Indian Public Policy Review 2023, 4(4): 84-92
https://doi.org/10.55763/ippr.2023.04.04.004

IPPR

Covid-19 and the Goalkeeper of the Indian Economy

S. Manjesh Roy[*]

Abstract

The decision and the conviction to keep the capital markets functioning amidst the uncertainty of COVID-19 lockdown, proved to be a game changer for the Indian economy. The robust systems put in place over decades and reinforced with measures to strengthen systemic integrity during COVID, revived the inherent trust in the Indian markets, especially at the retail level. The buoyant numbers of new trading and demat accounts opened, new investors in Mutual Funds etc. are a reflection of this trust. At a structural level, apart from decreasing dependence on FPI investments, the retail segment has witnessed a secular shift from savings to investment. Additionally, within investments, there is a shift from fixed income to equities. This deepening of the investor base has moved the Indian capital market to a higher orbit igniting a structural shift in the economy.

Keywords: Indian Capital market resilience, Retail shift to equities from debt, declining impact of FPI investment, deepening of investor base, structural shift in the economy

Publication Date: 09 August 2023

* The author works in the financial sector. The views and opinion expressed are personal.

1. Introduction

In a football match, the goal scorers hog the lime light and receive all the adulation. In contrast, the goalkeeper, who would have contributed equally, if not more to the victory by saving goals, does not elicit as much attention. This contrast was starkly brought out in the semi-finals of the World Cup 2022 in which Argentina defeated the Dutch 4-3 in penalty shootout. Lionel Messi celebrated this victory with his goalkeeper, who had miraculously saved two goals in the shootout, even as the rest of Argentina's team was huddled in jubilation with their final goal scorer.

We attempt to unearth similar such goalkeeper of the Indian economy during the COVID-19.

Similar to football, managing a country's economy is always a team effort, albeit more gigantic in scope and complexity. The executive and its various agencies, monetary authority, sectoral regulators, etc. each have their well-defined roles to play. In a watershed event, like the COVID-19, the complexity of managing the economy only gets compounded.

A plethora of measures were taken by each of the entities to address the unprecedented challenge of COVID. The outcome of these measures, along with externalities, is reflected in the present state of the economy. Simplistically, the outcome varies across segments and sectors of the economy ranging from fully recovered (financial sector), partly recovered (manufacturing), yet to get off the ground (employment) etc. During the possibly receding waves of Corona, this may be a good time to reflect and unearth the goalkeeper in this team game of managing the economy.

2. The facts

The deepening of the securities market in the COVID interregnum, is too glaring a phenomenon to be missed out (Table – 1). The average of the new trading, demat accounts, MF folios opened, average monthly inflow to MF Systematic Investment Plan (**SIP**) and the inflow to equity schemes of MFs, during the last three years (post COVID) are 381%, 418%, 50%, 29% and 14% higher, than their preceding three years (pre-COVID) period, respectively.

Table - 1: Select Data of Capital Market

(Number / Rs. in crore)

	2017-18	2018-19	2019-20	2020-21	2021-22	2022-23*
New Trading Accounts	1.25	1.30	1.59	4.21	9.89	5.86
New Demat Accounts	0.41	0.40	0.50	1.43	3.46	1.86
New Unique Investors in MFs	N.A.	1.93	0.15	0.20	1.09	0.30
New Folios of MFs	1.59	1.11	0.73	0.81	3.16	1.16
Average monthly inflow to MF through SIP	5,599	7,724	8,340	8,007	10,381	12,684
Net Inflows to Equity Oriented MF schemes (NFO + Purchases - Repurchases / Redemptions)	2,71,797	1,09,701	87,301	2,14,743	2,46,730	74,541
Equity Mobilized by Listed Corporates (IPO (Excl. OFS) + FPO + Rights + SME/IGP + QIP + Pref. Allot.)	1,66,315	2,27,181	2,88,496	2,08,483	1,60,939	91,935

Data Source: Websites of BSE, NSE, SEBI and AMFI

*March – 2023: data is till December 2022.

The open question is whether the above outcome was just a happenstance or a result of thoughtfully crafted policy measures? We explore the same.

