Sustaining the retail boom in capital markets

Retail investors should be empowered with appropriate analytics, enriched websites and unbiased decision-making tools

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The securities markets have leveraged developments in ICT (information and communication technology) in not just holding and transferring of securities but also in trading and settlement. The pandemic has brought in many new investors, connecting seamlessly through new-age brokers who have made investments and transactions in stocks a breezy and a less costly affair.

An SBI report on retail participation shows that the share of demat value of equity securities held by individuals has increased from 31.9 per cent in March 2020 to around 36.6 per cent in May 2021 for CDSL and from 13.6 per cent to 15.8 per cent for NSDL in the same period.

Ease of compliance processes, the spread of digital banking, the convenience of digitised document proofs, and comfort of monetary transaction through various digital modes (as evidenced by the 318 per cent growth by volume in UPI transactions and a 236 per cent increase in IMPS transactions from March 2020 to November 2021, according to NPCI) anchored the growth of retail in the securities markets.

While the retail participation in securities markets is a good sign in terms of financialisation of savings, the vulnerability to poor investment decisions due to the market noise and unsolicited research calls is also high. In terms of investment performance, the benchmark indices and the large-cap stocks of most sectors have been better performers. However, as for many mid- and small-cap scrips, their performance has not been the same between their peak during the pandemic and now. Even if one were to consider the top 500 stocks by market capitalisation, about 80 were losers while the majority 420 were winners during the last 52 weeks.

Stocks with a declining market capitalisation have seen extensive interest from retail investors, making them vulnerable compared to institutional players with well-researched financial information and direct connect with entities that informs them about growth plans and corporate governance issues.

Thanks to the meme stocks and the vitality of the 'FAANG' stocks in the US markets during the pandemic, retail participation in developed markets also peaked at 56 per cent (either directly or indirectly) in 2021. The history of capital markets with higher financialisation of savings, such as the US and the EU, reveals that participation in the equity market happens mainly through institutional investments than direct participation; unlike in India, which witnessed strong direct participation interests.

Information is key ISTOCK

Significant interest

In India, an analysis of holdings by various investors reveals a significant 16 per cent increase in retail stake (value terms) in the top 1,450 listed companies till year-end 2021. Even IPOs attracted retail investors to such an extent that of the six new offerings in the first quarter of 2021, three were subscribed more than nine times by retail investors. They seemed least bothered by the lethal impact of the second wave of the pandemic.

Prime Research data show that retail holding fell in 658 companies, and the average stock price of these companies increased by a much higher 44.51 per cent compared to the other 958 companies where retail holdings and their prices have also increased. What did the retail investors gain for their enthusiasm to invest in the securities market, moving money away from a low-interest rate instruments? Though one year is a short period,, Informed stock picking would have helped them avoid investing in stocks lured by vested interests.

To sustain the current momentum in the growth of retail participation, retail investors should be empowered with appropriate analytics, including stock performance metrics through various modes such as websites of intermediaries, including exchanges. Retail empowerment is also critical to sustain the enthusiasm for direct participation than through professional managers.

While the low-interest rate regime and increasing use of digital banking help attract retail investors, it is to reduce their gullibility that market intermediaries and infrastructure institutions provide them with the capability of data-based decision-making after taking into account their risk-taking capacity and investment horizon.

Though many authorised research providers give recommendations, they come at a cost. Training in data-based decision-making and common mistakes to be avoided in making investments are essential for retail investors. Market intermediaries led by exchanges should provide retail-investor-friendly websites, enriched with easy-to-digest data and financial metrics on stocks apart from e-learning modules for informed investing.

Like in India, in the US too retail interest in the equity market has been high during the pandemic, which resulted in the Gamestop stock blow-up driven primarily by internet forum Reddit.

While there are prohibitions around such activities in India, a proactive approach by market intermediaries led by exchanges in terms of enriched websites and supported by unbiased decision-making tools leveraging ICT is essential in preventing a reversal of the current 'bull run' and making retail investors wary of investing in equities.

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