participating in that market.

59. Harry Markowitz, "Portfolio Selection", The Journal of Finance, Vol. 7, No. 1, March 1952, pp. 77–91
60. Harry Markowitz, the father of modern portfolio theory, first investigated portfolio diversification benefits (for which he received the Nobel Prize in Economics) in 1990. His Nobel lecture is available at: http://www.nobelprize.org/nobel_prizes/economic- sciences/laureates/1990/markowitz-lecture.pdf, last accessed December 30, 2015
61.Association of Mutual Funds in India, "Mutual Fund History", last accessed January 9, 2016, https://www.amfiindia.com/research- information/mf-history

Indian investors certainly seemed to have realized that these funds help optimize their portfolio. However, an all-inclusive overview of the population that includes all investors and non-investors shows that a meagre 10 percent of the entire urban surveyed pool invests in MFs (Figure 7.2).

Figure 7.2: Mutual Fund Investors as a Proportion of Total Respondents



Source: SIS 2015

According to the SIS 2015, 58 percent of regular MF investors affirm that they will continue to remain invested in MFs during times of market volatility. Since short-term price movements are not representative of the longer-term holding period returns of a MF, this is certainly an astute decision. However, according to Table 7.1, just 22 percent of investors hold on to their MFs for more than 3 years whereas more than half of them (57 percent) invest for less than a year. This is analogous to the AMFI data[62] that shows that 47 percent of MF investors stay invested in the same scheme for less than a year while 36 percent invest for holding periods longer than 3 years. Since benefits of equity or mutual funds holdings are especially realized when held

62. Association of Mutual Funds in India, Folio and Ticket Size, June 2015, last accessed November 6, 2015, https://www.amfiindia.com/Themes/Theme1/downloads/home/folio-and-ticket-size.pdf

in the long run, this quick turnover of MF investments indicates an obvious sign of investor impatience – i.e., when investors engage in profit making too quickly or offload their investments too early due to downward market trends.

Table 7.1: Holding Duration of Mutual Funds

MF Holding Duration	Percentage	Cumulative
< 6 Months	38.0%	38.0%
6–12 months	19.0%	57.0%
1–3 Years	21.0%	78.0%
> 3 Years	22.0%	100.0%

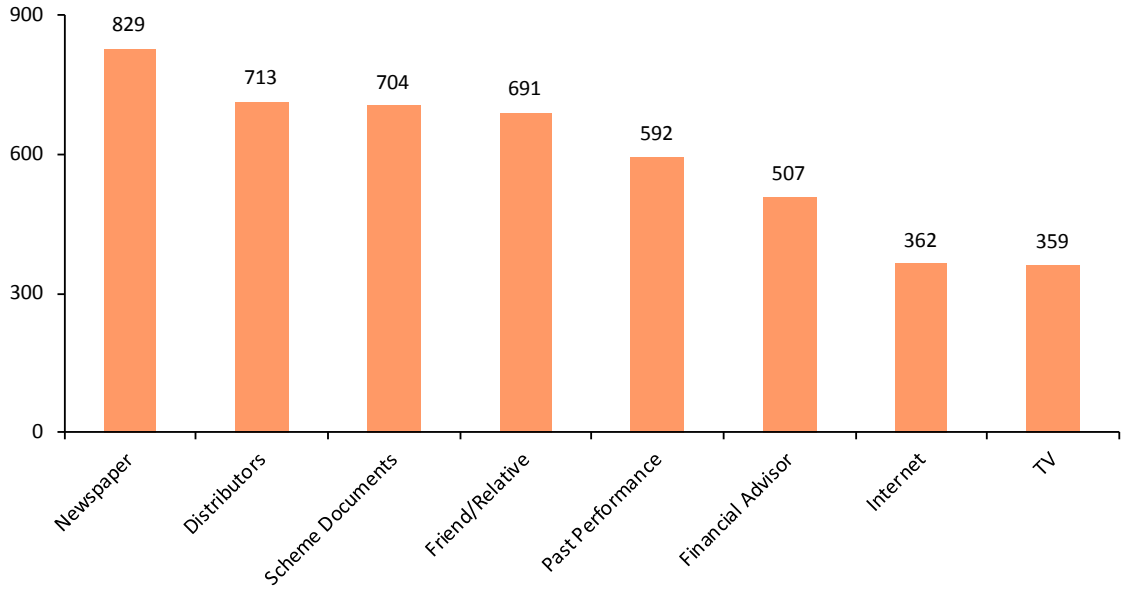
N=1,494 (all urban, regular MF investors, SIS 2015)

Information Sources

While Internet penetration is increasing in India (10 percent of the population from December, 2011 to 35 percent of the population in March, 2016)[63], it has remained a young person's domain with 75 percent of Internet users below the age of 34, 16 percent of users in the 35-44 years range, and only 9 percent users over the age of 45[64]. Since Indian investors tend to be older (average age of surveyed investors is 41 years), despite the rising Internet penetration in India and the large television audiences in the country, information flow concerning mutual funds and new fund offerings are still controlled by traditional news sources. According to the SIS 2015 data (see Figure 7.3), although 55 percent of investors acquire information concerning MFs from newspapers, a mere 24 percent use the Internet to receive information while an equal percentage procures this information from the television.

63. Internet Live Stats, Internet Users by Country (2016), last accessed March 23, 2016, http://www.internetlivestats.com/internet-users-by-country/
64. Statista, Distribution of Internet Users in India as of September 2013, by Age Group, last accessed March 20, 2016,

Figure 7.3: Information Sources about Mutual Funds



N=1,494 (all urban, regular MF investors, SIS 2015)

As discussed in Chapters 4 and 6, this pattern of Internet equivocation for investment matters stems from a variety of reasons like age and investor awareness while cyber security maybe an important concern too. SEBI (as a member of IOSCO) has adopted the "Principles for Financial Market Infrastructures (PFMIs) laid down by CPMI-IOSCO" on cyber security[65], there have been no reports of hacking of Indian trading accounts and the Indian customers are certainly becoming more comfortable with e-commerce[66], and yet, purchasing financial products online is evidently still not popular[67]. Indian markets have not yet seen the confidence-building measures taken by financial intermediaries in developed countries (through identity theft protection guarantees)[68].

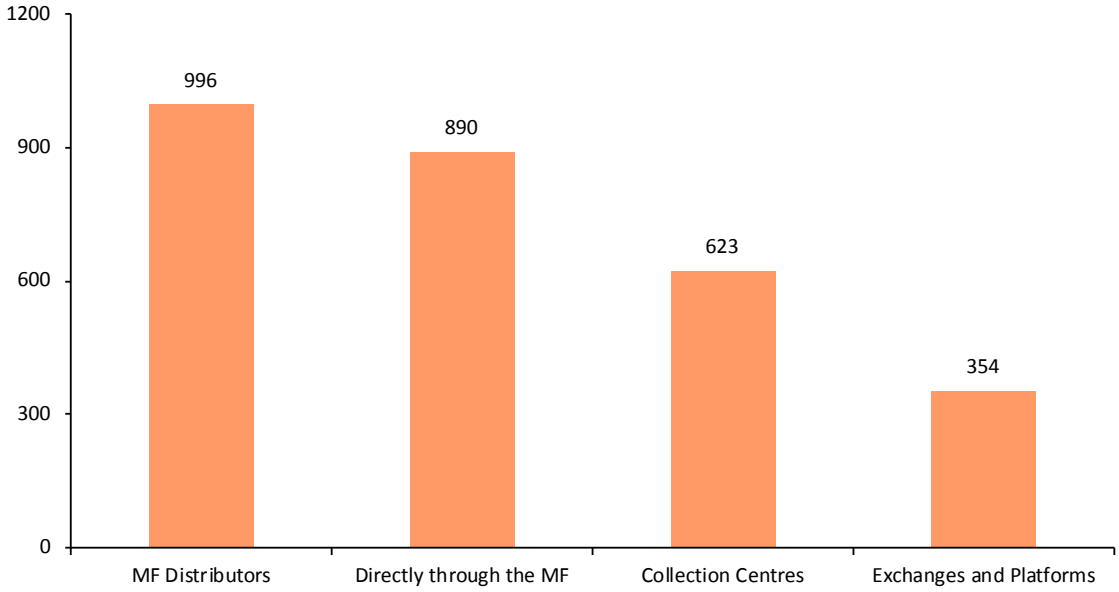
Whether it is acquiring information from conventional sources like newspapers, or in using old-style methods for investing like MF distributors and collection centres, or investing directly through the fund itself, mutual fund investments continue to follow traditional paths of investment. The influence of financial intermediaries and

65. SEBI, Circular: Cyber Security and Cyber Resilience Framework of Stock Exchanges, Clearing Corporation and Depositories, July 6, 2015, last accessed January 11, 2016, http://www.sebi.gov.in/cms/sebi_data/attachdocs/1436179654531.pdf
66. Statista, Digital Buyer Penetration in India from 2011 to 2018, last accessed April 9, 2016, http://www.statista.com/statistics/261664/digital- buyer-penetration-in-india/
67. Fidelity Customer Protection Guarantee, last accessed February 9, 2016, https://www.fidelity.com/security/overview
68. Scottrade, Secure Online Investing & Identity Theft Protection, last accessed February 9, 2016, https://www.scottrade.com/online-

word of mouth marketing are also extremely important in this market. The SIS data confirms that 48 percent of investors gather information regarding mutual funds that are available in the market from friends and family while 47 percent rely on MF distributors for this information. See Chapter 4 for similar discussions on broader investment markets and Chapter 6 on IPOs that details in what way the investment markets are dependent on traditional media and financial intermediaries for information and application forms. Although regular MF investors who were surveyed in this section, also display corresponding lack of internet savviness and yet, most (88 percent) are aware that MFs can be purchased online (and thus, the MF details and application forms are available on the internet).

However, change is imminent in the industry and ease of use will usher in the direction of online securities markets. The easy investment plans available using SIPs is arguably a harbinger of that change. While the SIS 2015 data finds low Internet usage for trading stocks, MFs (see Figure 7.4) and IPOs, nearly 60 percent of regular MF investors are using SIPs to invest in MFs.

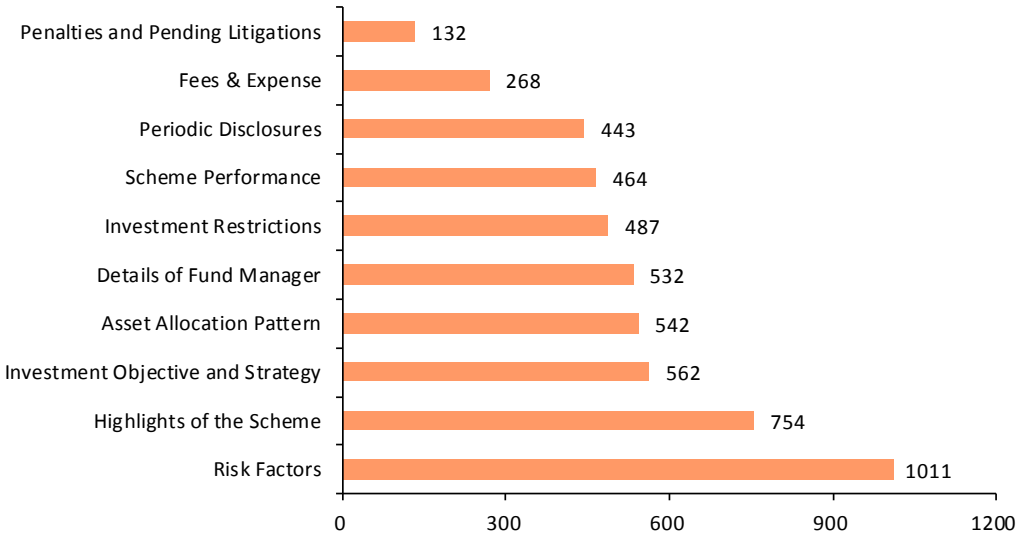
Figure 7.4: Mutual Funds Investment Channels



N=1,494 (all urban, regular MF investors, SIS 2015)

While investors are not always rational in their information sourcing (as seen above) or financial decision-making (as seen in Chapter 9), most MF investors read the relevant sections of the SID (Figure 7.5). 68 percent of respondents read through the Risk Factors in the SID while 51 percent study the Scheme Highlights – the two primary sections that contain most of the valuable information for the retail investor. Regular MF investors seem to understand the risk benefits of investing in MFs. This risk-averse rationality is also reflected in the SIS data, which shows that 31 percent of investors read about the Past Performance of the relevant funds. Savvy investors who appear to be aware of risk metrics and scheme details while taking their investment decisions are also aware of the often-repeated warning that past performance is not a guarantee of future results.

Figure 7.5: Parts of SID read by Investors

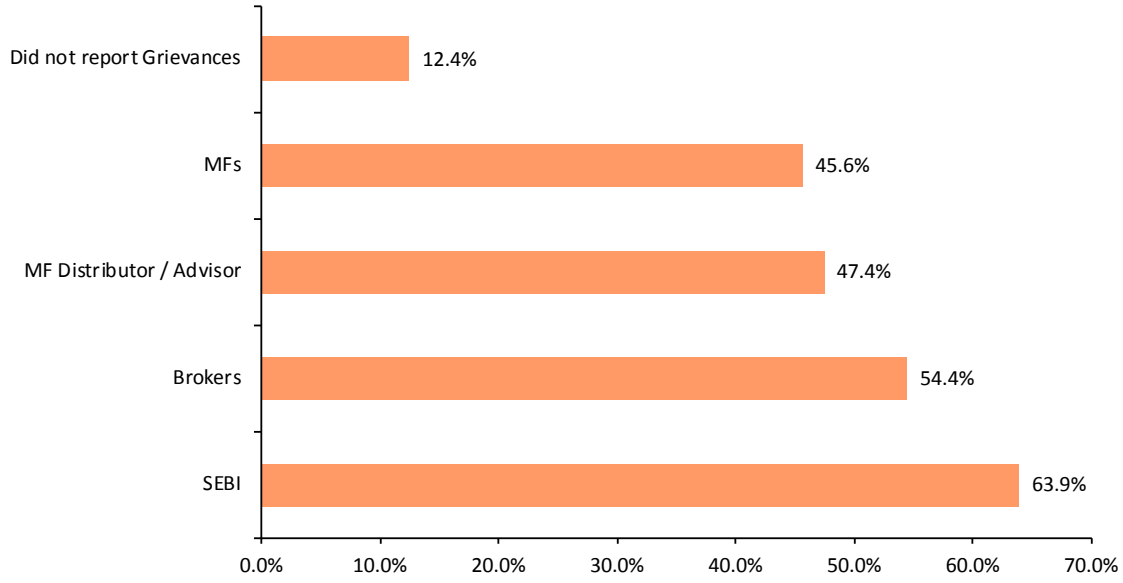


N=1,494 (all urban, regular MF investors, SIS 2015)

As Chapter 4 underlines in detail, most investors reach out to SEBI for any markets-related grievances. This substantiates the fact that SEBI is recognized as the primary regulator of the securities markets and that its outreach efforts have had a positive impact on the investor population. Similarly, in cases of complaints concerning mutual funds, 64 percent of investors register their grievances with SEBI, which is significantly

more than those who reach out to their brokers (54 percent), the MF distributors (47 percent) or the MFs themselves (46 percent). However, the SIS data shows that about 12 percent of the grievances are not reported at all and thus, relevant industry bodies and regulatory institutions should try and ensure that a more robust outreach program addresses and resolves all complaints (see Figure 7.6).

Figure 7.6: Grievance Registration Amongst Mutual Fund Investors



N=1,494 (all urban, regular MF investors, SIS 2015)

Mutual funds are the most popular investment vehicle for Indian investors and that is indeed good news for SEBI as these instruments provide significant risk reduction benefits due to diversification. This section was a detailed questionnaire for those investors who regularly participate in the MF market to understand their reasons for participation and also their problems and challenges with this market. It is clear from the SIS 2015 data that the awareness programs in this area of securities market has truly had a significant effect in the past decade with investors acting rationally in many aspects of the market, except arguably holding their investments for a shorter period than necessary to truly gain from the long term growth of the securities market.