In March 2020, when the lockdown was announced in India, COVID was still an 'unknown threat'. There were rumours swirling around, fanned by the social media, that roads would no longer be usable as they would be piled-up with human corpses. There was palpable panic all-round. On March 13 and 23, 2020 the SENSEX crashed by 10 % and 13 % respectively, triggering the circuit breaker, leading to the freezing of the market for 45 minutes. Even as leveraged 'investors' (margin traders / loan against shares, traders) were being roasted in this mayhem, short sellers and speculators were having a field day, fishing in troubled waters.

The simplest and safest decision would have been to just shut down the markets temporarily and wait. But this was not done. Instead, status quo was maintained. Not even the market timing was reduced, as was the case with the Forex markets[1]. Neither was short selling banned nor was any hurdle placed on the FPIs, who were exiting the market in droves, withdrawing Rs 1.18 trillion in March 2020 alone.

Instead, the margins were increased, enhancing the systemic integrity. It bears pointing out that the cited circuit breaker stoppage was not a knee-jerk reaction to the prevalent panic, but a mere compliance to the extant regulatory norms, which are already known to all the participants. This non-shifting of the goal post during the unprecedented times was an unambiguous signal that, come 'hell-or-high water', the (capital market) show must go on!

Unlike stress tests, which are theoretical exercises through simulations, the systems of the MIIs withstood real life extreme turbulence; SENSEX fell by about 39% from its peak of 42,274 on 20.01.2020 to 25,881 on 23.03.2020 and then rose by 63% to the cited peak on 09.11.2020, all without any failure in settlement.

Having thus reinforced the immutability of market functioning through surveillance measures, it was backed by a slew of measures on ease of doing business, onboarding, digitisation of the process etc. Specifically, norms for raising funds, rights issue, preferential allotment etc. were simplified. The concept of trading of rights entitlement was ushered in, opening a new avenue for investors. Pricing norms for stressed companies were relaxed. Growth companies were allowed to come out with IPOs, albeit without dilution of interest of retail investors.

A slew of relaxations and exemptions on various compliance norms for listed companies including for fund mobilisation, mutual funds, registered intermediaries were made, spanning across timelines, filing requirements etc.

Increasing the digitisation of the process, specifically the eKYC norms, was a game changer in as much as it enabled opening of a humongous number of trading and demat accounts online, even during the lockdown.

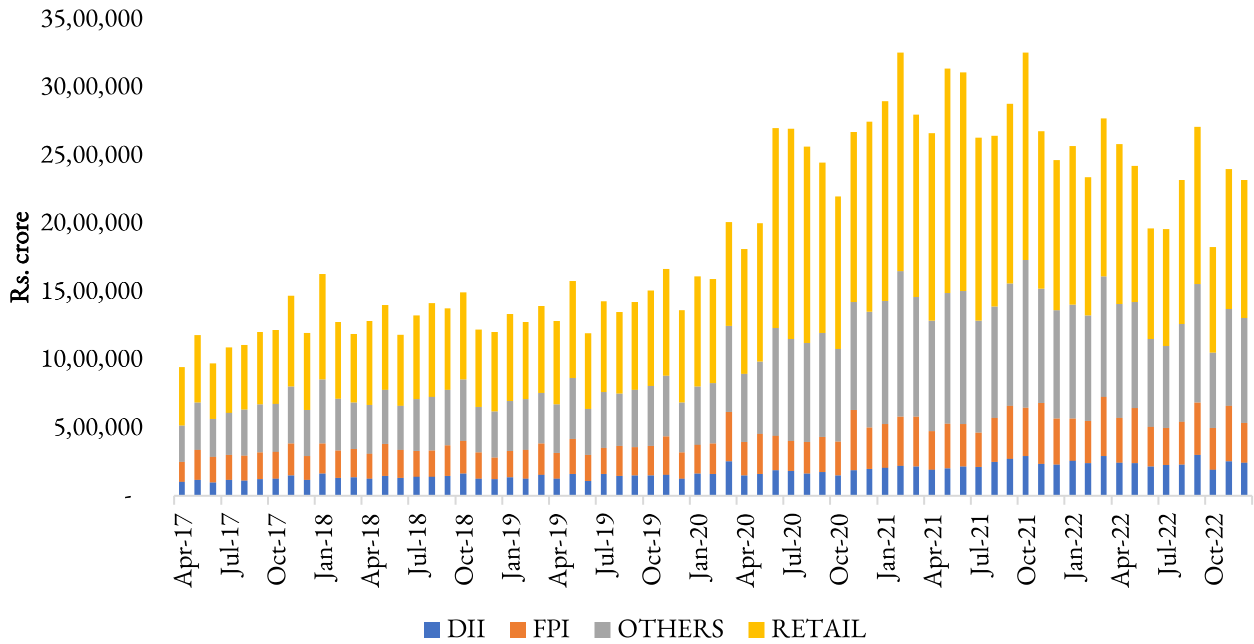
In parallel, RBI also came up with a slew of measures to mitigate the disruption caused by COVID. In addition to injecting durable liquidity of up to three years to banks and NBFCs & MFIs through LTRO and TLTRO in February and April 2020, respectively, the RBI also came up with the Special Liquidity Facility for Mutual Funds (**SLF-MF**) on April 27, 2020, to address the liquidity pressure on debt funds. Banks were eligible to avail this funding window to buy or conduct repo of debt instruments from / with MFs. This had a salutary impact as the redemption pressure abated; so much so that this facility was never required to be used at all.

