INDIA: ASIA-PACIFIC'S NEXT MUTUAL FUNDS GIANT

The "Incredible India" slogan, so often used to describe tourist opportunities in India, could just as easily be used to describe the development and growth of the Indian mutual funds industry over the last 20 years. In September, we published a detailed report looking at the India funds market. Here are a few highlights.

India has become one of the world's fastest-growing economies. With a massive population, it is perhaps the only possible challenger to China in terms of emerging markets. Yet it has also had active capital markets for over 140 years, with stocks listed on the Bombay Stock Exchange (BSE) as far back as 1875.[1]

In aggregate, India's 24 different regulated stock exchanges comprise the world's 10th largest market with an overall capitalisation of more than INR154 trillion (USD2.2 trillion as of May 2019).[2] In recent years, these markets have begun to attract attention from global investors, following a period of strong returns. India has embraced technology and become a world leader in all aspects of IT development. As one of the original BRICS designations, it could be argued that, more than any other member, India has turned out the best for investors.[3]

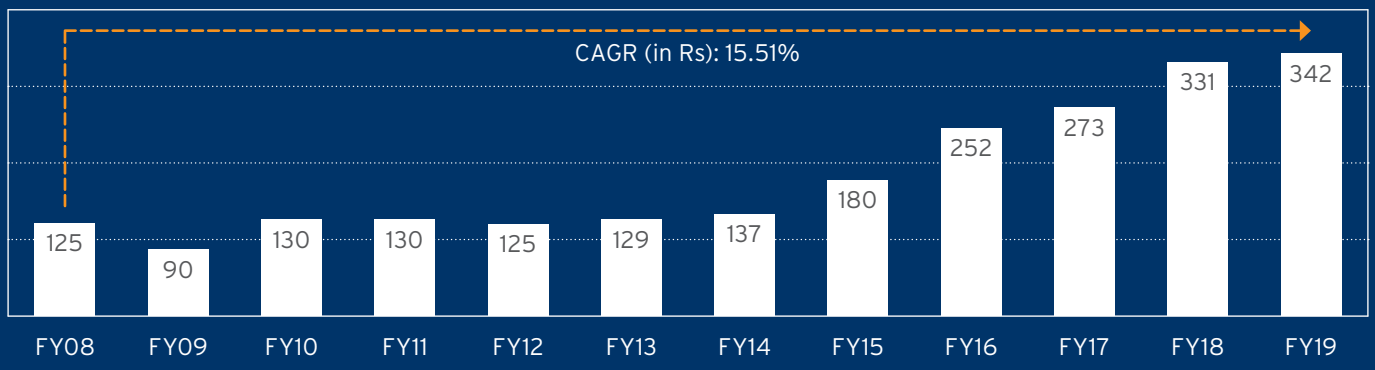
The development of India's mutual funds industry

The first unit trusts (mutual funds) were introduced to India in 1963 with the government controlled Unit Trust of India (UTI).[4] In 1987, new product providers entered the market. Initially these were major public-sector government-controlled banks. From around 1993, the private sector was allowed to enter with more dedicated fund management businesses that began to offer more diversified funds. There are now 44 mutual funds companies offering products covering a wide variety of investment choices. ETFs and hedge and alternative investment funds are also made available. However, there is little opportunity in the institutional space to manage assets for pension funds, unless they can be added to the list of approved managers for India's National Pension System.

Figure 1. Timeline of developments

Source: Citi. Data source: AMFI. Diagram: EY.

Figure 2. Mutual funds AUM (US$bn) 2008-19 [5]



Today the fund industry is not just thriving: it is growing very strongly and evenly split between institutional and retail investors, with the latter increasing their proportion rapidly as local stock markets perform well.

As at June 2019, the Indian mutual funds industry AUM stood at INR24.47 trillion (USD350 billion). CAGR for the last 10 years has been in excess of 15% per year.