08 INVESTORS AND MARKET PARTICIPANTS

KEY FINDINGS

- **The investor base in India is increasing; nearly 75 percent of the investors in SIS 2015 participated in the securities markets for the first time within the last five years.**
- **Although retail participation is rising, most retail investors trade either weekly or monthly and institutional algorithmic trading (computerized, automated trading) accounts for an increasing percentage of trades in the exchanges.**
- **Limited retail trading frequency, rising Internet penetration and a surge in the number of Authorized Persons (AP) is significantly altering the traditional dynamics of the brokerage industry. Smaller brokers are either disappearing or are merging to form larger and more stable consolidations.**
- **Despite a growing dependence on online technology in India, a mere 22 percent of investors use the Internet to place their trades while a staggering 78 percent continue to 'call in' their trades.**
- **While most investors do not trade online due to a lack of awareness about the procedures related to online trading systems, there is significant technology aversion and inertia as well.**
- **Demonstrating a reliance on brokers and sub-brokers, more than 70 percent of investors depend on financial planners and maintain running accounts/standing orders with their brokers.**
- **SIS 2015 concludes that it is the Indian investor's emphasis on service quality and financial reliability (rather than brokerage charges or physical proximity) that is instigating the smaller brokers to consolidate into larger, more robust establishments.**
- **Although 90 percent of investors are aware that this is not a mandated ruling, 66 percent provide their financial intermediaries with a Power of Attorney (PoA).**
- **Despite a strong relationship with the broker, retail investors continue to primarily trust their own judgment when making investment decisions.**

Chapter Rationale

The investor base in India is increasing; the SIS survey finds that within the last five years, nearly 75 percent of investors have participated in the securities markets for the first time. Nonetheless, rising volumes in the stock market are primarily being driven by institutional algorithmic trading (computerized automated trading) and not by retail investors who mostly trade either weekly or monthly. Limited retail trading frequency, rising Internet penetration and a surge in the number of Authorized Persons (AP) is critically affecting the brokerage industry. The traditional dynamics of the industry are changing since smaller brokers are either disappearing or merging to form larger and more stable consolidations. However, despite a growing dependence on online technology in India, according to the SIS data, only 22 percent of investors use the Internet to place their trades while a staggering 78 percent continue to 'call in' their trades. Underlining their reliance on brokers and sub-brokers, more than 70 percent of investors depend on financial planners and maintain running accounts/ standing orders with their brokers. While it is true that the Indian brokerage industry's traditional structure is also shifting, the survey seems to conclude that it is not the Internet but the Indian investor's emphasis on service quality and financial reliability that is instigating the smaller brokers to consolidate into larger, more robust establishments. Since it is established reputation and financial soundness (rather than brokerage charges or physical proximity) that the Indian investor focuses on while choosing a financial intermediary, these larger firms are becoming more powerful and influential in the brokerage business. Underscoring the strong relationship with their brokers, the SIS data depicts that 66 percent of investors provide their financial intermediaries with the power of attorney, and yet, the data also unexpectedly ascertains that retail investors still primarily trusts their own selves—and not their brokers—for investment decision-making.

Introduction

The Global Financial Crisis (GFC) left a strong mark on the psyche of the individual investors. Retail investors shied away from the securities markets to invest in safer savings and capital formation instruments like gold, commodities and even bank deposits. However, US investors (the world's largest securities market) increased

their exposure to securities by over 25 percent in the five years between 2010 and 2014 and by the end of 2014, a positive change in sentiment was palpable across the globe. In spite of the rising rate of investment in financial instruments, the total number of US households with brokerage accounts decreased during the same period. Technological advances are rapidly changing the global brokerage business. A close analysis of long-term trend data underlines the Internet's effect on US brokerage houses: from 19.4 million (18.2 percent) households with brokerage accounts in 2001 to 17.2 million (14 percent) household with brokerage accounts in 2014[69]. Similarly, although the penetration of securities markets is increasing in India, a large number of brokerage houses are closing down.

Trading Patterns

The investor base in India is gradually expanding. According to the SIS survey, nearly 75 percent of investors have participated in the securities markets for the first time within the last five years. Table 8.1 showcases the data of 4,305 investors, which is roughly, the entire pool of investors in this survey. Most of the investors have been investing in the markets for less than 5 years; however, the data also show a sizeable number of investors who have been investing for 6 to 10 years and a smaller sample of investors in the 15+ years of experience in the markets.

Table 8.1 – Number of Years Participating in the Securities Markets

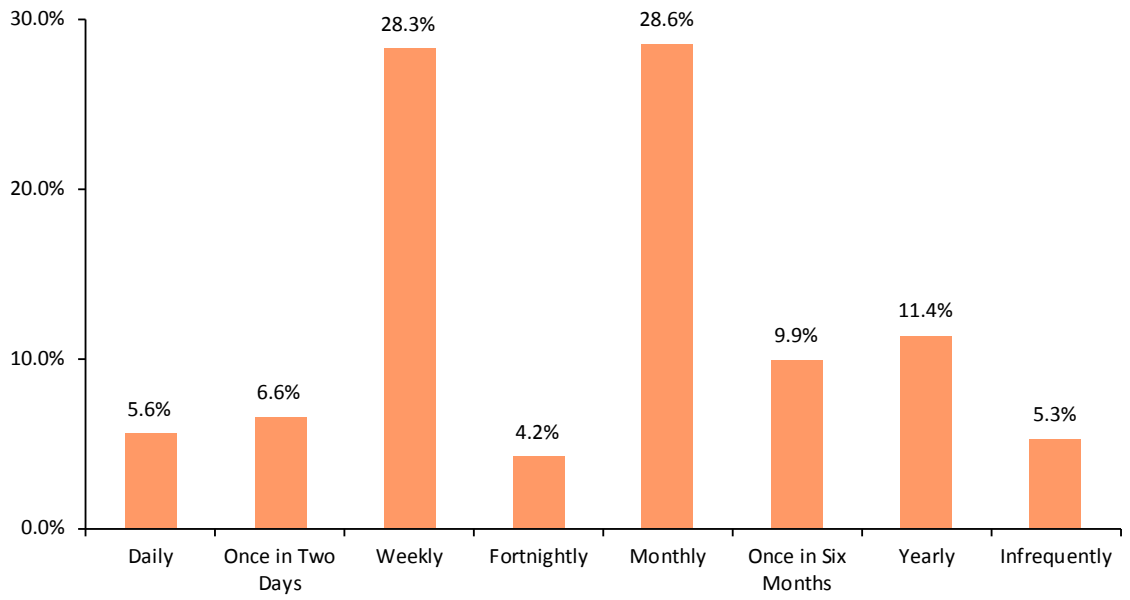
Years in the Market	Frequency	Percentage	Cumulative
1 to 5	3100	74.8%	74.8%
6 to 10	1047	21.6%	96.4%
11 to 15	125	2.7%	99.1%
16 to 20	23	0.3%	99.4%
20+	10	0.6%	100.0%

N=4,305 (subset of urban investors who responded, SIS 2015)

69. Constantijn W. A. Panis and Michael Brien, Brokerage Accounts in the United States, November 30, 2015, Advanced Analytical Consulting Group and Deloitte, last accessed 20 March, 2016, https://www.dol.gov/ebsa/pdf/brokerageaccountsintheus.pdf

As on 31st March 2015, algorithmic trading (computerized automated rules based trading, largely used by institutions) accounted for more than 40 percent of all trades in the Indian stock exchanges, and thus, encompassed a significant portion of the rising volumes. While many retail traders have day-traded during their time in the markets (about 40 percent), most investors do not trade as often. The distribution of trading frequency is multimodal with about 30 percent trading once a week, another 30 percent of investors trading once a month, and only 6 percent trading every day. This is definitely desirable for policy makers (though not necessarily brokers) since excess trading in the retail market leads to high transaction costs and thus, lower returns for the small investor.

Figure 8.1 – Trading Frequency amongst Investors



N=5,356 (all urban investors, SIS 2015)

Table 8.2 tabulates the frequency with which investors follow the market and shows, surprisingly, that despite the very low number of investors who trade daily, 18 percent of investors follow the market everyday. At par with the 44 percent who trade more than once a month, a little over 50 percent track the markets at least once a week. This equivalence remains pretty robust over longer time periods as well, leading to the obvious conclusion that investors who trade more frequently tend to follow the markets more regularly.

Table 8.2 – Investors' Market Movements Tracking Frequency

Follow Market Movement	Frequency	Percentage	Cumulative
Daily	990	18.4%	18.4%
Once in Two Days	516	9.6%	28.0%
Weekly	1318	24.5%	52.5%
Fortnightly	197	3.7%	56.2%
Monthly	1082	20.1%	76.3%
Once in Six Months	425	7.9%	84.2%
Yearly	726	13.5%	97.7%
Infrequently or Never	123	2.3%	100.0%

N=5,356 (all urban investors, SIS 2015)

Financial Intermediaries in India

In India over the past decade, brokers and market participants continue to play a large role in securities markets functions. Contrary to the Indian trend the global investors are moving to online trading and investments[70]. According to SEBI's data, as of 31st March 2015, in Indian markets there were a total of 6,147 cash segment brokers, a drop of 35 percent from the previous year's number of 9,411 (at the end of FY 2011-12, this was 10,268)[71]. The number of sub-brokers fell by 18 percent from 51,885 at the end of FY 2014 to 42,351

70. Andre Cappon, "The Brokerage World Is Changing, Who Will Survive?", Forbes, April 16, 2014, last accessed January 15, 2016, http://www.forbes.com/sites/advisor/2014/04/16/the-brokerage-world-is-changing-who-will-survive/
71. SEBI, SEBI Bulletin April 2015, last accessed February 15, 2016, http://www.sebi.gov.in/cms/sebi_data/attachdocs/1430125406381.pdf

at the end of FY 2015 (at the end of FY 2012, this was 77,141). In April 2015, the first month of FY 2015-2016, the number astoundingly dropped to 3,195 brokers and 41,625 sub-brokers. The derivative sector brokers have marginally outperformed the broader industry. According to SEBI's May 2015 Bulletin data, the number of brokers increased from 2,337 in FY 2012 to 3,031 in FY 2014 while in April 2015, the number stands at 2,810 brokers. The traditional dynamics of the industry are shifting as smaller brokers are either disappearing or are merging to form larger, more stable consolidations[72]. SEBI's data on the "Percentage Share of Top 'N' Members in Turnover in Cash Segment" shows that while the top 25 brokers accounted for 38 percent of transactions in 2008-09, the share has moved up to 51.2 percent in March 2015[73].

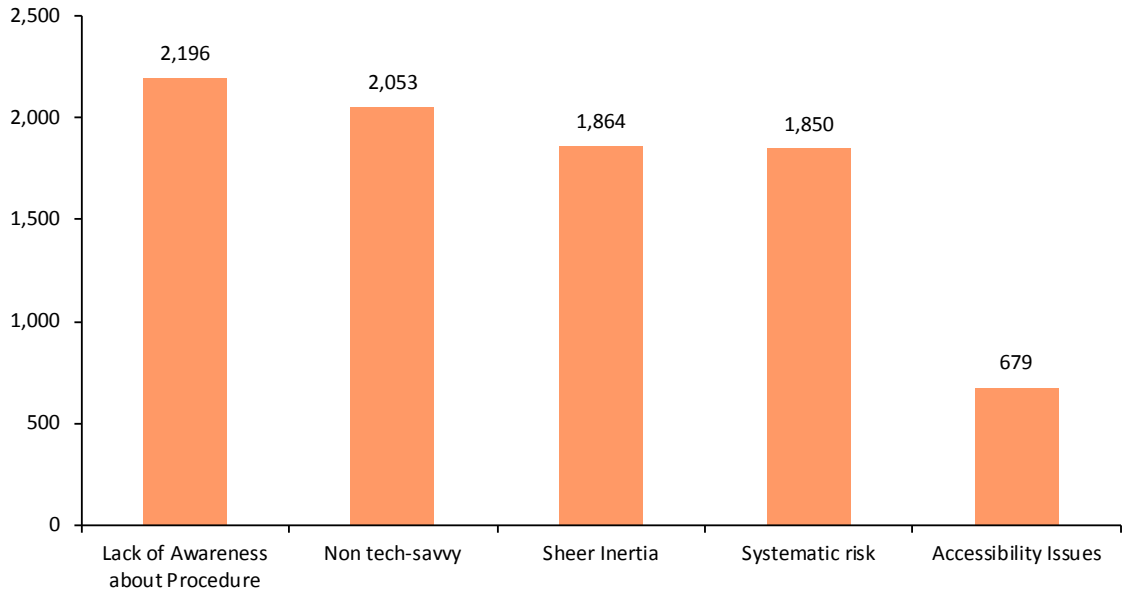
When the SIS dug deeper to try and ferret out the exact reasons for the drastic drop in the number of brokers, it seemed a wide array of factors—from limited retail trading frequency and rising Internet penetration to a surge in the number of APs and the shutting down of numerous subnational exchanges over the past year—are all critically affecting the brokerage industry[74].

Increasing Internet usage in developed markets has ensured a marked decrease in the usage of brokers and consequently, a sharp squeeze in their fee structures[75]. While Internet penetration is increasing in India (10 percent of the population from December 2011 to 35 percent of the population in March 2016)[76], it has remained a young person's domain with 75 percent of Internet users below the age of 34, 16 percent of users in the 35-44 years range, and only 9 percent users over the age of 45[77]. Since Indian investors tend to be older (average age of surveyed investors is 41 years), the continuous drop in the numbers of registered brokers and sub-brokers in India appears not to be a phenomenon that the Internet alone has generated.

Even amongst those households, which use the Internet to receive information about matters related to investments, it has not yet become the tool of choice for securities markets trading. Amongst the SIS 2015 participants, only 22 percent trade online, and yet, nearly 55 percent have traded at least once by using an Internet facility provided by their broker. Additionally, nearly 70 percent of urban investors have accessed exchange websites to gather information concerning 'terminal deactivation of brokers'. However, as Figure 8.2 points out, it is the 'lack of awareness' about the procedures of online trading that has been the prime deterrent for most investors while the 'lack of technology savviness' has also played a significant role. Other than 'sheer inertia', which is arguably true for older investors, there are also substantial fears regarding the systematic risk in online trading, which needs to be allayed by online brokers and regulators.

72. Ashish Rukhaiyar, "Shares of Larger Brokerages on the Rise", Mint, May 04, 2015, last accessed March 10, 2016,
73.SEBI, SEBI Bulletin April 2015, last accessed February 15, 2016,
http://www.sebi.gov.in/cms/sebi_data/attachdocs/1430125406381.pdf
74. Ashley Coutinho, "Brokers Shut Shop on Falling Volumes, Compliance Costs", Business Standard, January 12, 2016, last accessed January 16, 2016, http://www.business-standard.com/article/markets/brokers-shut-shop-on-falling-volumes-compliance-costs-116011200755_1.html
75. Constantijn W. A. Panis and Michael Brien, Brokerage Accounts in the United States
76. Internet Live Stats, Internet Users by Country (2016), last accessed January 23, 2016,
http://www.internetlivestats.com/internet-users-by- country/
77. Statista, Distribution of Internet Users in India as of September 2013, by Age Group, last accessed March 20, 2016,
http://www.statista.com/statistics/272394/age-distribution-of-internet-users-in-india/

Figure 8.2: Reasons for not Trading Online



N=5,356 (all urban investors, SIS 2015)

In 2009, SEBI created a new role in the securities markets—Authorized Persons (AP)—which whilst similar to a sub-broker, yet has significantly lower compliance requirements. APs simply need to register with the stock exchanges and not with SEBI. According to SEBI's data (January 2014), "it approved 13,396 surrender applications of sub-brokers between April to September, 2013. In the same period, the net addition of APs was 15,465"[78]. Additionally, the shutting down of about 20 regional exchanges that did not meet the net worth and daily turnover criteria set by SEBI affected smaller brokers in non-metro cities in FY 2014-15[79].

78. Ashish Rukhaiyar, "Shares of Larger Brokerages on the Rise", Mint, May 04, 2015
79. Sneha Padiyath, "Retail Broker Count Shrinks Further", Business Standard, June 1, 2015, last accessed March 17, 2016, http://www.business- standard.com/article/markets/retail-broker-count-shrinks-further-115060101371_1.html

Interactions with Financial Intermediary

Despite a growing dependence on online technology in India, the SIS data finds that a mere 22 percent of investors use the Internet to place their trades while a staggering 78 percent continue to "call in" their trades. Demonstrating a reliance on brokers and sub-brokers, more than 75 percent (3,378) investors maintain a running account with financial intermediaries, nearly 73 percent (3,234) investors furnish brokers and depository participants with standing instructions for transactions on their behalf, and about the same number (72 percent or 3,214 investors) use a financial planner.