However, much before the SLF-MF, the illiquidity problem cum redemption pressure brewing in certain debt schemes of an AMC since September 2019 got aggravated in the COVID panic. The Supreme Court verdict in the matter of Telecom Companies in January 2020, which, *inter-alia*, rendered the value debt paper of Vodafone zero, added to the woes of the debt market. Cumulatively, the aforesaid events led to the winding up of six debt schemes by that AMC on April 23, 2020. However, from February 2021[2] onwards, the investors of these six debt schemes started getting their money back as the value of the underlying instruments got restored. Nevertheless, it was the signalling impact of RBI's SLF-MF scheme, which stemmed the tide of redemption pressure on debt schemes.

The cumulative impact of the measures taken reinforced the trust in the markets and also ushered in the transition to the 'new normal' during COVID.

The trend in decoupling of the Indian capital market from FPI investments accelerated during COVID and thereafter became entrenched. Chart – 1 captures confidence of the retail investors as reflected in their dominance in the cash segment of NSE as a percentage of traded volume. In contrast, the falling share of FPIs in traded volume, practically mirrors that of the retail share, in the obverse.

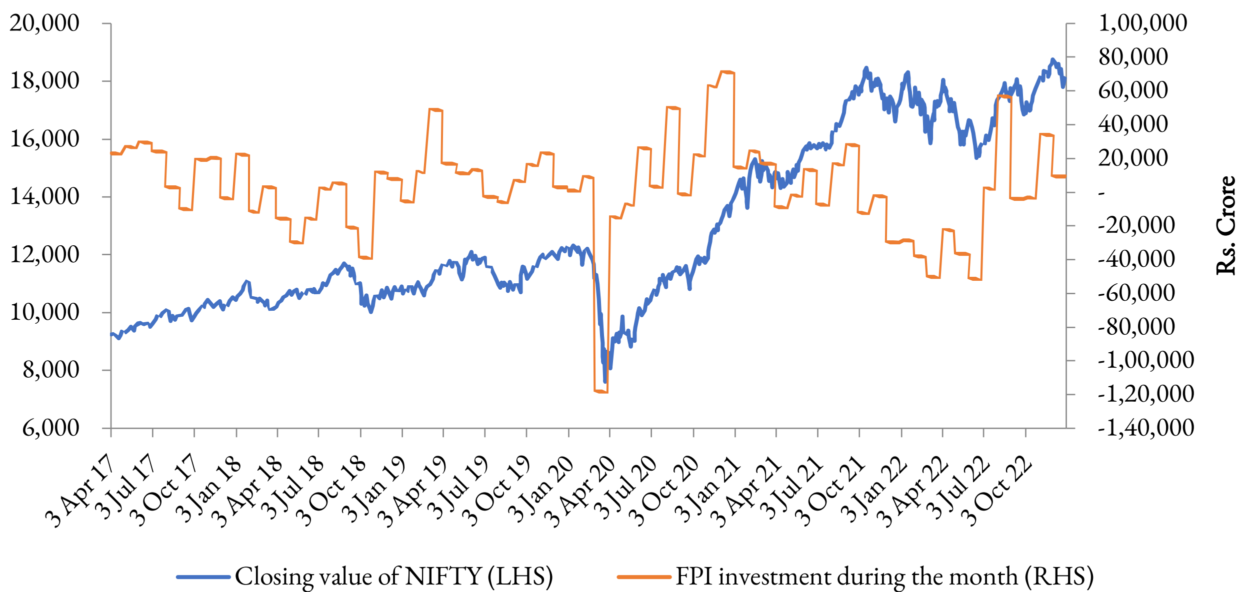
Chart – 1: Segment wise monthly traded volume in NSE, April 2017 to December 2022 (in Rs. crore)



Data source: NSE

Perhaps, based on this confidence exhibited by the retail investors and the steady participation by the DIIs, the FPIs returned from June 2020 onwards, followed thereafter by a mixed pattern, as captured in the Chart – 2.

