

Fresh P-notes investments flood market

Rajesh Bhayani / Mumbai December 28, 2007

100 more FIIIs registered with Sebi even as grey areas remain

Fresh investments through participatory notes (P-notes) are flowing into the cash market in huge quantum. The rush of investments is because foreign institutional investors (FIIs) have enough headroom to invest through P-notes.

Sources said some of the recent high-profile initial public offers (IPOs) had seen a good amount of money coming in through P-notes, with FIIs' P-notes issues falling within the Securities and Exchange Board of India's (Sebi) stipulation.

Sebi has restricted P-notes investments in the derivatives market, asking the investors to unwind their positions within 18 months. At the same time, the regulator has permitted P-notes investment in the cash market up to 40 per cent of the FIIs' assets under custody.

An incremental 5 per cent increase in P-notes investment has been allowed, subject to the reach 40 per cent level. P-notes are offshore derivatives instruments (ODIs) issued by FIIs to investors, who do not come under Sebi's supervision.

According to sources, the new funds coming through P-notes are better regulated by Sebi. Earlier, sub-accounts of FIIs were issuing P-notes, which is not the case on Thursday.

As a 5 per cent annual increase is allowed through P-notes investment, FIIs are eligible to issue fresh P-notes in 2008, according to a broker.

There is a general perception that the recent sell-off by foreign institutional investors (FIIs) could be triggered by unwinding of their P-notes positions. However, this is only partially true.

A major part of the unwinding in P-notes is taking place in the derivatives market, with the cash market seeing some unwinding of positions. Yet, fresh investments are coming through issue of fresh P-notes.

Siddharth Shah, head of funds, Nishith Desai Associates, said, "Sebi has certainly simplified the registration procedure for FIIs and the number of registered FIIs is rising. Some issues still need to be addressed as certain FII applications are being deferred pending policy views on the Mauritius-registered entities and the like."

"Sebi is also expected to issue a new circular clarifying what the regulated entities mean for the issue of ODIs/P-notes, the absence of which is creating some ambiguities as to who would be deemed regulated for holding ODIs."

Meanwhile, many sub-accounts have got themselves converted into FIIs and there is no pressure on them now to square off their investments through P-notes.

Since Sebi's restrictions on P-notes in mid-October, 101 new FIIs have been registered, taking their total tally to 1,214. The number of new sub-accounts has increased by 181, bringing their number to 3,626.

ON FULL STEAM

- Recent high-profile IPOs have seen a good amount of money coming in through P-notes
- Funds are rising as FIIs have enough room to issue fresh P-notes
- Sebi's simplification of the registration procedure has led to the number of registered FIIs rising