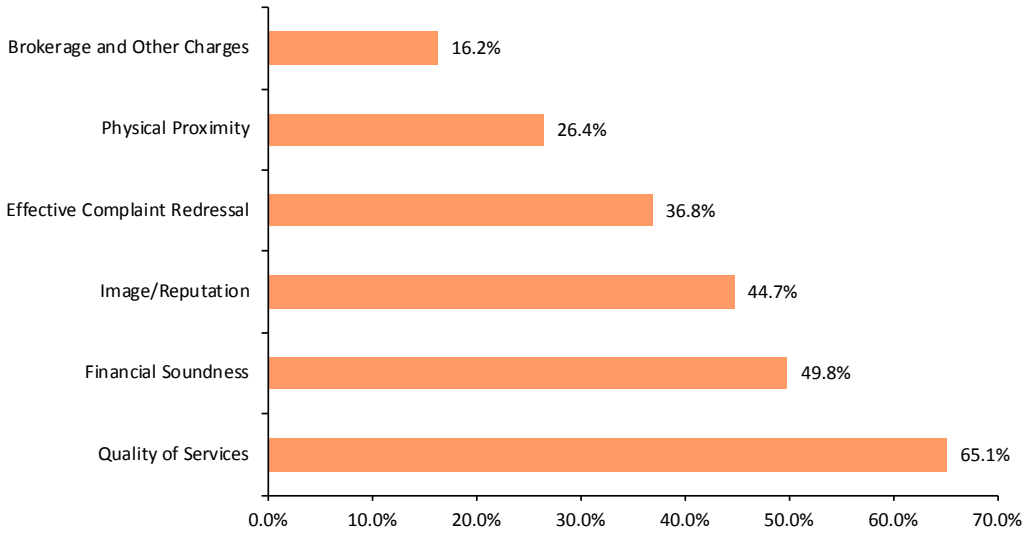
To try and understand the symbiotic relationship between investors and financial intermediaries, the SIS survey not only closely studies investor behaviour patterns but also meticulously questions investors on their rationale while choosing their financial intermediaries or brokers. Given the current state of the industry, this is a vital question for the brokerage community and regulators.

With nearly 70 percent of investors prioritizing the quality of services when determining upon a financial intermediary, Figure 8.3 clearly showcases the decision-making process of retail investors. Additionally, while 50 percent of investors deem the financial soundness of the broker to be crucial, another 45 percent focus on the broker's image or reputation. The SIS data unambiguously concludes that retail investors are particularly quality conscious and are averse to any potential counterparty risk when dealing with brokers; they would rather rely on financial reliability and brand recognition. Given the muted importance assigned to brokerage charges and physical proximity, the SIS survey determines that a larger brokerage house with a well-known brand and top quality service may outperform a local intermediary with lower costs and thus, it may be the Indian investor's emphasis on service quality and financial reliability that is instigating the smaller brokers to consolidate into larger, more robust establishments. Since it is established reputation and financial soundness (rather than brokerage charges or physical proximity) that the Indian investor focuses on while choosing a financial intermediary, these larger firms are becoming more powerful and influential in the brokerage business. The findings closely match the data observed in SEBI bulletin and the financial press – that smaller brokers are shutting shop at an alarming pace.

Underscoring the strong relationship with their brokers, over 63 percent of investors provide a Power of Attorney

to their financial intermediaries, which allows the broker/depository participant to directly debit funds and securities from their account without their explicit permission. This is indeed a large number considering the amount of leeway it can potentially provide, and the SIS data confirms that 90 percent of investors are aware that it is not essential to give this right to their intermediary.

Figure 8.3 – Reasons for Choosing a Financial Intermediary



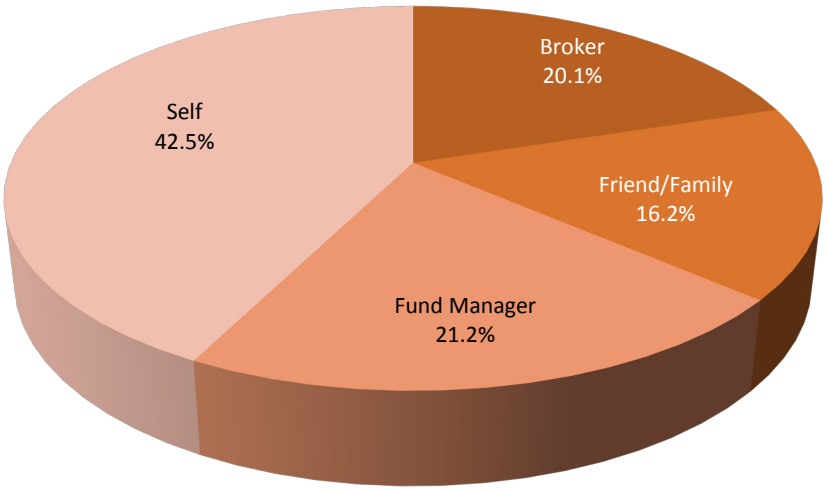
N=5,356 (all urban investors, SIS 2015)

Nonetheless, when it is time to trust someone to make an investment decision, more than 40 percent of investors depend on themselves (see Figure 8.4). This is a visible self-confidence bias indication, a much-documented phenomenon observed in behavioural finance where the individual investor makes glaring mistakes in investments resulting in a loss of wealth due to over-trading, over confidence and behavioural biases like name recognition. Barber and Odean[80] (2000) in their paper "Trading Is Hazardous to Your Wealth: The Common Stock Investment Performance of Individual Investors" note that, "Individual investors who hold common stocks directly pay a tremendous performance penalty for active trading" and "Overconfidence can

80. Brad M. Barber and Terrance Odean, "Trading Is Hazardous to Your Wealth: The Common Stock Investment Performance of Individual Investors", Journal of Finance, April 2000, Volume 5, Issue 2, pp 773–806

explain high trading levels and the resulting poor performance of individual investors." While we discuss investor perceptions and biases in chapter 9, it seems that although the SIS data documents an overwhelming dependence on financial intermediaries, the use of financial planners or fund managers are restricted where it seems to be most essential.

Figure 8.4 – Trust Vis-à-vis Investment Decision-Making



N=5,356 (all urban investors, SIS 2015)

09 HOUSEHOLD PERCEPTIONS OF FINANCIAL MARKETS

KEY FINDINGS

- **Perceptions of risk, returns and liquidity about investment instruments are not always in line with their actual risk/return/liquidity profile.**
- **Return perceptions directly align with past performance data.**
- **Liquidity perceptions are also closely in line with the actual liquidity of instruments.**
- **Due to a lack of awareness about less popular instruments, investors perceive debentures and bonds to be at a higher risk than mutual funds and equities.**
- **When the word 'risk' is mentioned, most investors equate it to 'danger', 'loss', or 'uncertainty' while just 16 percent consider it 'thrilling' and a mere 8 percent deem it as an 'opportunity'.**
- **Investors worry more about market risks like volatility and financial losses rather than operational risks like corporate governance issues and trading on insider information.**
- **While investors correctly grasp many different aspects of the securities market like direct risk-return relationship or the market capitalization-risk correlation, they also reveal certain biases like overconfidence.**

Chapter Rationale

Alan Greenspan (Governor, US Federal Reserve Bank, 1989 – 2006) famously caused the markets to crash by mentioning the phrase 'irrational exuberance' while describing the then current situation of the market. Behaviour in financial markets can be fairly irrational, which is seen in the rise and fall of equities and indices sometimes on the basis of no new information, on basis of rumours, or on the basis of information which might not have any direct or indirect bearing on the value of the stock. This bounded rationality can be seen in herding behaviour of market participants. Similar biases can be observed in investment choices. In some cases, real estate markets overheat because the price rise can be a self-fulfilling prophecy (since everyone thinks prices should go up, it does). This causes both fundamental valuation and actual prices to diverge. On the other hand, some investment options which might be optimal for an individual may be ignored completely, either due to ignorance about the instrument or due to its misplaced risk estimates.

The SIS data finds that even among households that invest, which include urban, educated and higher income clusters, perceptions of risk, returns and liquidity about investment instruments are not always in line with the actual risk/return/liquidity profile; often leading to expectations mismatch. However, Government of India (GoI) and SEBI's successful outreach efforts have increased awareness for certain instruments (like mutual funds) and consequently, most investors (66 percent) invest in diversified mutual funds which are safer and more reliable than equities (55 percent). Although the SIS respondents perceive mutual funds to have lower risk than equities, perhaps due to a lack of awareness or due to some much-publicized alleged frauds in the retail bond market[81], they consider debentures and bonds riskier than either of these instruments. This may be an effect of the increasing rate of corporate defaults[82] in India over the past two years[83]. Return perceptions, on the other hand, directly align with past performance data: equities are expected to outperform mutual funds, which are, in turn, anticipated to significantly outperform bonds. Liquidity perceptions are also closely in line with the actual liquidity of instruments.

Unsurprisingly, a close study of the risk questionnaire section shows that risk perceptions are particularly out of line with reality since most investors have a high level of risk aversion. Rather than an opportunity, risk is considered a hazard. Investors seem to be most concerned

81. Securities Exchange Board of India, Public Notice to the Investors of Sahara India Real Estate Corporation Limited and Sahara Housing Investment Corporation Limited, Mumbai: SEBI, 15 April, 2011, last accessed December 29, 2015, http://www.sebi.gov.in/cms/sebi_data/attachdocs/1304940797264.pdf
82. CRISIL Ratings, CRISIL Annual Default and Ratings Transition Study – 2014, Mumbai: CRISIL, August 2014, last accessed December 15, 2015, https://www.crisil.com/pdf/ratings/crisil-rating-default-study-2014.pdf
83. ONICRA, ONICRA Default Study 2015, Gurgaon: ONICRA, 2016, last accessed March 18, 2016, http://www.onicra.com/images/pdf/Publications/Onicra-Default-Study-2015.pdf

with market risks like volatility, which are inherent risks to investing in securities rather than more idiosyncratic operational risks, which should be the primary cause for apprehension about investing. Since most investors seem to trust their own judgment on investment decisions, these risks remain ignored, aggravating the biases inherent in financial decision-making. However, the representativeness (name recognition) bias is low among Indian investors and they demonstrate an acute understanding in certain facets of finance, which is not observed even in developed markets data. For instance, the direct relationship between higher risk and higher return seems well understood and complementarily, that small caps stocks provide the highest returns but are more risky, while large caps are less risky but have smaller returns.

Introduction

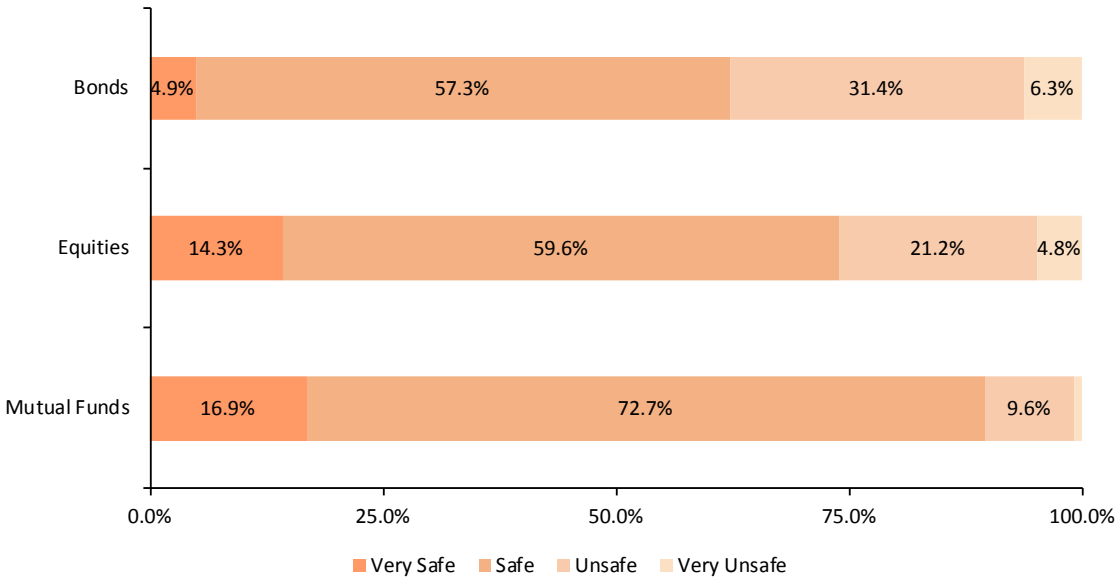
Perceptions regarding securities markets and investing are often not in tandem with reality. This is a key research problem in finance today, and the behavioural (psychological) aspects of the markets are a prime focus for academics and policy makers in the field. The vast research on behavioural economics (for which the psychologist Daniel Kahneman won the Nobel Memorial Prize in Economics) unmistakably demonstrates that individual psychology (driven habitually by its biases and mental shortcuts) primarily drives the growth of securities markets[84]. A seminal book on the topic, Animal Spirits, is based upon decades of research in the area, is co-authored by two Nobel Laureates in Economics, and tries to conclusively prove that sentiments not only drive markets but also affect macroeconomic variables like inflation, growth, consumption and even interest rates. Economists have found that the prevalent sentiment (using Consumer Sentiment survey results) cause upcoming economic downturns. Thus, policy makers definitely cannot ignore market sentiments and perceptions and SIS 2015 is a step in that direction[85,86].

84. Daniel Kahneman, "Maps Of Bounded Rationality: A Perspective On Intuitive Judgment And Choice", Prize Lecture, December 8, 2002, last accessed December 31, 2015,
http://www.nobelprize.org/nobel_prizes/economic-sciences/laureates/2002/kahnemann-lecture.pdf
85.George A. Akerlof and Robert J. Shiller, Animal Spirits: How Human Psychology Drives the Economy and Why It Matters for Global Capitalism, Princeton University Press, 2009
86. John G. Matsusaka and Argia M. Sbordone, "Consumer Confidence and Economic Fluctuations", Economic Inquiry, April 1998, Vol. 33, Issue 2, pp. 296–318

Risk–Returns–Liquidity Perceptions of Investment Instruments

Although the surveyed investors accurately perceive mutual funds to have lower risk than equities (Figure 9.1), surprisingly, perhaps due to a lack of awareness, and some much-publicized alleged frauds in the retail bond market and the increasing rate of corporate defaults in India, they consider debentures and bonds a risker than either of these instruments. While there is limited data on commodity futures or derivatives (currency or equity), investors seem to ignore the risks associated with the leverage in these instruments. In spite of a correct directional call, a small drop in the value of a derivative can wipe out the investor's entire equity. This makes derivatives and future significantly riskier than 'plain vanilla' investment instruments like bonds or equities.

Figure 9.1 – Risk Perception of Investment Instruments

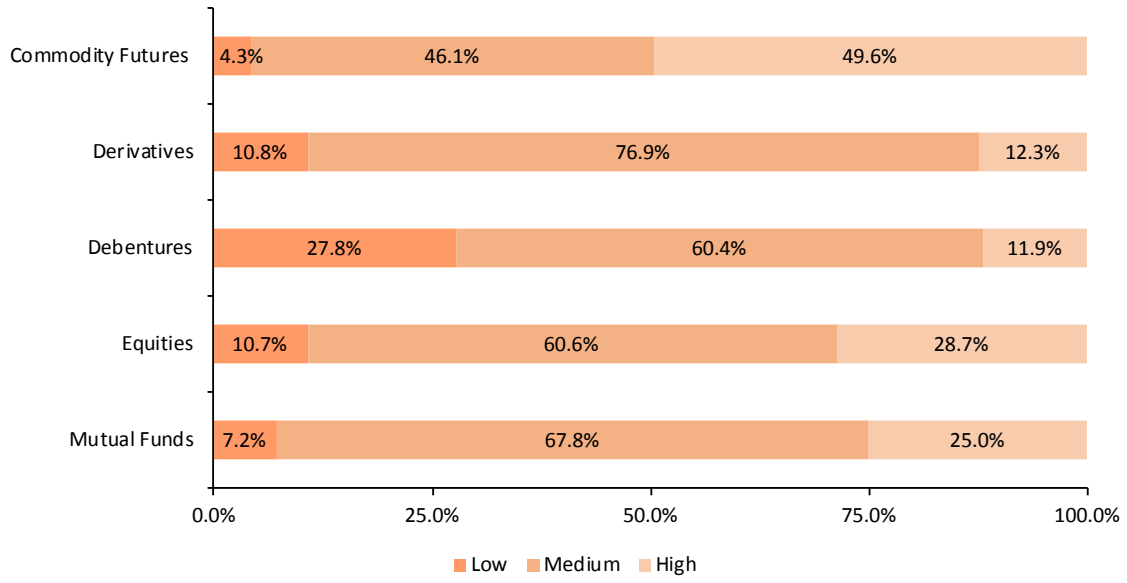


N = 5,356 (all urban investors, SIS 2015).

87. Securities Exchange Board of India, Public Notice; CRISIL Ratings, CRISIL Annual Default; ONICRA, ONICRA Default Study (see Footnotes 1, 2

While risk perceptions seem to not completely be in line with reality, especially for debentures and derivatives, the returns expectations completely align with historical data. Figure 9.2 depicts the returns expectations of investors and illustrates that among traditional investments, returns expectations are highest for equities (29 percent High), followed closely by Mutual Funds (25 percent High). On the other hand, returns expectations from Bonds are lower than that from other investments (12 percent expect High returns and 28 percent Low). Due to the sharp drop in commodity prices in 2015, it appears that retail investors are expecting a sharp rebound and thus, there is anticipation that commodity futures will reap high returns whereas, with only 12 percent expecting high returns from currency or equity derivatives, investors seem not very hopeful about either the fate of the INR or the returns from the stock market this year after a stellar performance (BSE Sensex was up 25 percent) in 2015.