Chart 2: NIFTY 50 (close) Vs. FPI investment, April 2017 to December 2022 (Rs. in crore)



Data Source: Websites of SEBI and NSE

This data implies that FPI outflows no longer have material impact on the Indian capital market. And yet, the line separating confidence from exuberance is indeed a very thin one, necessitating further deep dive.

3. Analysis

The growth of the capital market post COVID is attributed by some observers to the availability of cheap money and excessive liquidity. However, this attribution ignores the fact that capital market regulatory framework and MII systems are robust. Of course, low interest rates did help, but it also has had negative externalities.

RBI has been successfully borrowing gargantuan amounts for the Government year after year (Rs. 12 trillion in 2021-22 alone) at artificially low rates (financial repression), thereby keeping fiscal deficit and the public debt, low. However, the social impact of negative interest rates has been severe. In the movie 'The Mummy Returns', the soul of long since dead Egyptian priest gets resurrected and goes on to wreak havoc. Figuratively, the reversion to the taxpayer funded Old Pension Scheme (**OPS**) by some State Governments is equivalent to the return of the Mummy in public finance. Given the vociferous populist clamor, more financial weak States could resort to OPS[3]. The resultant impact on the combined fiscal and debt position of Union and State Governments, can only be negative.

In complete contrast, capital markets measures have had positive externalities. First, the average amount of equity mobilised by listed companies, (excluding the Offer for Sale component[4]), in each of the three-year pre and post COVID period has been a sizable Rs. 2.27 trn. and Rs. 1.54 trn., respectively (see Table - 1). Not surprisingly, the debt-to-equity ratio for listed companies dropped to the lowest in six years to 0.59 in 2020-21[5]. As much as high corporate leverage eventually leads to high NPAs in the banking sector[6], the record 10-year low net NPAs of 1.3% in September 2022[7] can be attributed to their deleveraging through equity mobilisation.

Second, the banking system did play its complementary role in ensuring smooth operation of payment and settlement systems even during the peak COVID. However, long before Core Banking Solutions was made mandatory for all bank branches (remember, outstation cheques took up to a week to clear?) it was the audacious transition by the stock exchange settlement to T+5, T+3 & T+2 in December 2001, May 2002 and April 2003, respectively, that hastened and catalysed the complete automation of the banking industry. This externality of capital markets has not received the recognition that it deserves and is worthy of a separate study[8].

The pertinent question now is whether the impressive increase in numbers pertaining to capital markets (in Table - 1) actually help in achieving its *raison d'etre*, namely, channelising savings into investments? And is this phenomenon a durable one? We examine the evidence.

First, equity mobilisation by listed companies and its externality of low NPA is dealt with already and hence not repeated here. Additionally, in terms of 'evidence of absence', it may be stated the lack of ADR / GDR issues by Indian corporates since 2018[9], is but a reflection on the availability of capital

as well as its ease of mobilisation in the domestic market. Further, 'reverse filliping'[10] by Indian start-ups, corroborates the aforesaid.

Second, the savings rate. The macro picture of savings and its components presents a complex scenario. The savings rate in the economy (i.e. of Govt. + Private + Households) has shown a secular declining trend and is a matter of grave concern (see Table – 2). However, the silver lining in this dark cloud is that the absolute contribution of households to savings increased from about 60% to 78.5% in this period. A golden sheen to this silver lining is that the net savings in financial assets[11] of the households (at 52.47%) exceeded their savings in physical assets for the first time ever in 2020-21. In other words, more resources are available in the economy from the households for furthering investments and thereby future growth.

