

Liberal norms for QFIs soon to spur capital flows

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New Delhi The Securities and Exchange Board of India (Sebi) is looking to relax some of the processes to make it easier for qualified financial investors (QFIs) to buy stocks in India. The regulator plans to allow QFIs to buy stocks directly through a stockbroker instead of asking them to route funds through a qualified depository participant (QDP). Although QFIs were allowed to buy Indian equities in January, the requisite trading infrastructure is not in place.

The finance ministry, however, does not plan to relax the requirement of having a permanent account number for a QFI to invest in India. Meanwhile, however, the regulator has given permission to 27 QDPs to set up shop to enable QFIs to buy Indian stocks and equity mutual funds. The proposed easing of the route for QFIs to buy stocks is expected to catalyse capital inflows and address, to some extent, the mismatch between the current account deficit and capital flows which has caused the rupee to depreciate.

Sebi officials believe that over time QFIs could replace investments coming through participatory notes (P-notes). P-notes are derivatives products with stocks and derivatives as underlying assets and are issued to overseas investors who cannot directly invest in Indian stocks. The total value of P-notes on equity, debt and derivatives stood at R1.65 lakh crore as on March 31, 2012, according to Sebi data.

As per the existing dispensation, a QFI is required to remit funds to a rupee pool account of a QDP and place orders with the QDP which then verifies the funds and securities and communicates the order to the broker.

However, the new move may not be enough to persuade QFIs to invest in India. Kishore Joshi, senior associate with law firm Nishith Desai Associates, points out that there needs to be an intermediary in India who should monitor the investment limits of QFIs, the funds that are coming in and going out and, importantly, meet the QFIs' know your customer norms. "The primary reason for QFI investments not taking off was the responsibilities vested with the QDPs. If the DPs are bypassed, who will be responsible for monitoring the process and communicating with the regulators?" he asks.

Joshi adds that allowing QFIs to trade directly through brokers should be fairly simple. "There are many HNIs (high net worth individuals), family offices that are keen on coming to India under the QFI route and such a move would encourage them," he says. Market watchers believe that ideally Sebi should open up the QFI route to non-resident Indians as well, as they are already treated at par with foreign investors under the FDI route, except for a couple of sectors.

The government earlier this year liberalised rules for investment in the Indian equities market by permitting a new class of investors – QFIs – to invest in India. "We have given approval to 27 QDPs. They are putting in place requisite infrastructure after which trading can begin," a Sebi official said. QFIs comprise foreign individuals, foreign pension funds and foreign trusts, and can invest directly in stocks and equity mutual funds. In this year's Budget, the government permitted QFIs to buy corporate bonds, the framework for which is being finalised.

A suggestion has also been made to Sebi that QFIs can be allowed the option to appoint a local custodian of securities. A QFI can hold a maximum of 5% of the paid-up equity capital in a single security. All QFIs can hold up to 10% of the paid-up equity capital of a firm. The former limit will be monitored by QDPs, and the latter by depositories NSDL and CDSL.

Time to relax

- * Qualified financial investors (QFIs) currently route funds through qualified depository participants (QDPs)
- * Sebi has allowed 27 QDPs to set up shop to enable QFIs to buy stocks and equity mutual funds
- * Over time, QFIs could replace investments through P-notes, which have a value of R1.65 lakh crore as on Mar 31
- * The finance ministry, however, does not plan to relax the requirement of having a PAN card for a QFI to invest here