Figure 9.2 – Returns Expectations

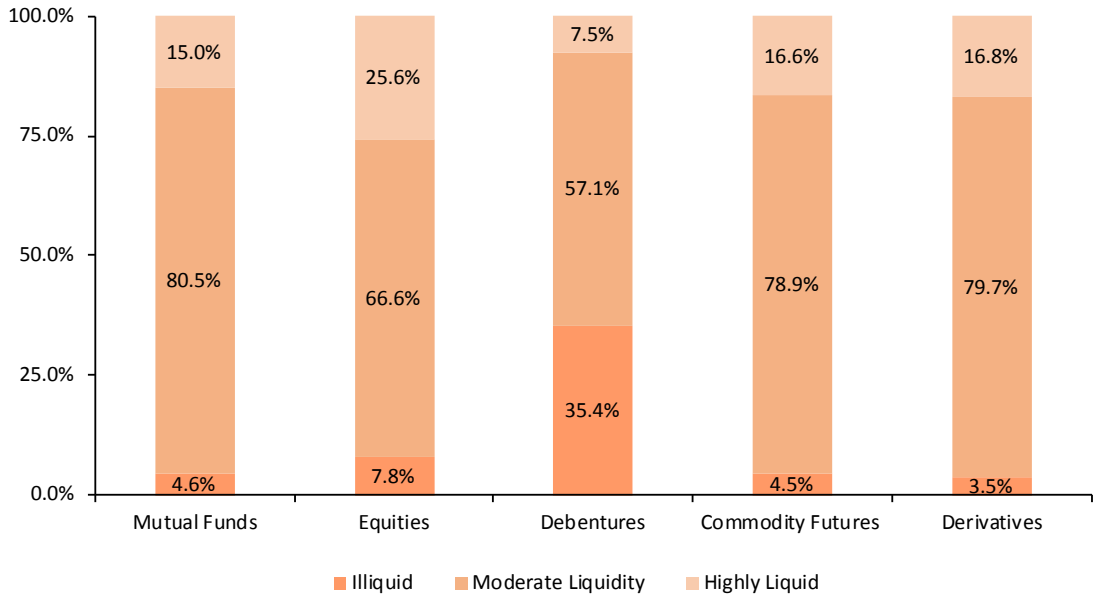


N = 5,356 (all urban investors, SIS 2015).

Analogous to returns expectations (and unlike risk perceptions), investors also appear to have a fair understanding of the liquidity amongst investment vehicles (Figure 9.3). Market participants realize the low liquidity of debt instruments and the high/moderate liquidity of equities and mutual funds. Overall, equities are quite accurately perceived to be more liquid than mutual funds. The data also shows that derivatives are considered equally or somewhat more liquid than mutual funds and equities. This is close to reality, since the liquidity in equity and equity derivative markets tend be similar in India[88] while on the other hand, currency and commodity markets usually do not trade in spot currency and physical commodities and are thus, not as liquid[89].

The liquidity perception of derivatives are also considered significantly higher than of bonds, which aligns with reality as secondary markets for bonds are limited.

Figure 9.3 – Liquidity Perception



N = 5,356 (all urban investors, SIS 2015).

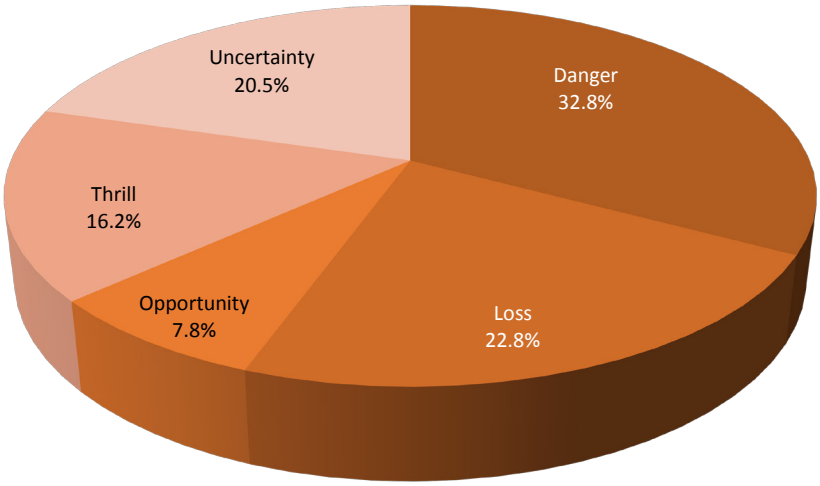
88. Sudhakar Reddy Syamala, V.N. Reddy, and Abhinav Goyal, "Commonality in Liquidity: An Empirical Examination of Emerging Order-Driven Equity and Derivatives Market", Journal of International Financial Markets, Institutions and Money, Forthcoming
89. Chicago Mercantile Exchange (CME) Group, CME FX Futures: A Sound Alternative to Cash FX, Chicago: CME Group, 2010, last accessed March 14, 2016, https://www.cmegroup.com/trading/files/tradingfxfutures.pdf

Household Risk Perceptions and Sentiments

The SIS data on risk, returns and liquidity perceptions demonstrates that while individual retail investors are surprisingly rational about certain aspects of financial decision-making, they can also be completely irrational regarding a number of other market aspects. This section is divided into two sub-sections enumerating the areas where the Indian retail investor's perception is close to reality and vice versa.

This chapter has its roots in behavioural finance– an academic field that studies the psychological aspects of securities markets and market participants. Traditional economic theory assumes the rational man theory of decision making, which reasons that the decision maker not only has complete information and can take instantaneous decisions that are immediately executed but also possesses infinite computing capabilities. Nevertheless, behavioural economics and finance brings economic research closer to reality and allows policy makers to understand exactly where the decision makers are biased in their choices, how they perceive risk and returns, how they are using mental short cuts, and thus, informing policy outreach and financial literacy programs. The word 'risk' itself has different meanings to various investors. A direct question on perception of risk highlights the risk aversion among Indian investors. When the word 'risk' is mentioned, 'danger' is the first word that comes to the mind of 33 percent of investors, and 23 percent think of 'loss', and yet another 20 percent think of it as 'uncertainty'. Perceptions that risk can be thrilling (16 percent) or can lead to opportunities (8 percent) are limited to less than a quarter of the investor base.

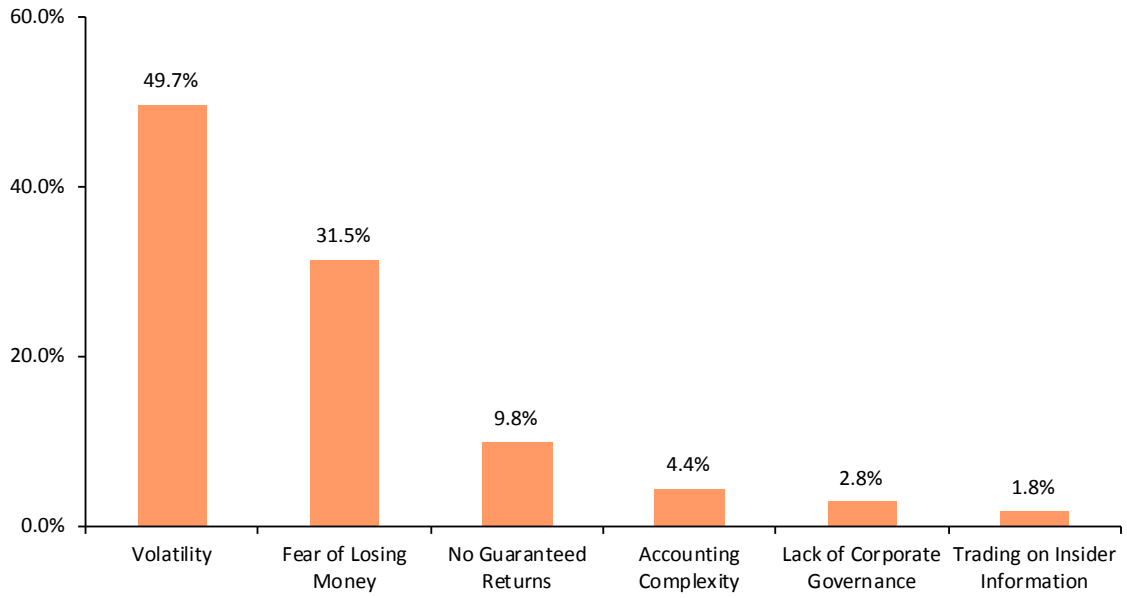
Figure 9.4: Different interpretations of the word 'Risk'



N = 5,337 (urban investors, SIS 2015).

This traditional risk aversion and behavioural biases amongst investors is also visible in their choice of top-three problems with investments in the stock market (Figure 9.5). According to investor perceptions, volatility is the most important 'problem' associated with the stock markets while the fear of losing money and the lack of guaranteed returns are also primary reasons of concern. It seems that, investors are interested in participating in the securities markets, and yet, hope to avoid any market risk. On the other hand, they are willing to ignore non-systematic or operational risk like corporate governance issues, potential accounting fraud or trading on inside information, and thus, show a biased view of risk of financial securities.

Figure 9.5: Top Three problems with Investing in Stock Markets



N = 5,356 (all urban investors, SIS 2015).

A large percentage of investors (Table 9.1) also showcase the self-confidence bias and rank "Observe Markets in Details" as the primary method they use to minimize risks related to investments (31 percent). Additionally, a significant percentage of investors (21 percent) display representativeness bias when they invest primarily in stocks and bonds of well-known corporations in an attempt to minimize risk. However, 30 percent mention that they invest principally in MFs to reduce their potential risk portfolio, further confirming the SIS finding that awareness programs by private and public institutions about mutual funds have been effective.

Table 9.1: Process used for Risk Mitigation

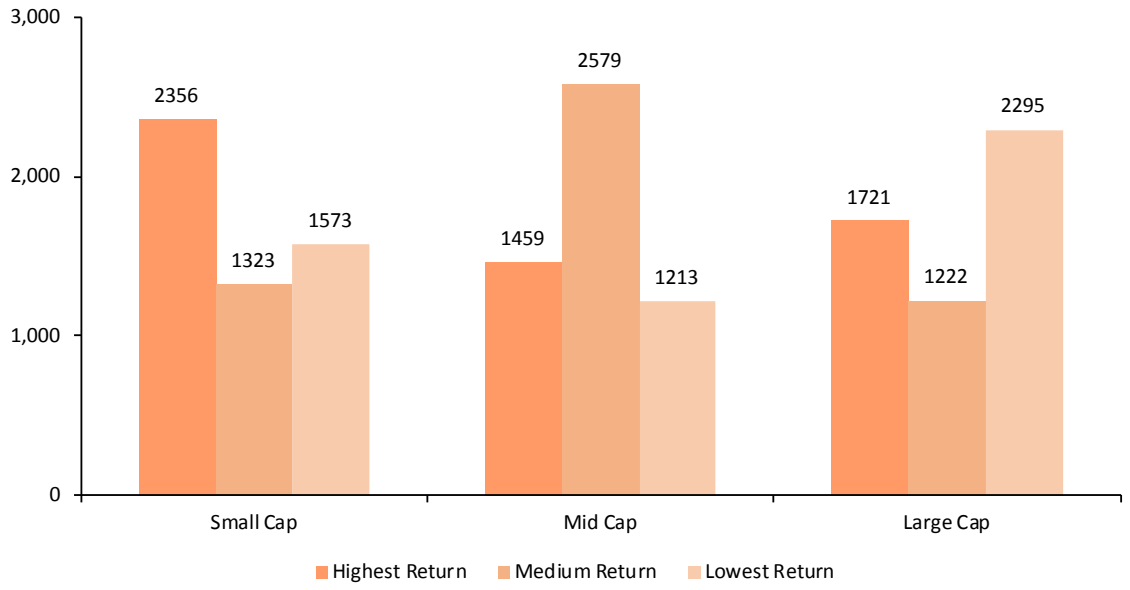
Rank	Stock/Bond of Known Company	Primarily Invest in MF	Observe Markets in Detail	Use Well-established Brokers	Invest in Small Parts	Total
1	21.0%	30.0%	30.0%	6.0%	13.0%	100.0%
2	13.0%	27.0%	18.0%	21.0%	21.0%	100.0%
3	24.0%	13.0%	21.0%	18.0%	24.0%	100.0%
4	9.0%	7.0%	24.0%	36.0%	24.0%	100.0%
5	28.0%	29.0%	12.0%	9.0%	22.0%	100.0%

N = 5,356 (all urban investors, SIS 2015).

While there are numerous market aspects where investors display profound biases, the retail Indian investor is surprisingly rational regarding a number of other market facets. 71 percent of investors feel that higher returns almost always imply higher risk. This is an unexpected finding that showcases a high level of financial awareness. It is common for investors to get swayed by the 'guarantee' of higher returns and ignore the risks associated with high return investments, and yet, the SIS 2015 data suggests an exceptional financially savvy Indian investor. Shefrin (2002)[90] finds that the investor expectations tend to be entirely contradictory to the reality of risk-return relationships and accordingly, survey respondents over a multi-year time span anticipate higher returns from stocks that they had perceived to be more safe. The paper shows that since investors expect recognized companies to outperform lesser-known companies (representativeness bias) and since known companies tend to be larger and have less volatile stocks, in effect, investors expect low risk stocks to have high returns. Surprisingly, the Indian retail investor does not showcase this strong representativeness bias, which is further proven by their lack of regard for 'brands' when investing. More than 70 percent of SIS 2015's total respondents (investors and non-investors) declared that they did not consider a recognized CEO or brand to automatically translate to a higher performing stock.

90.Hersh Shefrin, "Do Investors Expect Higher Returns from Safer Stocks than from Riskier Stocks?", The Journal of Psychology and Financial Markets, Vol. 2, Issue 4, June 2002

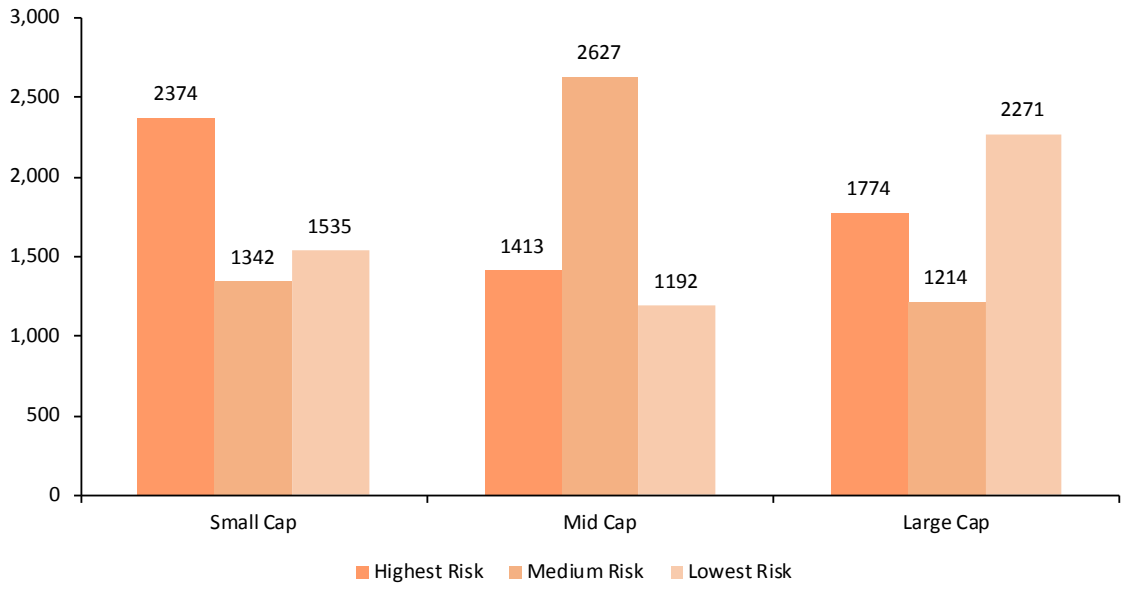
Figure 9.6: Returns Expectations by Market Capitalization



N = 5,356 (all urban investors, SIS 2015).

This essential understanding of the risk-return relationship also correlates to an innate understanding of the differential risks and returns of stocks based on the market capitalization. Figure 9.6 shows the perception of risk-return relationship with the size of the firm. As can be observed in securities markets data, larger firms have the lowest risk but also the lowest returns.

Figure 9.7: Risk Perceptions by Market Capitalization



N = 5,356 (all urban investors, SIS 2015)

Taxation is yet another area in which the Indian investor's rationality is striking. While the SIS 2015 data has found that tax savings is not a primary reason for investing (probably due to lack of tax savings investment instruments or due to the very low tax net in India, as discussed in Chapter 4), most investors (85 percent) do consider the ex-post tax impact when they take investment decisions.