Size and scale of India's domestic market

According to industry data, the numbers of investors in mutual funds in India is around 30 million, which represents less than 2.5% of the population. To date, the majority of fund sales have been made in the top 30 cities with Mumbai and Delhi having almost a 50% share. However, industry forecasts are projecting substantial future growth from second-tier (B30 or beyond top 30) cities and from schemes such as the Systematic Investment Plan.

The penetration trend beyond the B30 is still very patchy. There are almost 100 cities in India with a population in excess of 500,000 people, where the use of mutual funds is still at a very early stage of development.

HNWI, a rapidly growing sector

Within India, the numbers of high-net-worth-individuals (HNWIs) is expected to grow rapidly over the next few years. Their wealth holdings are estimated to exceed USD2 trillion currently, and could rise to over USD3 trillion by 2020.[6]

To meet the demand of these investors, there has been substantial growth in the numbers of private banks and private bankers operating in India. In mid-2018, it was estimated there were in excess of 2,500 private bankers in India, working for around 45 private banking firms.[7] This includes domestic Indian firms and the larger global players.[8]

In addition to investors within India, it is estimated there is a population exceeding 31 million non-resident Indians (NRIs) all over the world. These NRIs are often also more experienced in mutual funds investing, and have become a significant source of inbound capital and investment.

The Indian mutual funds market is fragmented. Of the 44 fully established and licensed businesses operating, 17 are either partly or wholly owned by foreign players. Many of the more recent entrants to the market have yet to establish any significant market presence. Often SEBI is encouraging them to set up outside the top 30 cities to enable a broadening of the market beyond existing wealth centres.

Figure 3 shows the top five mutual fund companies have a market share of almost 60%, leaving just 40% market share between the remaining 39 firms. Indeed, 30 firms have less than 1% market share each.

Given the rate of growth, however, it can be expected that there will be good opportunities in the next few years for smaller and newer firms to get better established and grow significantly. To do this will require both excellence in the product line-up and some degree of uniqueness in the manner with which products are being offered to the market.

Figure 3. Mutual funds managers in India with top 5 by market share [9]

	Name	AUM (US$bn)	Market Share %	Insurance Co. or Foreign owned	Who?
1	HDFC MF	51.79	13.99%	Part foreign & Ins	Aberdeen Standard Life
2	ICICI Prudential MF	48.18	13.11%	Part foreign & Ins	Prudential (UK)
3	SBI MF	43.93	11.60%	Part foreign	Amundi
4	Aditya Birla Sun Life MF	36.28	10.07%	Part foreign & Ins	Sun Life
5	Reliance MF	31.80	9.55%	Part foreign & Ins	Nippon Life
6	Kotak Mahindra MF	23.03	6.14%	100% Indian	
7	UTI MF	22.55	6.53%	Part foreign	T Rowe Price
8	Franklin Templeton MF	17.85	4.86%	100% Foreign	Franklin Templeton
9	Axis MF	14.60	3.67%	Part foreign	Schroders
10	IDFC MF	11.75	2.83%	100% Indian	
11	DSP MF	11.09	3.20%	100% Indian	
12	L&T MF	10.50	2.90%	100% Indian	
13	Tata MF	7.66	2.22%	100% Indian	
14	Sundaram MF	4.46	1.25%	100% Indian	
15	Mirae MF	4.18	0.99%	100% Foreign	Mirae
16	Invesco MF	3.52	0.98%	100% Foreign	Invesco
17	Motilal Oswal MF	2.81	0.78%	100% Indian	
18	LIC MF	2.33	0.62%	100% Indian	
19	Canara Robeco MF	2.26	0.60%	Part foreign	Robeco
20	Edelweiss MF	1.73	0.48%	100% Indian	
21	HSBC MF	1.66	0.45%	100% Foreign	
22	Baroda MF	1.60	0.46%	100% Indian	
23	JM Financial MF	1.10	0.36%	100% Indian	
24	Principal MF	1.04	0.29%	100% Foreign	Principal
25	BNP Paribas MF	1.03	0.29%	100% Foreign	BNP Paribas
26	IDBI MF	0.92	0.37%	100% Indian	
27	DHFL Pramerica MF	0.77	0.31%	Part foreign & Ins	Prudential (US)
28	Mahindra MF	0.71	0.19%	100% Indian	
29	Indiabulls MF	0.65	0.20%	100% Indian	
30	Union MF	0.62	0.17%	Part foreign & Ins	Dai-ichi Life
31	BOI AXA MF	0.45	0.15%	Part foreign & Ins	AXA Life
32	PPFAS MF	0.30	0.07%	100% Indian	
33	IL&FS MF	0.22	0.07%	100% Indian	
34	IIFL MF	0.22	0.07%	100% Indian	
35	Quantum MF	0.21	0.06%	100% Indian	
36	YES MF	0.20	0.08%	100% Indian	
37	Essel MF	0.15	0.06%	100% Indian	
38	IIFCL MF	0.08	0.02%	100% Indian	
39	Taurus MF	0.06	0.01%	100% Indian	
40	Quant MF	0.06	0.01%	100% Indian	
41	Shriram MF	0.02	0.01%	100% Indian	
42	ITI MF	0.01	0%	100% Indian	
43	Sahara MF	0.01	0%	100% Indian	
44	SREI MF	0	0%	100% Indian	
	Total	349.5	100%		