Table – 2: Data on Savings

	2017-18	2018-19	2019-20	2020-21	2021-22
Savings as % of G.D.P.	32.07	31.75	29.87	28.24	N.A.
Gross Savings of Households in financial assets, as % of GDP (A)	12.03	11.98	11.95	15.70	10.82
Net Savings of Households in financial assets, as % of GDP (B)	7.64	7.90	8.03	11.63	8.31
Savings of Households in physical assets, as % to GDP (C)	11.65	12.45	11.54	10.54	N.A.
Net Savings of Households, as % of GDP (B + C)	19.29	20.34	19.57	22.17	N.A.
New Small Savings Scheme Accounts^ (in crore)	N.A.	4.66	4.12	4.11	2.33

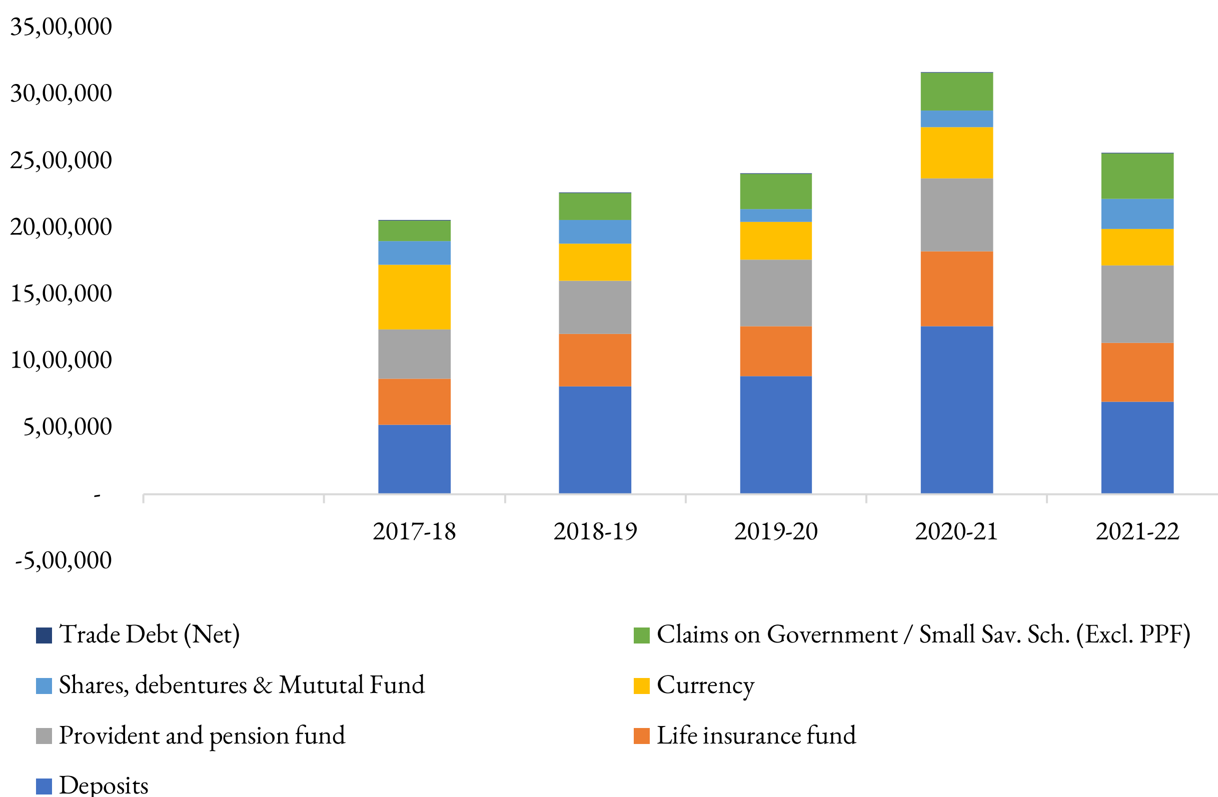
Source: RBI website & Lok Sabha Website

^ Till November 2021

The individual components of the household savings show an interesting behavioural pattern in the pre and post COVID period[12]. The constraints on spending during the lockdown, the increased need for precautionary savings and financial protection products led to a huge surge in the savings of households[13] in currency, deposits, and insurance policies in 2020-21 (see Chart - 3). Accordingly, the savings of households ballooned from (its medium-term average of) about 12 % of GDP in 2019-20 to 15.7% in 2020-21. Subsequently, as normalcy returned, spending also revived, leading to a huge reversal of holding in these three components in 2021-22, with deposits registering the largest fall. In absolute terms, savings of household fell from Rs. 31.62 trn. in 2020-21 (15.7% of GDP) to Rs. 25.6 trn. in 2021-22 (10.8% of GDP). However, bucking this trend, the investment by household (equity, debenture & MF units) showed an increase in absolute value from Rs. 1.25 trn. to Rs. 2.28 trn. in this period!