The SIS 2015 data presents a mixed picture of the Indian investor, where a risk-related understanding of the markets are the weakest and the self-confidence bias is profound while they display a high level of sophistication in their understanding of other aspects of the markets like returns, liquidity and even the risk-return relationship. Outreach efforts from private and public agencies should be focused to help mitigate the issues arising from the former.

10 AWARENESS OF REGULATORY POLICIES, SEBI AND INVESTOR LITERACY PROGRAMS

KEY FINDINGS

- **According to SIS 2015, 32 percent of surveyed urban investors have participated in either a government or a private investment awareness program.**
- **While SEBI programs are the most popular, private firms also have prevalent financial literacy programs.**
- **About 95 percent of investors consider these programs to be beneficial.**
- **Newspapers are not only the most important source of information regarding awareness programs but they are also the most visible source of communication from SEBI.**
- **Nearly 50 percent of investors have visited SEBI website.**
- **Overall awareness levels concerning rules and regulations pertaining to the securities markets are high among the investor community:**
    - **88 per cent follow government and regulatory policies relating to markets.**
    - **78 percent are aware of SEBI policies that help boost retail market investment.**
    - **90 percent are satisfied with SEBI-initiated KYC uniformity.**
    - **82 percent are aware of the simplified Saral Account Opening Forms (AOF).**
- **However, 84 percent of surveyed respondents affirm that SEBI's efforts to publicize securities markets policies need improvement.**
- **In case of grievances, while investors knock on multiple doors (including their financial intermediaries and the police), more than 50 percent choose to approach SEBI.**

Chapter Rationale

A recent paper in the Journal of Finance shows[91] significant evidence that, "Nearly all households that score high on financial literacy or rely on professionals or private contacts for advice achieve reasonable investment outcomes. Compared to these groups, households with below-median financial literacy that trust their own decision-making capabilities lose an expected 50 bps on average." Although the consequences of muted financial literacy had not yet been computed when SEBI was formed, regulatory awareness and financial literacy has always been an important SEBI directive.

SEBI (as well as other private securities markets participants) conduct awareness literacy programs to encourage participation, improve awareness about markets and also help investors recognize the potential value of long-term investing and the common pitfalls of investing in the securities markets – namely, lack of diversification, overconfidence and name recognition bias. While SEBI programs are the most popular, nearly 30 percent of the surveyed urban investors have also participated in either a government or a private investment awareness program and 95 percent of these participants consider such programs to be beneficial. Furthermore, the SIS 2015 discovers that though television and SEBI website are significant means of information dissemination (nearly 50 percent of surveyed investors have visited SEBI website), newspapers are not only the most important source of information regarding awareness programs but they are also the most visible channel of communication from SEBI.

Arguably, owing to these wide-ranging levels of communication and information dissemination, overall awareness levels concerning rules and regulations pertaining to the securities markets are high among the investor community. Although more than 80 percent of surveyed investors are familiar with SEBI's rules relating to the uniformity of KYC or the Saral AOF procedures, an equivalent percentage affirm that SEBI's efforts to publicize securities markets policies need improvement. Nonetheless, in case of grievances relating to the securities markets, while investors approach multiple agencies (including their financial intermediaries and the police), more than 50 percent choose to get in touch with SEBI, primarily due to its well-regarded role as the regulator of the securities markets.

91.Hans-Martin Von Gaudecker, "How Does Household Portfolio Diversification Vary with Financial Literacy and Financial Advice?", Journal of Finance, Vol. 70, Issue 2, March 12, 2015

Introduction

To help understand the general public's level of awareness concerning regulatory policies, it is crucial that policy makers are well acquainted with the financial literacy programs that SEBI (and other private securities markets participants) conduct to encourage participation in the securities markets and improve the level of awareness about these securities. Not only does this provide a metric to measure the success of past programs but it also helps create a road map for future potential outreach strategies.

Investor Literacy Programs

As mentioned earlier in the chapter, financial literacy is a prime driver of investment returns, and thus, should be encouraged. According to the SIS data, a little over 32 percent (1,418) of the survey respondents have attended financial literacy/education programs. Of these respondents, a 100 (i.e., 7 percent of all respondents who have been to a financial literacy program) have attended a program by SEBI, while 6 percent have attended programs by private wealth management groups.

However, most investors did not participate in any financial literacy or education programs and neither did most of them specify a reason for non-participation. Amongst those who did specify, reasons included 'lack of time', the perceived 'lack of need to participate in such programs', and 'lack of awareness' regarding program details. Thus, it is essential that regulators and agencies try to impress upon investors that financial literacy programs or financial planners affect portfolio returns positively.

According to Table 10.1, while investors gained awareness about financial education and literacy program from a variety of sources, newspaper still remains the most popular medium for information in this sphere. Word-of-mouth from friends and family, closely followed by SEBI website, are also significant sources of information dissemination and rank higher than television. This data highlights the importance of regulator outreach also shows its effects on investor choices and improved financial literacy.

Table 10.1 – Source of Information about Financial Literacy Programs

Newspapers	Friends/Relatives	SEBI Website	Television	Hoardings	Brokers
458	448	431	352	184	32

N = 1,905 (subset of urban investors who responded, SIS 2015)

Most of those who participated in these programs (a total of 205) did so in 2013, 170 respondents participated in 2014 while a mere 60 participants attended in 2015 (till September, 2015). The participation in these literacy programs can be termed useful if it helped investors deal better with risk and make smarter investment choices. Cross tabulating data from investment choices and investor education, it can be seen that investment choices in equities and mutual funds are not related to participation in financial literacy programs. However, when tabulating leveraged instruments like Commodities Futures and Derivatives (Equities/Currencies) it is seen that participation in these markets amongst program participants is lower. Among the investors, about a third participated in these programs, thus if there was no effect of participation, a third of current investors in every market instrument would be participants in these financial literacy programs. However, the cross tabulation in Table 10.2 shows a stark difference. Investors who participated in financial literacy programs make up 32 percent of all investors and similarly 34 percent of all mutual fund investors (as well as 34 percent of equities investors). However, they form a very small portion of investors in derivatives (only 16 percent) and futures (only 14 percent). The effects of leverage can be significant for retail investors, and the risks from the sharp swings in valuation of levered instruments is usually always mentioned in financial literacy programs.

Table 10.2 – Tabulation of Investors by Participation in Investor Education Programs

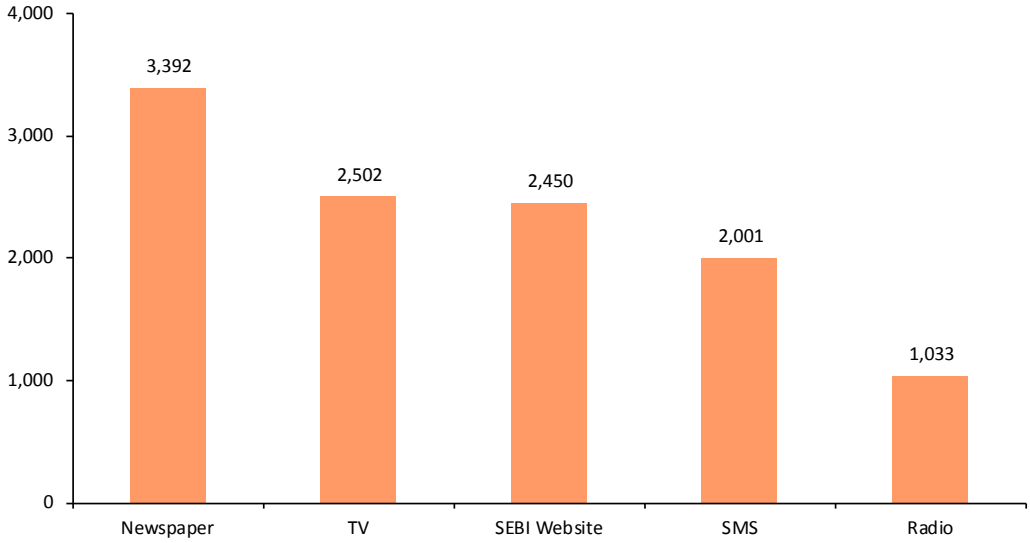
Current Investment	Mutual Funds	Equities	Derivatives	Debentures	Commodity Futures	All Investors
Non-Participant	1591	1376	243	645	126	2982
	66.2%	65.8%	84.1%	75.9%	85.7%	67.8%
Participant	814	715	46	205	21	1418
	33.8%	34.2%	15.9%	24.1%	14.3%	32.2%
Totals	2405	2091	289	850	147	4400

The final word on investor literacy programs, whether undertaken by SEBI or other private firms, lies with investors. According to the survey, nearly 95 percent of relevant investors found that these investor education programs helped them make the right decisions concerning their investment choices, while 91 percent found these programs adequate for allowing them to take the right investment decisions.

Outreach Efforts and Its Success

The SIS survey attempts to not only understand investor behaviour but it also helps generate informed policy decisions by measuring the outcomes of outreach programs. To gauge the success of SEBI's outreach programs, survey participants were closely questioned concerning the manner and medium of their interaction with SEBI.Figure 10.1 details out the responses.

Figure 10.1 – Reaching Investors: Sources of Communication from SEBI



N = 5,356 (all urban investors, SIS 2015)

Despite the rise in new media, newspapers still remain the most successful mode of communication for SEBI in urban areas. Television comes a close second, but with a larger cost attached to it. SEBI website is also very visible, with 46 percent of the securities markets investors having visited it and received information from it. In the previous survey, only 7 percent of investors used SEBI website for information.

Overall investor awareness about SEBI's as well as other regulatory rules are very high amongst the sampled investors.

- 87 percent regularly follow government and regulatory policies pertaining to securities markets.
- 76 percent are aware of the measures taken by SEBI to boost retail participation in securities markets, viz., reservations for retail investors in IPO, introduction of direct plans with lower expense ratio, Basic Service Demat Account (BSDA), discount in Offer For Sale etc.
- 93 percent are satisfied with the uniformity of KYC norms initiated by SEBI.

- 78 percent are aware that individual investors can open a trading account and demat account by filling up a simplified Account Opening Form (AOF) termed SARAL AOF that requires just one documentary proof of address (either residence/correspondence or permanent) while opening a trading account and / or demat account to participate in cash segment

- 80 percent are aware of the investor grievance mechanism and the arbitration mechanism available at the stock exchanges.

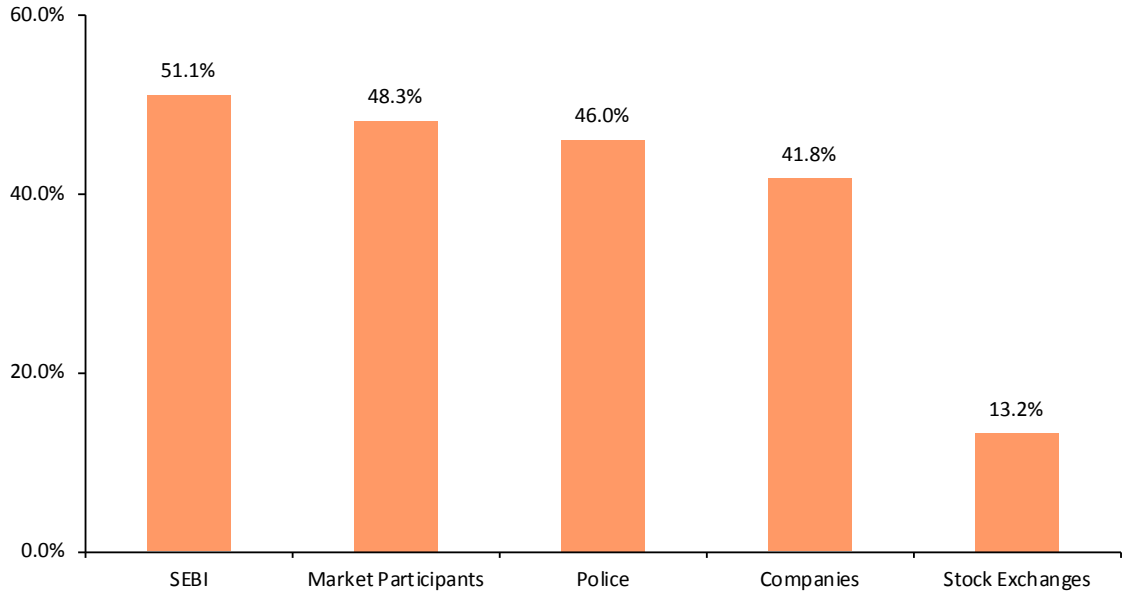
- 77 percent are aware of the Consolidated Account Statement (CAS) facility that allows an investor to view all of his/her investments in Mutual Funds and securities (Demat) at one place

However, despite such high levels of awareness of regulations and policies, when asked about publicity, (unsurprisingly) 83 percent of securities markets investors mentioned that there is further need to publicize information by regulators.

Redress Mechanisms for Grievances

Following up on grievances, especially quick and impartial resolutions, is key to the success of a regulator's function and affirms faith in the securities markets. From websites to telephone helplines, SEBI has created multiple grievance redress apparatuses and based on the survey findings, the awareness of these processes and associated policies seem to be significantly high amongst investors. SEBI Complaints Redress System (SCORES) portal has been created specifically for the purpose of providing investors a user-friendly tool for complaints about the securities markets. To precisely gauge exact causes of markets-related issues and especially the resolution methodology, the survey questioned investors in detail. Figure 10.2 highlights the fact that while investors knock on multiple doors to address their concerns, about 71 percent are aware of SEBI's grievance redress mechanisms and more than 50 percent of those with troubles reach out to SEBI. Almost 50 percent of investors contact their brokers, the police or the company concerned while just 13 percent of these complaints are communicated to the stock exchanges.

Figure 10.2 – Recourse for Grievances Regarding Financial Markets



N = 4,400 (subset of urban investors who responded, SIS 2015)

According to SIS 2015, amongst those investors who filed a complaint with SEBI, 87 percent were satisfied with SEBI's feedback. It is important to note that while SEBI satisfactorily sorted about 88 percent of these complaints, nearly 49 percent of those investors who approached SEBI had issues while lodging the complaint itself. While the SCORES portal allows easy online complaints to be filed against both listed companies and financial intermediaries, investors may lodge complaints by writing to SEBI. They may seek help from SEBI helpline.

11 GEOGRAPHICAL ANALYSIS OF INVESTOR BEHAVIOUR AND PREFERENCES

KEY FINDINGS

- **Cultural/regional influences strongly impact investment decisions.**
- **50 percent of all Indian investors are from the West zone while a mere 7 percent reside in the South zone. The North and East zones constitute 26 percent and 15 percent, respectively.**
- **27 percent of West zone respondents are investors whereas just 15 percent, 9 percent and 5 percent of respondents from the North, East and South invest in the securities markets.**
- **The regional differences persist even amongst high-income and higher-educated groups.**
- **While 32 percent of the population in the top-15 cities are investors, barely 1 percent from the bottom-5 cities participates in the securities markets.**

Chapter Rationale

A pan-Indian survey that focuses on drawing out regional and cultural disparities, which strongly influence investment behaviour and investment instrument choices (with emphasis on savings, investments and risk aversion) unmistakably shows that even after controlling for other factors like income and education, cultural/ geographical influences strongly impact investment decisions. This seems to be the key to answer the questions that arise from the surprising statistics emerging from the SIS 2015's geographical focus data from across the four Indian zones. According to this data, about half of all Indian investors are from the West zone while a mere 7 percent reside in the South zone. The North and East zones constitute 26 percent and 15 percent, respectively. Additionally, 27 percent of the West zone respondents are securities markets investors whereas, just 15 percent, 9 percent and 5 percent of respondents hail from the North, East and South zones. This strong regional incongruence persists even amongst high income and high education groups that tend to invest more in the markets. A deeper probe into the survey data proves that more localized, city-level statistics also portray similar discrepancies in investor behaviour: 32 percent of the top-15 cities are investors while among the bottom-5 cities, barely 1 percent participate in the securities markets.

Introduction

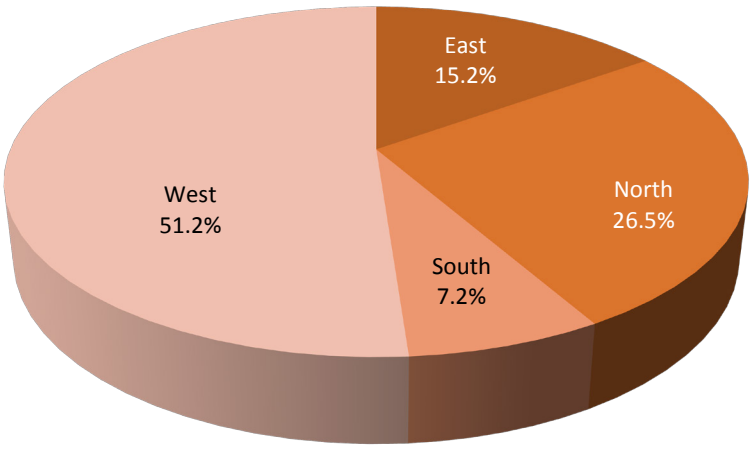
Academic research has established that racial and ethnic differences have a profound influence on savings, investments and risk aversion, even after controlling for other factors like income and education[92]. The SIS 2015 data compares and analyzes investment choices across Indian states and zones and reaches the same conclusion.