Can you mobilise a billion investors?

There can be no doubt that the Indian mutual funds market presents many complex challenges for all participants. At the same time, it offers outstanding opportunities. Where else in the world is there such a well developed market for investors with so small a level of actual participation by retail investors? Only in the last couple of years have retail investors begun to realise the benefits of mutual funds investing, especially using regular savings plans to accumulate assets and wealth. This aspect alone can only bode well for the future of the market, as investors become less susceptible to market volatility.

In March 2017, the Association of Mutual Funds in India (AMFI), on behalf of the industry as a whole, launched the Mutual Funds Sahi Hai investor education and awareness initiative. The initiative was designed to reach out to Indians across all states and languages through TV, digital, print and other media to allow them to self-educate on mutual funds through a website. The website offers simple content with articles and videos that prospective investors should find easy to understand. It also offers tools and calculators to help plan for life goals. The primary objective of the campaign was to increase the numbers of investors in mutual funds by more than 5 million a year.

Based on feedback to date, it appears to have been successful in achieving this goal. The campaign, in its second year, focused on using debt funds, attempting to increase the proportion held in such funds from a relatively low 10% of all investors.

Just by considering the size and scale of the Indian mutual funds market, an observer can quickly come to realise there has been extraordinary growth in the last 10 years or so. Yet, unlike many other markets in the Asia-Pacific region, the Indian market has been open for foreign participation, albeit in a more passive manner than may have been expected. Of the top 10 largest mutual funds companies, only two are 100% Indian owned. Some key statistics captured in figure 4 can help us understand the position a little better.

But it has not been so easy for foreign firms to enter the market and achieve success. Many have learned the hard way that they have needed to allow their business to develop domestically, rather than follow practices adopted in other substantial markets. Manufacturing local Indian-invested funds to be sold via banks and financial and wealth managers has proved the correct recipe.

Figure 4. Key statistics for India

>1.36 billion	US$2.2tr	7.3%	US$342bn	30m
Population of India	Size of the securities market	GDP growth in 2019	Size of the mutual funds market	Estimated number of retail investors

26.2m	150,000	124,000	44	19
Number of SIP investors	Number of HNWI families	Number of mutual funds distributors	Number of mutual funds companies	Number of ETF providers

With maybe more than 99% of all assets in the mutual funds business invested domestically, however, risk diversification becomes important — hence the interest of foreign firms to be able to sell their global expertise. This, though, is greatly restricted by India's strong foreign-exchange controls. While they do allow a proportion of assets to be invested in international markets, the total aggregate they allow is less than 2% of the size of the market, a figure that has by far yet to be reached.