Intriguingly, the savings of households in small savings schemes also showed absolute increase during this period (see Chart – 3), although the number of new accounts opened shows a declining trend (Table – 2) coterminous with the increase in new accounts / folios in capital markets.

Chart – 3: Components of savings of Households



Data source: RBI website

Third, investment in Mutual Funds[14]. The shift in retail preference from savings to investment is evidenced in the MF industry, where individual investors held Rs. 23.56 trn. (about 58 %) of its Assets Under Management (AUM) (Rs. 40.76 trn.) in December 2022. Within investment, the shift from fixed income to equity is tangible as the AUM of equity-oriented schemes of MFs (Rs. 13.65 trn.) exceeded that of debt-oriented ones (Rs. 12.98 trn.) for the first time ever in March 2022[15]. And in July 2022, the AUM under equity exceeded 50% of the industry's AUM. Further, the retail preference for equity is overwhelming as 80% of their investments in MFs are in equity-oriented schemes and in turn, 89% of equity-oriented schemes are held by individual investors in December 2022. The increase in retail participation from Tier-3 and 4 cities, as mentioned in SEBI Annual Report, 2021-22, the steady and rising investments through SIP, irrespective of market gyrations, et al, are all subsumed in the above numbers.

The aforesaid indicates that there is a secular shift from savings to investment and within investment, there is a shift from fixed income to equities. These exuberant numbers would inevitably undergo mean reversion but would settle at a higher level. In other words, in terms of deepening, the Indian capital market has moved to a higher orbit and that is a structural shift in the economy.

While past performance is certainly not a guarantee for the future, the resilience exhibited by the capital market regulatory systems in overcoming the cascading challenges of the recent past, namely,

increasing interest rate cycle, liquidity tightening, unpredictable FPI movements, geopolitical uncertainties etc., indicates that the system is agile enough to respond to emerging situations.

4. Conclusion

As much as adversity is the true test of character, the COVID-19 provided a platform for the capital market regulatory systems to showcase its inherent robustness, resilience, and agility, built brick by brick over decades. Can we then give a big round of applause for the goalkeeper of the Indian economy?

Notes

[1] As a corollary to which the market timing of the currency segment of F&O was reduced and possibly that of Commodities F&O too.
[2] After the verdict of the Supreme Court in this matter.
[3] The link between the sustained period of negative real interest rate and the return to OPS is indirect - States with poorest financials have reverted to OPS to 1) save their monthly contribution to NPS & 2) use the corpus returned from NPS, to fill in their primary, revenue and fiscal deficit. As the incumbent will not be around when the unsustainable pension liabilities eventually become due for payment, the return to OPS is a cynical manipulation of legitimate public clamour for positive returns, into a populist measure.
[4] The concern raised by observers that large a component (about 70%) of IPOs is OFS, may not be entirely valid as OFS frees up capital to fund new investment by the PE Funds.
[5] India Inc's FY21 debt-equity ratio at 6 yrs low on massive deleveraging move, Business Standard, 11.01.2022
[6] FRDI Bill: Indian banking require a non-doctrinaire approach and not bail-in like western world, by the author, Money Life, 05.02.2018
[7] Financial Stability Report, RBI, December 2022
[8] Another externality deserving accolade is as follows. Way back in 2010, when the evil potential of media (including social media) in manipulating the public (like in the US elections) was not even fully recognized, SEBI metamorphosed itself from investor to citizen's protector, by causing media, i.e. entities outside its regulatory ambit, to disclose in their news reports, advertorials etc., any 'Private Treaty' (shares allotment in lieu of coverage) with listed or to-be listed companies. SEBI Press Release dated 27.10.2010.
[9] TaMo one of many as India Inc turns averse to ADRs and GDRs, Business Standard, 25.01.2023.
[10] Shifting of domicile back to India by Start-ups, Economic Survey, 2022-23.
[11] net of financial liabilities
[12] Vidya Mahambare, 'Our household savings are moving towards normalcy', Mint, 05.10.2022.
[13] Savings of households is calculated as the change in the opening and closing balances of stock of financial assets at the end of each financial year.
[14] Data source: AMFI website
[15] MF equity AUM surpasses debt, Business Standard, 18.05.2022