92. Sharmila Choudhury, "Racial and Ethnic Differences in Wealth and Asset Choices", Social Security Bulletin, Vol. 64, No. 4, 2001– 2002

Where Are The Investors?: A Zonal Analysis

The SIS 2015 data finds that a variety of underlying factors like income, education and occupation affect investment behaviour and investment instrument choices, whereas certain factors like age or marital status seem to have no effect at all (see Chapter 4 for details). However, the distribution of investors across geographical zones illustrates that cultural influences are one of the most important considerations affecting the investment decision process. It is not a mere accident that more than 50 percent of investors in the country reside in the West Zone while just 7 percent are from the South (see Figure 11.1).

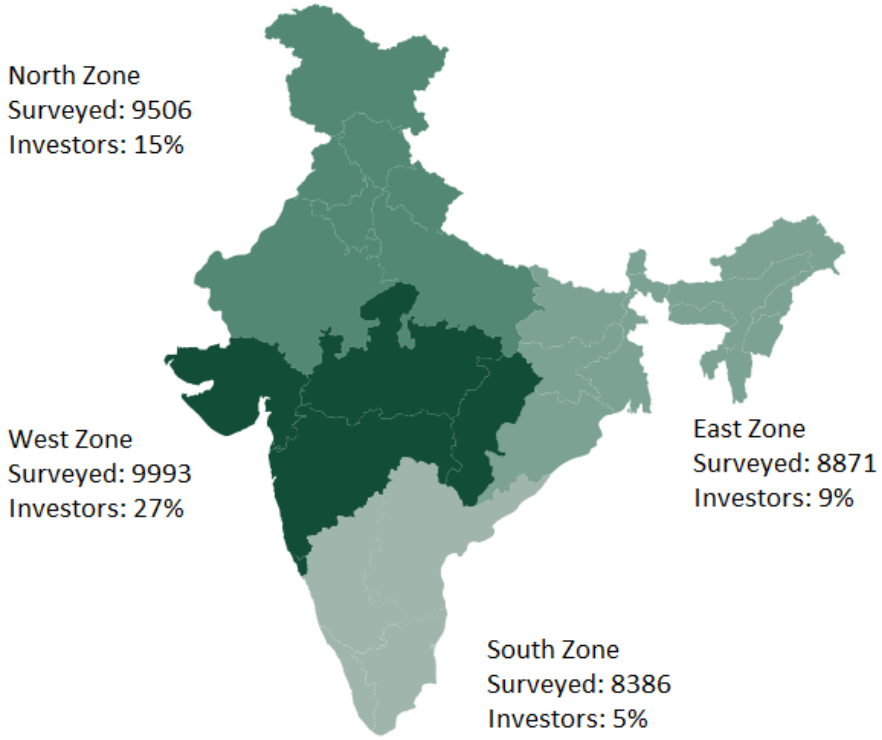
Figure 11.1: Percentage of Indain Invetors by Zone



N = 5,356 (all urban investors, SIS 2015)

To control for differing sample sizes across zones based on population and sampling techniques (see Chapter 3), Figure 11.2 represents a zonal heat map with investors as a percentage of respondents. In the West Zone, 27 percent of respondents are investors while the North has 15 percent of respondents as investors. In the East and the South zones, 9 percent and 5 percent of respondents are investors, respectively. Since this data is in line with the zonal numbers for demat accounts, these surprising results are not in doubt. Remarkably, according to data from National Securities Depository Limited (NSDL)[93], only two states in the West zone (Maharashtra and Gujarat) account for nearly 40 percent of demat accounts in India.

Figure 11.2: Investors as Percentage of Zonal Survey Respondents



Darker Shade indicates higher sample size while lighter shade indicates smaller sample sizes.

N = 36,756 (all urban respondents, SIS 2015)

93. Rediff.com, Five States Hold 60% of Total Demat Accounts, December 07, 2007, last accessed December 11, 2015, http://www.rediff.com/money/2007/dec/27demat.htm

Additionally, to confirm that it is cultural distinctions and not underlying, unobserved homogeneity regarding other attributes that produce these results, a more detailed socio-economic analysis of the data provides a confirmation. Across zones, amongst the income group that earns higher than ₹20,000, an analogous difference in percentage of investors is clearly noticeable. In the South, only 9 percent of the population with incomes higher than ₹20,000 invests in the securities markets, whereas, in the West, more than 30 percent amongst the same economic group invests in securities markets. Moreover, according to the SIS 2015 analysis (see Chapter 4 for details), the other primary driver for investment is education: higher education indicates a higher propensity to invest. Nonetheless, the zonal differences persist even amongst respondents with more than 10 years (11-15 and 15+) of education. The West and the North zones record 31 percent and 20 percent of the highly educated group as investors, respectively, while it is 11 percent and 8 percent in the East and South zones, respectively. This distinctive variance between the West zone and the rest of the country has remained consistent over the time; in the 2011 survey, 55 percent of all investor households were from the West Zone.

Risk Aversion and Zonal Investment Choices

Historically, bonds/debentures are the lowest risk investments among the securities market instruments analyzed in SIS 2015. Mutual funds, while riskier instruments than bonds, have lower risk than equities due to the benefits of diversification. And derivatives are riskier than equities due to the volatility from leverage. A geographical break up of investment instruments data showcases the degrees of risk aversion (Table 11.1). Investors in the South have the lowest investments in the riskier derivatives and futures instruments, while it is the North which leads in investments in these instruments.

Table 11.1: Investors and Investment Instruments Used, by Zone

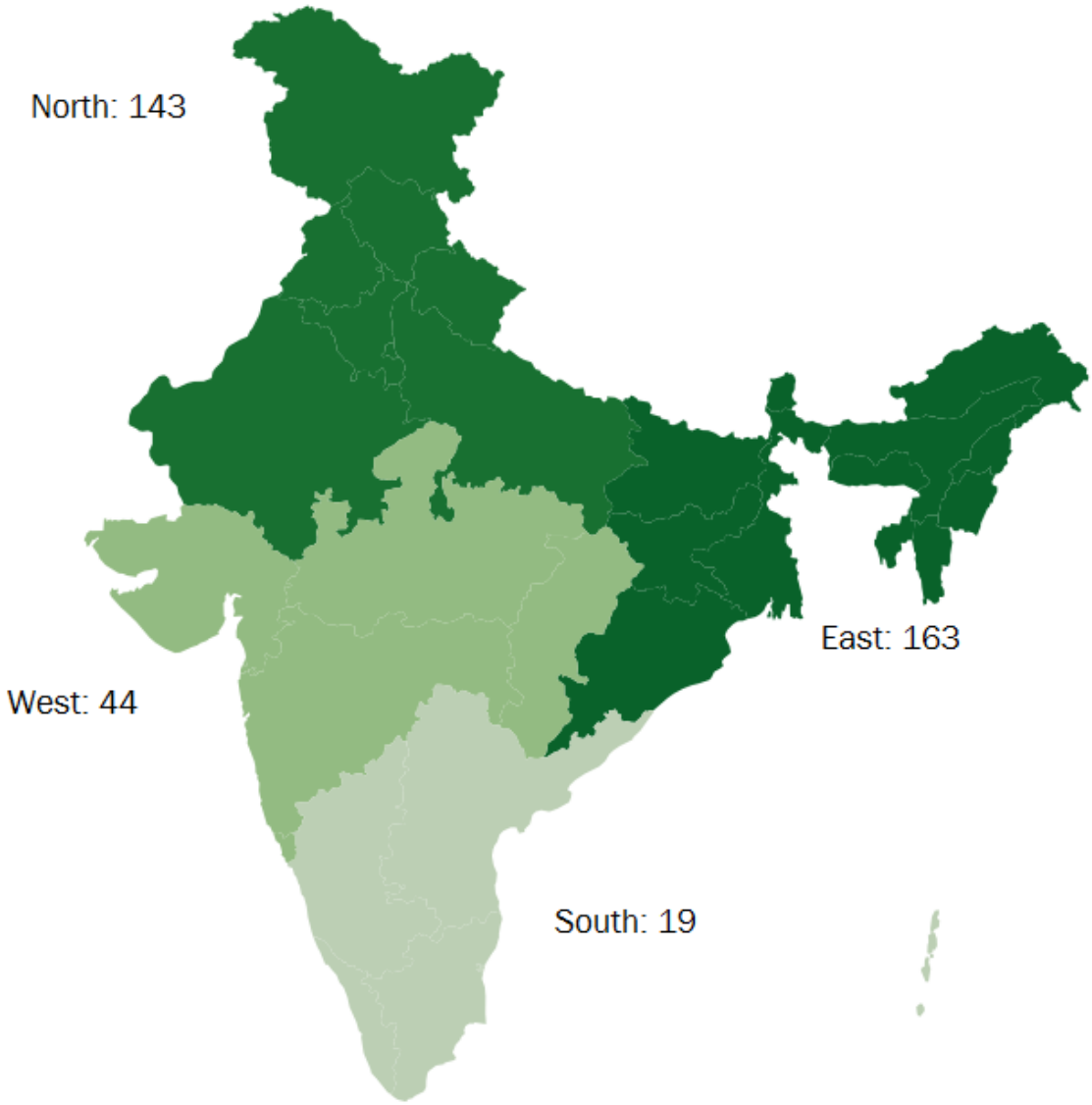
Instrument	East	North	South	West
Mutual Funds	633	859	212	1832
Equities	143	804	157	1837
Debentures	37	218	88	913
Derivatives	0	212	5	294
Commodity Futures	163	143	19	44
Totals	812	1419	385	2740

N = 5,356 (all urban investors, SIS 2015)

This risk aversion is also supported by the data from a direct question on risk. When asked what was the first thing that comes to their mind when they hear the word risk, the word loss was mentioned by nearly 40 percent of respondents in the South, compared to 29 percent in the West, and 12 percent in both East and the North. Thus risk aversion levels are highest in the South both from the respondents' stated and revealed preferences, while it is lowest in the North.

One surprising result is a higher incidence of trading in currency futures in the North and the East, when compared to the West (see Figure 11.2). While risk aversion should lead to lower investments in derivatives markets, this might seem counter-intuitive. However, since the North and the East land have international borders, this might be an effect of cross-border trading (formal and informal) in certain areas which creates this demand for currency futures.

Figure 11.3: Commodity Futures Demand Map



Darker Shade indicates higher sample size while lighter shade indicates smaller sample sizes.

N = 369 (all currency derivative investors, SIS 2015)

Does The Education-Investment Correlation Hold True in Every Zone?

One of the key findings of the urban data analysis of SIS-2015 is the Education-Investment correlation (see Chapter 4 for details). To understand whether this relationship is robust across the state groups, this data is visualized in a Figure 11.4. The concentric circles display the percentage of investors by education levels, with the education levels increasing with the size of the circle. The smallest (inner most) circle depicts those respondents who are not literate, while the outer circle represent those with over 15 years of education.

Figure 11.4: The Education-Investment Correlation across Zones

N = 36,756 (all urban respondents, SIS 2015)

A Comparison Between the Top-15 and Bottom-5 Cities

Similarly, the top 15 cities in terms of total investors are concentrated in the West zone although large urban clusters in other parts of the country also feature in that list. Amongst the top-15 cities, the West zone not only records a total of 10 cities (whereas there are just 3 cities from the North, 1 from the East and 1 from the South), all the top-5 cities are from the West zone too. Amongst a total of 9,798 survey respondents from these cities, 32 percent are investors. In sharp contrast, less than 1 percent of the population in the bottom-5 cities are investors. In this group, 1 city is from the South, 3 from the East and 1 from the West. The high representation of the East in this list is due to 3 cities of the North East, which have a negligible rate of investors. However, even in the North East zone, there are significant intra-zonal differences. Cities like Gangtok, Guwahati and Tinsukia have significant investors while cities like Imphal, Shillong and Kohima have literally no investors. Since neither household income nor education can rationalize these disparities, it appears that it is local cultural influences that are the key factors in investment decisions.

12 THE MARKET PARTICIPANTS' SURVEY

KEY FINDINGS

- **Most Market Participants (MPs) (63 percent) are in business for over 10 years, while 32 percent are in it between 5 to 10 years. The numbers vary by segment, with nearly all (98 percent) Depository Participants (DP) and only 51 percent sub-brokers and mutual fund agents are in the business for over 10 years.**

- **Most MPs focus on the secondary markets alone, except DPs who usually participate in both**

- **Unsurprisingly, DPs also have the largest customer base, with brokers following them in size, while most Authorized Persons and MF Agents have a smaller customer base.**

- **More than 90 percent (919 out of 1,016) MPs operate within their city limits. It is predominantly DPs (72) who function outside their state of origin.**

- **Equities (56 percent) are the most popular instruments traded via financial intermediaries, followed by mutual funds (45 percent). Less than 5 percent invest in derivatives or bonds.**

- **MPs' perceptions of risk, returns and time horizons for plain vanilla instruments like equities, mutual funds and bonds are in line with reality. However, even among these market participants, comparative risk-returns for derivatives are skewed lower than historical data.**

- **Only a few MPs find their business has declined over the past 5 years. This is arguably due to survivorship bias.**

- **To attract new clients, most MPs use face-to-face interaction (52 percent), followed closely by mass media advertising (51 percent) and phone calls (50 percent). While bulk SMS (45 percent) is still popular, social media (17 percent) is not yet a common practice.**

- **To retain existing clients, most MPs improve client services (52 percent) and offer additional services at discounted rates (51 percent).**

- **In many instances, MP and Investors have different perceptions on the same subject. While investors mention that market risk like volatility is the primary cause of low market participation, MPs think it is due to the availability of safer high return, low risk alternatives**

Chapter Rationale

The Market Participants' (MPs) Survey includes responses from a total of 1,016 respondents, 100 brokers, 311 Sub-Brokers, 305 Authorized Persons (AP), 90 Depository Participants (DP) and 210 Mutual Fund Agents (MFA),from across the country. The various types of market participants are unique in their size, geographical footprint and market focus. For instance, DPs are not only larger in size but also in client volume and operate within a broader geographical area (i.e., they also function outside one's city or state). They are also in the business for significantly longer than brokers, sub-brokers or APs.

The business of market participants is going through significant changes and upheavals. While the direct reasons for the troubled business environment enumerated by participants for these are unsurprising and include competition, taxes, and lower commissions. The detailed survey also highlights crucial incongruities between financial intermediaries and their clients, that is, between the suppliers and the consumers of securities markets services. Both investors as well as MPs consider, directly or indirectly,'riskiness' of the securities market as the primary reason for low participation of retail investors. Investors mention market risks as the primary cause of low market participation and MPs mention that it is due to the availability of low risk, high return savings alternatives. However, the reason behind why investors participate in the markets showcases disconnect between MP and investor views. For investors, the reason why they participate in capital markets is primarily for capital gains, while according to MPs, those engaging their services use it for retirement and capital preservation.

Additionally, despite their central position in securities markets, MPs also showcase some biases and lack of information. While MPs mentioned 67 percent of their clients have engaged in panic selling, yet only 33 percent of them would urge investors not to sell during a sharp downturn. And though they have a clear idea of the risk-return-time horizon profiles of equities, mutual funds and bonds; in the case of derivatives, most MPs do not correctly perceive the comparative risk and returns profiles of derivatives.

These disconnects could be considered in the light of the fact that a mere quarter of MPs have taken part in trainings provided by private and public organizations, despite 100 percent of participants being aware of them. Additionally, the regularity with which they learn about policies and regulations too need to be improved with only 35 percent keeping track of policy and regulatory

changes more often that once a month.

The competitiveness which affects MPs in the market is also clearly visible from the significant efforts that they are taking to acquire new clients, with over half using face-to-face interactions and similar numbers using mass media advertising and tele-calling. Only 17 percent uses social media making it visible that similar to their clients, MPs also exhibit a preference for 'traditional' methods of conducting securities markets transactions. When MPs reach out to their client (nearly 67 percent at least once a quarter) nearly half place a call, and nearly 20 percent prefer to meet or to SMS. While letters have completely become outdated, email seems to be the most popular second line of communication. However, in case of receiving information MPs showcase their tech-savviness with 40 percent ranking social media as their most important source of information, followed by company website and then by mass media. Word of mouth and mass media seems to be the preferred second rank information source. Technology has been the primary reason for improving business for MPs, with improving technology and web access providing better margins and expansion possibilities.