This is perhaps in part due to the strong returns that the Indian securities markets have achieved over the last few years, together with the higher rates of interest that bank deposits earn. But the continued weakness of the Indian rupee will undermine this to some extent, and thus, as and when global markets achieve a more sustained period of growth, this might be a time when Indian investors become more interested to invest globally also.

Of course, it will not always stay like this. There will be a time when market conditions change and that is when many of the global fund managers operating in the market hope their positioning will enable their Indian businesses to capture a significant inflow.

Already, domestic mutual funds are able to access UCITS products from Luxembourg or Dublin within feeder or fund-of-fund routes. But these UCITS are not allowed direct entry to the Indian market at this stage and form a part of India's exchange controls.

Unlike most other major markets around the world, India does not offer much opportunity for global fund managers to participate in the institutional fund management market. The major Indian retirement funds have restricted opportunity to outsource their assets for management. Where they do, it is usually to the same eight managers that have been approved for use within the NPS. And getting added to that list has proven to be both time-consuming and problematic for most who have applied.

Similar to the mutual funds industry, the life insurance industry is also growing very fast. Many of the major life companies are also part-owned by global firms but conduct their business in a very domestic Indian fashion. As with the retirement industry, life companies are restricted on their ability to outsource assets for management by third-party fund managers. But many are directly connected to mutual fund companies, enabling them to have in-house access to investment management expertise.

The images of Indian Currency are used for representation purposes only

Should global fund managers consider entering the market?

This is the key question being asked by many global managers today. They look at the conflicting information, failures by some and success by others, and wonder which will be their fate. The reasons for participating are very compelling, but the willingness of global firms to allow a subsidiary to develop and grow on its own is still a rare occurrence. It is just not possible, nor have there been any examples of success, to parachute top international managers into India and grow a business from scratch. The size of investment required to participate, and the timeframe over which that success may be achieved, are such that only the most committed global firms have, until now, been able to enter the market.

The best route, and the one that has some degree of proven success, has been to partner up with a leading local enterprise to develop that business. This can be done either by acquiring one of the existing small mutual fund companies or more likely by working with one of India's many conglomerates wishing to add financial services to their portfolios. To some extent, the foreign partner would need to provide expertise in managing a mutual funds business, but they would also need to be prepared to recruit talented staff locally within India. Fortunately, there are plenty of such individuals, although, as elsewhere in the world, the top people are commanding top pay as well.

With the Indian population likely to grow to become the largest in the world within the next five to six years, and with GDP growth leading the economy to place between top three and five in terms of size within the next 10 years, India is certainly a most appealing market. Stable and supportive government has been a massive assistance and can be expected to continue to be supportive for the coming five years or more.

Can India become a global financial and fund management hub?

One of the long-held ambitions, not just of India but of many governments in the Asian region, is how can they become a financial hub or a fund management centre. This is seen as providing significant employment opportunities and thus economic growth. Often, there is a desire to emulate Hong Kong, Singapore or even Dubai, each of which has achieved this status.

For India, it does have many of the attributes necessary, such as scale, highly talented and well educated people, and financial markets. But it also has some inherent restrictions, such as exchange controls, a volatile currency and a lack of substantial foreign companies active in the local market. All these can change should the government be willing and market conditions allow, but in the short term it is unlikely to be achieved.

As economic growth occurs, personal wealth usually follows, and, as we have seen in India, many new millionaires and billionaires have been created over the last 15 to 20 years. These new wealthy HNWIs also dislike facing restrictions on how and where they invest their assets. Thus, many have been seen to be active in most of the world's expensive property markets. Many global private banks have benefited greatly from offering their services to this new wealth. India will need to be able to embrace this opening-up. This can be achieved through a gradual reduction in the enforcement of exchange controls. Enabling local investors more access to global stock markets especially via the mutual fund route, and possibly through use of UCITS products, under regulatory supervision might help.

This is a challenge that India will need to take on if it wishes to become more integrated with the world's financial community.