Despite the wide-spread shutting down of MPs, only few in the current survey find that their businesses suffered in the past five years. This is arguably due to a survivor bias arising out of the consolidation in this industry. And, while regulation tends to be a 'pain point' for most industries, it is heartening to find out that the regulator's role has positively affected the business of the MPs.

Introduction: Financial Intermediaries in India [94]

Over the past decade, although brokers and market participants continue to have a large role to play in securities markets functions, the global trend has been that large numbers of investors are moving to online trading and investments[95].

As of 31st March 2015, there were a total of 6,147 cash segment brokers, a drop of 35 percent from the previous year's number of 9,411 (at the end of FY 2011-12, this was 10,268)[96]. The number of sub-brokers fell by 18 percent from 51,885 at the end of FY 2014 to 42,351

94. From Chapter 8, SIS 2015
95. Andre Cappon, "The Brokerage World Is Changing, Who Will Survive?", Forbes, April 16, 2014, last accessed January 15, 2016, http://www.forbes.com/sites/advisor/2014/04/16/the-brokerage-world-is-changing-who-will-survive/
96. SEBI, SEBI Bulletin April 2015, last accessed February 15, 2016, http://www.sebi.gov.in/cms/sebi_data/attachdocs/1430125406381.pdf

at the end of FY 2015 (at the end of FY 2012, this was 77,141). In April 2015, the first month of FY 2015-2016, the number astoundingly dropped to 3,195 brokers and 41,625 sub-brokers. The number of brokers in derivative segment increased from 2,337 in FY 2012 to 3,031 in FY 2014 further to 2,810 at the end of April 2015. The traditional dynamics of the industry are shifting as smaller brokers are either disappearing or are merging to form larger, more stable consolidations[97].

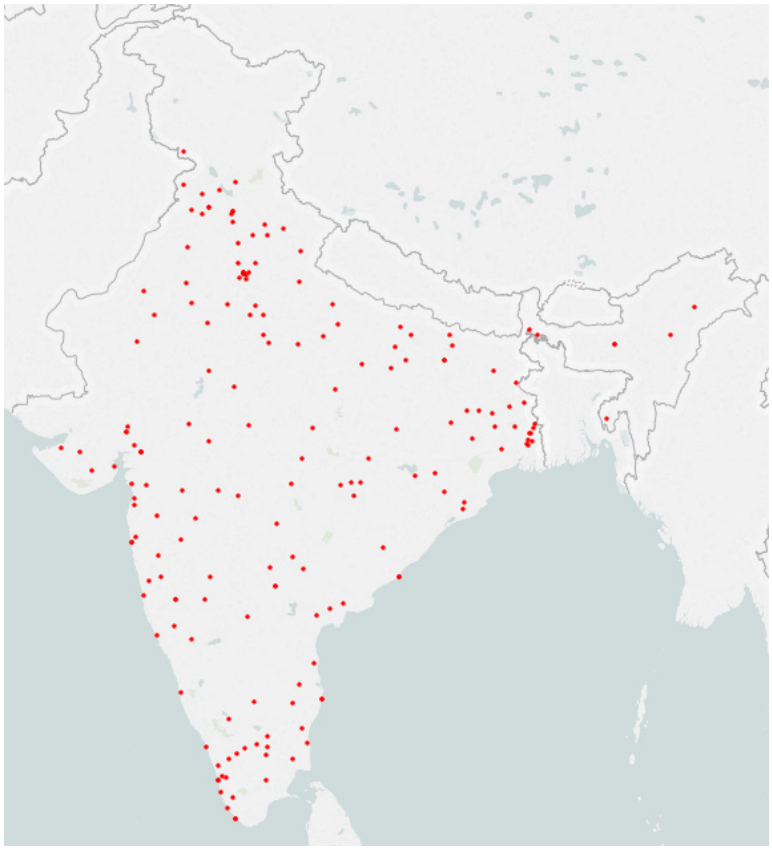
SEBI's data on the "Percentage Share of Top 'N' Members in Turnover in Cash Segment" shows that while the top 25 brokers accounted for 38 percent of transactions in 2008-09, the share has moved up to 51.2 percent in March 2015[98]. When the SIS dug deeper to try and ferret out the exact reasons for the drastic drop in the number of brokers, it seems a wide array of factors—from limited retail trading frequency and rising Internet penetration to a surge in the number of APs and the shuttering of numerous subnational exchanges over the past year—are all critically affecting the brokerage industry[99].

97. Ashish Rukhaiyar, "Shares of Larger Brokerages on the Rise", Mint, May 04, 2015, last accessed March 10, 2016, http://www.livemint.com/Money/Rvg2dixqzRH5Eh2Qj05x1N/Shares-of-larger-brokerages-on-the-rise.html
98. SEBI, SEBI Bulletin April 2015, last accessed February 15, 2016, http://www.sebi.gov.in/cms/sebi_data/attachdocs/1430125406381.pdf
99. Ashley Coutinho, "Brokers Shut Shop on Falling Volumes, Compliance Costs", Business Standard, January 12, 2016, last accessed January 16, 2016, http://www.business-standard.com/article/markets/brokers-shut-shop-on-falling-volumes-compliance-costs-116011200755_1.html

A Close Look at the Market Participants' Industry

The Market Participants' Survey includes responses from 305 Authorized Persons (AP), 100 Brokers, 90 Depository Participants (DP), 210 Mutual Fund Agents (MFA) and 311 Sub-Brokers (total of 1016 respondents) from across the country (Figure 12.1). This is the first comprehensive survey of market participants in India, and in a unique feature of SIS 2015.

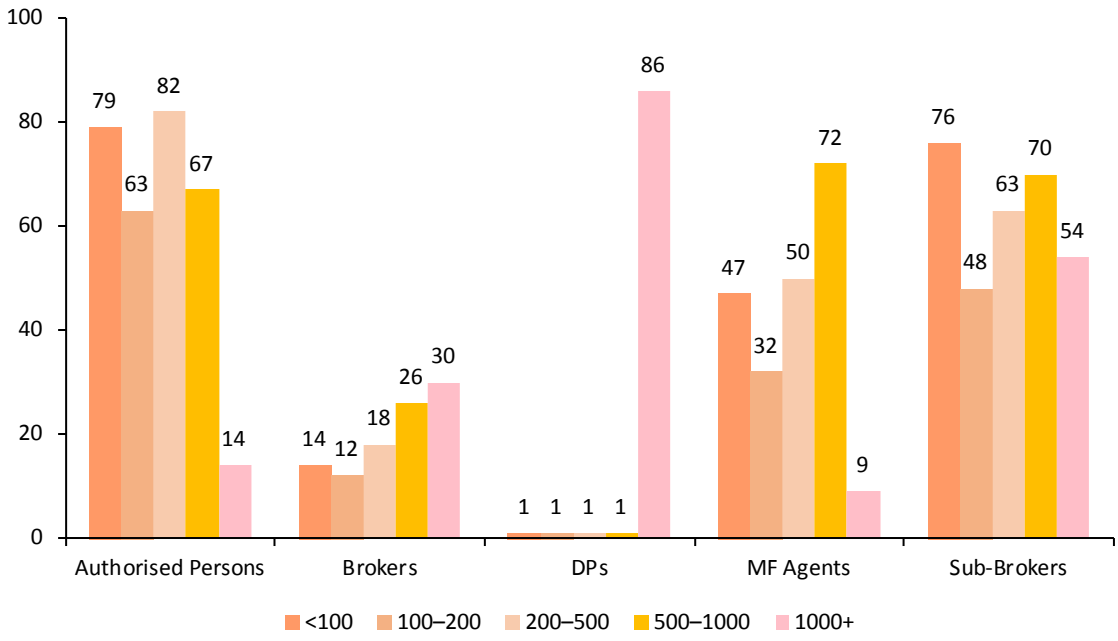
Fig 12.1: Market Participants Surveyed across the Country



The dots in the map indicates the concentration of the sample sizes of the Market Participants

While they are broadly in the same industry, these MPs are unique in the aspect of the business they service and their relevance to the securities market. APs are individuals registered with exchanges. They are similar to sub-brokers, only difference is that they do not have trading terminals. Although each of the five types of respondents are a financial intermediaries, the various types of market participants are unique in their size (Figure 12.2). Depository participants are few in number and they are larger institutions which are older, have larger number of clients and function across primary and secondary markets. Figure 12.2 shows the size of customer for the various financial intermediaries. While around 20 percent of APs, MFAs and Sub-Brokers have less than a 100 clients, and very few of them have more than 1000 clients, nearly all DPs have over a 1000 clients.

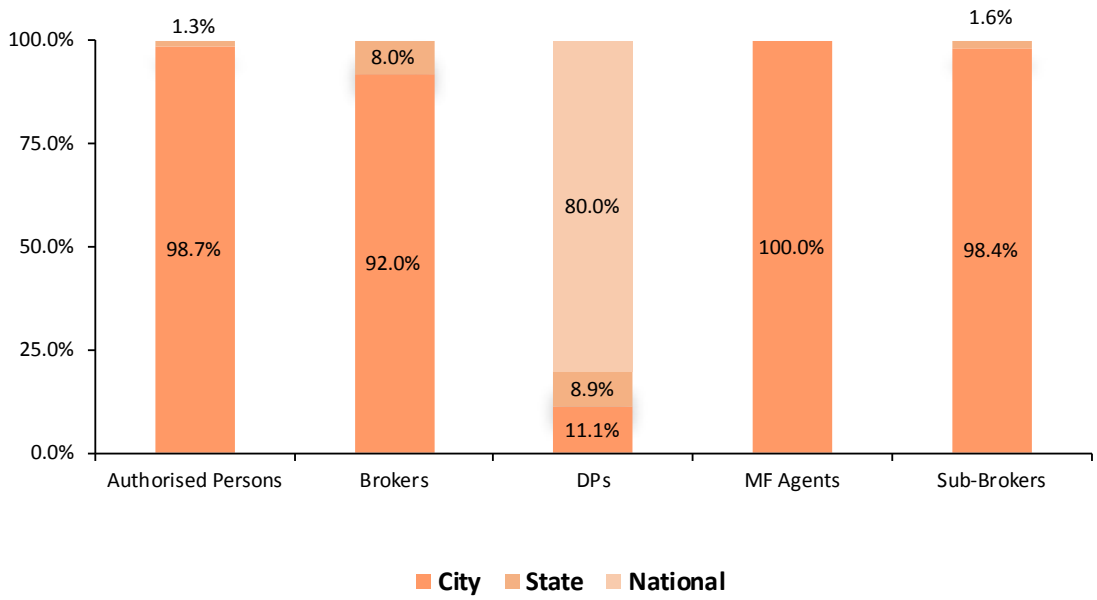
Figure 12.2: Number of Customers Serviced by Different Market Participants



N = 1,016 (Market Participants' Survey, SIS 2015)

Similarly for geographical coverage, the MPs vary in their footprints. As can be expected, nearly all APs, MFAs and Sub-brokers only function within their cities while 8 percent brokers function outside their city but within their state of origin. Not a single firm in these categories function outside the state lines. However, it is converse for DPs and only 11 percent of them are focused within their cities, and 80 percent reach out beyond their state of origin.

Figure 12.3: Geographical Base of Market Participants



N = 1,016 (Market Participants' Survey, SIS 2015)

Most market participants are in the securities market for over 10 years and among them, DPs even longer on an average (Table 12.1). It is likely that this is a sign of a survival bias among the responses for this survey. The shuttering of hundreds of MPs as discussed in the previous section has led to a visible consolidation in the industry, and the survivors of these consolidations are respondents to this survey.

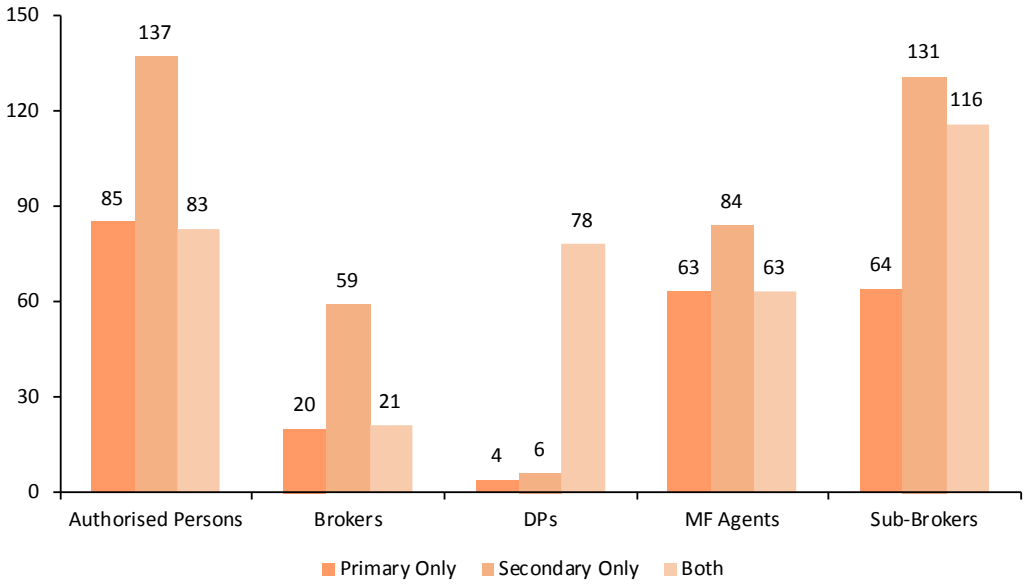
Table 12.1: Business Age Distribution for Market Participants

	Authorised Persons	Brokers	DPs	MF Agents	Sub-Brokers	Total
More than 10 years	187	78	88	118	169	640
5 to 10 years	107	17	1	80	123	328
1 to 5 years	9	3	1	9	19	41
Less than a year	2	2	0	3	0	7
Total	305	100	90	210	311	1016

N = 1,016 (Market Participants' Survey, SIS 2015)

The large scale closures of sub-brokers have also been balanced by the APs entering the markets. And among these market participants, while most primarily deal with secondary markets, DPs participate in both primary and secondary markets (Figure 12.4).

Figure 12.4: Market Focus (Primary or Secondary) of MPs

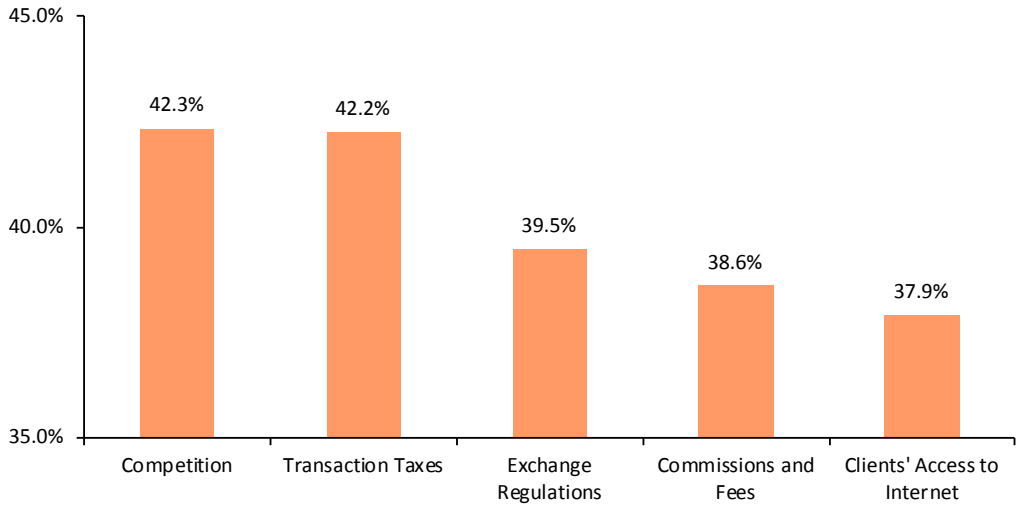


N = 1,016 (Market Participants' Survey, SIS 2015)

The Business of Market Participants: Information, Interactions, and Perceptions

The business of market participants is going through significant changes and upheavals, with rising competition from larger players in a shrinking business line. This is clearly reflected in the survey data as well (Figure 12.5). More than 40 percent of MPs have been negatively affected by competition in their business in the past 3 years. MPs also have lost out due to Transaction taxes (42 percent) and Exchange Regulations (38 percent). Lower commissions are marked visible from the global data as well, while client's access to internet, not a key reason, has started affecting the earnings of MPs. It can be expected to become one of the reasons as the internet savvy generations reach the age of investing, and clients, through their experience of e-commerce, become more comfortable with e-investing. SEBI has also taken significant steps in the direction of improving access to securities markets investing through the internet.