For more information on this topic, read our full report.[10]

Stewart Aldcroft
Chairman
Cititrust Limited

[1] Bombay Stock Exchange.
[2] From Wikipedia and www.ceicdata.com. Link Here.
[3] BRICS is the acronym for the five major emerging national economies or Brazil, Russia, India, China and South Africa.
[4] From Securities and Exchanges Board of India and from Unit Trust of India.
[5] From www.ibef.org. Link Here.
[6] From www.ibef.org, September 2017. Link Here.
[7] From "Wealth Management is the New Buzzword in Financial Services Sector" at www.economictimes.indiatimes.com. Link Here.
[8] From www.ibef.org. Link Here.
[9] From www.amfiindia.com. As at 31 March 2019. Link Here.
[10] See www.citigroup.com/emeaemailresources/gra30616_2019_IndiaCountryUpdate_v9.pdf Link Here.

Currency note: references to size and scale of assets, markets and other statistics originated in the Indian rupee (INR), which might have been stated in lakh or crore, part of the Indian numbering system. In most instances, these have been converted into the western numbering system and into US dollars so global readers can comprehend the scale in international terms. Because the rupee exchange rate against the dollar has varied considerably over the years (see appendix), the exchange rate used would have been applicable to the date of the statistic. So statistics in 2019 are based on INR70/USD1.

CONTACTS

If you would like to comment on any of the articles covered in this edition of *Global Trustee and Fiduciary Services News and Views*, share ideas for future content or write an article in the next issue, contact Amanda Hale, Andrew Newson or Matthew Cherrill at cititechnical@citi.com.

INTERNATIONAL

David Morrison
Global Head of Trustee and Fiduciary Services
david.m.morrison@citi.com
+44 (0) 20 7500 8021

Amanda Hale
Head of Regulatory Services
amanda.jayne.hale@citi.com
+44 (0) 20 7508 0178

Ann-Marie Roddie
Head of Product Development
annmarie.roddie@citi.com
+44 (0) 1534 608 201

ASIA

Caroline Chan
APAC Head of Fiduciary Services
caroline.mary.chan@citi.com
+852 5181 2602

Stewart Aldcroft
Chairman Cititrust Limited
stewart.aldcroft@citi.com
+852 2868 7925

EUROPE

Shane Baily
EMEA Head of Fiduciary Services
UK, Ireland and Luxembourg
shane.baily@citi.com
+353 1 622 6297

Jan-Olov Nord
EMEA Head of Fiduciary Services
Netherlands and Sweden
janolov.nord@citi.com
+31 20 651 4313

IRELAND

Ian McCarthy
Head of Fiduciary Services, Ireland
ian.mccarthy@citi.com
+353 1 622 0349

LUXEMBOURG

Patrick Watelet
Head of Fiduciary Services, Luxembourg
patrick.watelet@citi.com
+352 451 414 231

Pascale Kohl
Fiduciary Relationship Manager
pascale.kohl@citi.com
+352 451 414 279

Ulrich Witt
Fiduciary Relationship Manager
ulrich.witt@citi.com
+352 451 414 520

SWEDEN

Johan Ålenius
Head of Swedish Fiduciary Services
johan.alenius@citi.com
+46 8 723 3529

UNITED KINGDOM

Thérèse Craig
Head of Trustee and Fiduciary Services - Edinburgh
therese.craig@citi.com
+44 (0)131 524 2825

Richard Thomas
Head of Trustee and Fiduciary Services - London
richard.thomas@citi.com
+44 (0) 20 7508 4880

Fiona Craig
Fiduciary Client Manager
fiona.craig@citi.com
+44 (0) 131 524 2881

Iain Lyall
Senior Fiduciary Client Manager
ian.lyall@citi.com
+44 (0) 20 7500 8356

REGULATORY SERVICES TEAM

Andrew Newson
Senior Fiduciary Technical Analyst
andrew.c.newson@citi.com
+44 (0) 20 7500 8410

Matthew Cherrill
Senior Fiduciary Technical Analyst
matthew.charles.cherrill@citi.com
+44 (0) 20 7500 3382

www.citibank.com/mss

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