Figure 12.5: Top-5 Reasons for the Decline in the Market Participants' Business



N = 1,016 (Market Participants' Survey, SIS 2015)

The shuttering of broking firms/companies, the declines in the business of MPs (and its reasons) is apparently contradictory with the findings of SIS 2015, where it is reiterated often that financial intermediaries play an important role in retail investors' behaviour. When asked why participation rates in investment markets are low among retail investors, MPs felt that Safer Available Alternatives are the primary reason for low participation rates, followed by No 'Guaranteed Returns and Fear of Losing Money (Table 12.2). And the main Secondary Reason (most often Ranked II) is Volatility. This is somewhat in agreement with the investors view point where they find securities market comparatively risky. Most of the investors' responses clearly focused on various aspects of market risk (like volatility and inadequate returns) followed by lack of information as the primary issue they face with the markets.

Table 12.2: Reasons for Low Participation in Securities Markets

	Safer Alternatives Available	No Guaranteed Returns	Fear of Losing Money	Volatility	Lack of Corporate Governance	Accounting Malpractice	Market Manipulation
Rank I	297	272	187	112	99	37	10
Rank II	157	158	226	251	88	69	18
Rank III	103	103	70	103	73	81	12

N = 1,016 (Market Participants' Survey, SIS 2015)

But, the detailed survey also highlights crucial incongruities between financial intermediaries and their clients, that is, between the suppliers and the consumers of securities markets services. The reason behind why investors participate in the markets showcases this disconnect between MP and investor views. For investors, the reason why they participate in capital markets is primarily for capital gains, followed closely by improvement in lifestyle. Additionally, liquidity needs, and home buying also play a crucial role behind investing (Chapter 4, Figure 4.2). However, according to MPs, those engaging their services use it primarily for retirement and capital preservation, while capital gains and interests/dividends are ranked much lower (Figure 12.3). This might be an effect of the average age of investors using the services of financial intermediaries, that is, younger groups do not engage intermediaries and invest on their own, while those who do engage these intermediaries are older and this have a retirement focus. But, this data yet shows a strong disconnect between the risk attitudes towards securities market.

Table 12.3: Reasons for Clients to Invest in Securities Markets

	Retirement	Capital Preservation	Capital Gains	Interest/ Dividend	Regular Income	Tax	Liquidity
Rank I	293	279	228	101	99	10	6
Rank II	169	125	159	344	68	0	60
Rank III	26	44	48	103	17	22	38

N = 1,016 (Market Participants' Survey, SIS 2015)

Additionally, despite their central position in securities markets, MPs also showcase some biases and lack of information. While MPs mentioned 67 percent of their clients have engaged in panic selling, yet only 33 percent of them would urge investors not to sell during a sharp downturn. And though they have a clear idea of the risk-return-time horizon profiles of equities, mutual funds and bonds; in the case of derivatives, most MPs do not correctly perceive the comparative risk and returns profiles of derivatives (Table 12.4). In a 5-point scale, the risk, returns and time horizon required is ranked by MPs, with 1 as the least and 5 as the highest. It is clear that Equities are perceived as higher risk the MFs, which in turn are perceived higher risk than bonds. The reverse is true for returns expectations and time horizon require for optimal investing. These are purely in line with historical data and shows that MPs understand comparative risks of stocks, bonds and MFs. However, in case of derivative instruments like equity/currency derivatives and commodity futures, they are perceived lower risk and lower return instruments than stocks or MFs, showcasing the relative information shortage about these markets even amongst market participants.

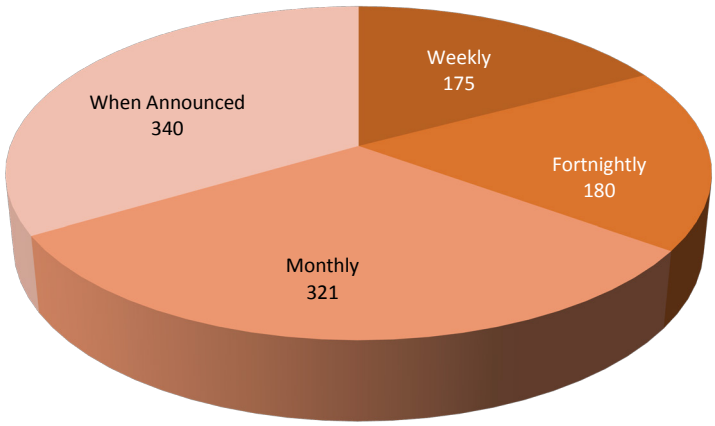
Table 12.4: Perceived Risk, Return and Time Horizon (Mean Score - 1 is Lowest and 5 is Highest)

Name of Instrument	Risk	Return	Time Horizon
Equities	3.3	3.3	2.9
Mutual Funds	2.7	2.7	2.9
Debentures	1.9	2.0	2.3
Derivatives	2.2	2.1	2.1
Commodity Futures	2.2	2.1	2.0

N = 1,016 (Market Participants' Survey, SIS 2015)

These disconnects could be considered in the light of the fact that a mere quarter of MPs have taken part in trainings provided by private and public organizations, despite 100 percent of participants being aware of them. These training programs have been run by SEBI, industry associations like AMFI, and larger private organizations like banks and mutual funds. MPs acknowledge that these programs can be helpful and 95 percent encourage investors to take these programs – while only 28 percent have participated in any of these programs. Additionally, the regularity with which they learn about policies and regulations too need to be improved with only 35 percent keeping track of policy and regulatory changes more often than once a month (Figure 12.6). Only 17 percent of respondents track policy changes every week or more often, while another 18 percent do so every fortnight. A vast percentage only hear about policy changes when they are announced and do not keep track of these on a regular basis.

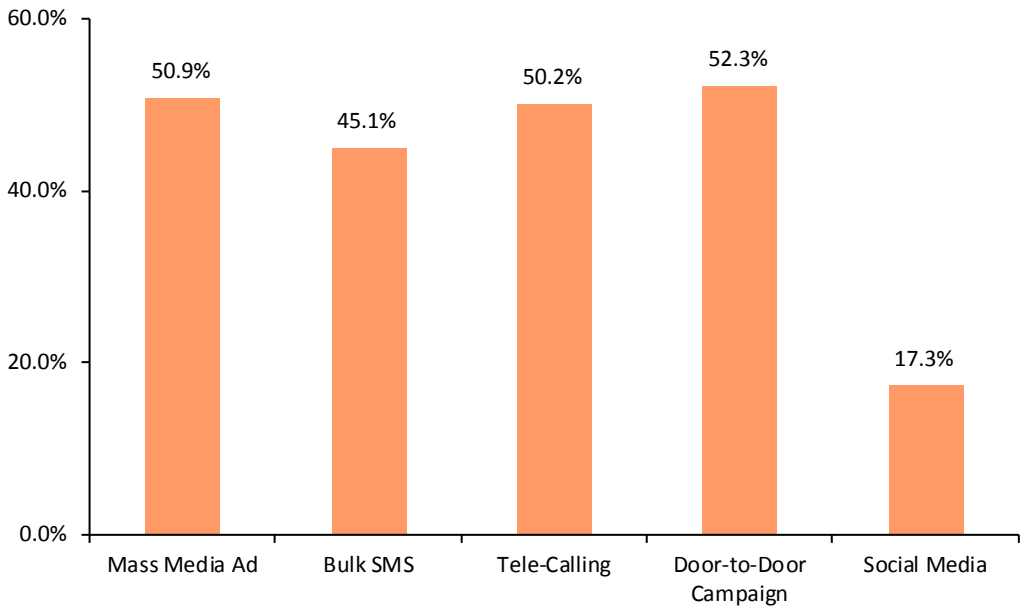
Figure 12.6: How often MPs Keep Track of Policy and Regulatory Changes



N = 1,016 (Market Participants' Survey, SIS 2015)

The competitiveness and the pressure on commissions and fees which affects MPs in the market is also clearly visible from the significant efforts that they are taking to acquire new clients (Figure 12.7), with over half using face-to-face interactions via door-to-door campaigns and similar numbers using mass media advertising (51 percent) and tele-calling (50 percent). Only 17 percent uses social media making it visible that similar to their clients, MPs also exhibit a preference for 'traditional' methods of conducting securities markets transactions. It is clearly unlikely that new clients would sign on to a securities market account simply by getting information on it from social media, despite the rise in such advertising over the past five years.

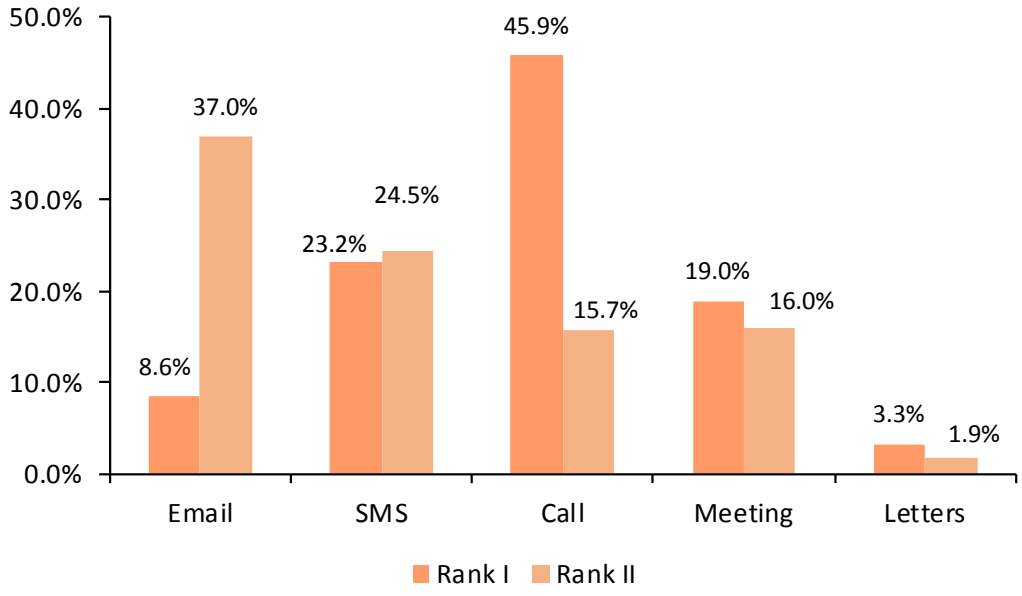
Figure 12.7: Methods for Acquisition of New Clients by MPs



N = 1,016 (Market Participants' Survey, SIS 2015)

Even when MPs reach out to their clients, this bias towards 'traditional' methods are consistently visible. Nearly 67 percent of MPs reach out to their clients at least once a quarter, with a majority of them even more often (Figure 12.8). And in nearly half of these interactions, MPs rank phone calls as the most likely instrument of contact, with nearly 20 percent preferring to meet in person and similar number using a SMS. While letters have completely become outdated, it is obvious that multiple channels of communication are open between clients and MPs and often email seems to be the most popular second line of communication.

Figure 12.8: How Often and via What Means do MPs Keep in Touch with their Clients



Daily	Weekly	Quarterly	Half-Yearly	Yearly
21.3%	15.6%	29.6%	26.7%	6.8%

N = 1,016 (Market Participants' Survey, SIS 2015)

However, in case of receiving information, the results of the survey were surprising and MPs showcase their tech-savvy image (Table 12.5). Over 40 percent ranked social media as their most important source of information, followed by company website (33 percent). Word of mouth and mass media seems to be the preferred second rank information source. It is thus clear that the reliance on traditional methods for client acquisition and customer relationships is primarily demand driven – the Indian investors are not yet comfortable with a complete online experience.

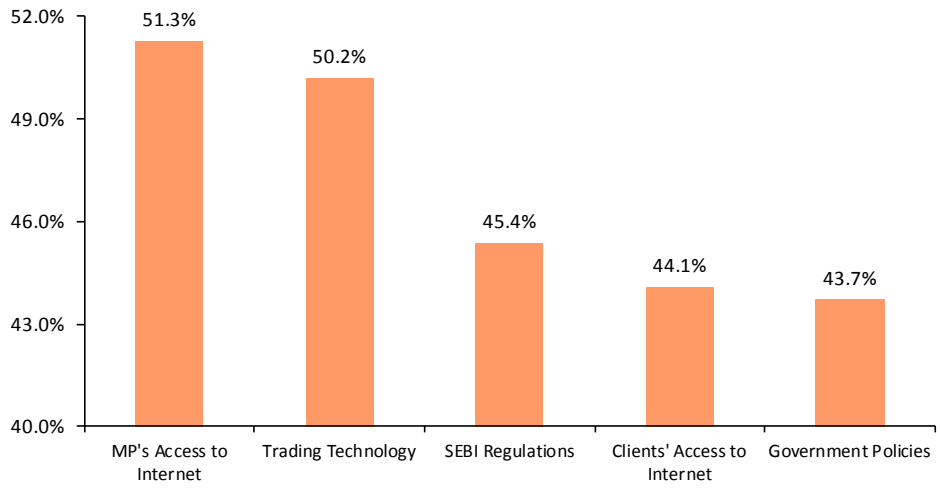
Table 12.5: Information Sources of MPs

Information Source	Rank I	Rank II	Rank III
Word of Mouth	5.1%	29.1%	8.6%
Mass Media	15.9%	27.4%	6.1%
Social Media	40.6%	17.9%	1.7%
Company Website	32.8%	13.6%	5.7%
Other Internet Sources	2.5%	6.1%	9.4%
Internet Forums	2.2%	0.3%	1.1%
Tips	0.9%	4.1%	0.3%

N = 1,016 (Market Participants' Survey, SIS 2015)

This affinity towards technology and its positive effects can also be observed from the changes in the business of MPs (Figure 12.9). Technology has been the primary reason for improving business for MPs, with web access (51 percent) and improved trading technology (50 percent) leading the top reasons for improvement of their businesses in the past five years. Both of these are reasons which can provide better margins and expansion possibilities across geographical boundaries. While the former seems to be useful for all types of MPs, the latter has not yet been exercised by most types of MPs, other than DPs who provide services at the national level. And, while regulation and regulator tend to be enumerated as a reason for lack of growth in many industries, especially in financial services, it is heartening to find out that the regulator's role has positively affected the business of the MPs.

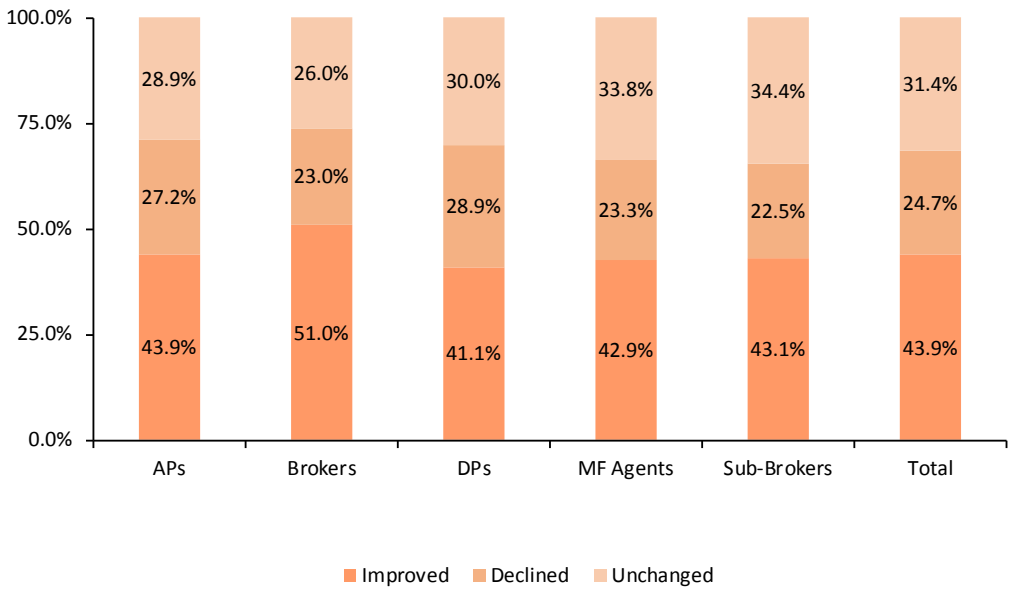
Figure 12.9: Top-5 Reasons for Improvement in the Market Participants' Business



N = 1,016 (Market Participants' Survey, SIS 2015)

Despite the wide-spread shutting down of MPs, only few in the current survey find that their businesses suffered in the past five years. This is arguably due to a survivor bias arising out of the consolidation in this industry. Despite the data on brokerages shutting shops, while 31 percent mentioned that their business was unchanged, 44 percent claimed their businesses had improved and only 25 percent said their business has declined in the past 5 years (Figure 12.10). This supports the Survivorship Bias hypothesis in the data as many players whose business declined sharply are out of business, thus survivors are benefiting from industry consolidation and have been surveyed as a part of SIS 2015.

Figure 12.10: How the MPs' Business has Changed over the Last 5 Years



N = 1,016 (Market Participants' Survey, SIS 2015)

This is one aspect of the survey which also holds true across different types of MPs, with about one-third mentioning that their businesses have not changed significantly, while about 40 percent seeing an improvement in the same time period and less than 30 percent finding some level of decline in their business.

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