SEBI's decisions will help in the long-term growth of the mutual fund industry

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SEBI's decisions will help in the long-term growth of the mutual fund industry. The Securities and Exchange Board of India (SEBI) has been continuously amending the rules governing the mutual fund industry over the last couple of years, and continued this practice in its recent board meeting too. The changes this time are, however, welcome as they seek to increase penetration of the industry and improve governance at fund houses. The decision to relax the profitability criteria for entities floating a mutual fund asset management company (AMC) will allow companies that are constrained by their past profitability record to launch an AMC. There is a definite need to improve the penetration of mutual funds in the country. The number of mutual fund folios and demat accounts show that just 2 per cent of the population is investing in these instruments. Of the household financial savings, mutual funds account for only 7 per cent. The assets of the fund industry are also concentrated in larger cities with only 16 per cent of these originating beyond the top 30 cities.

Improved communication network along with the proliferation of smart phones has made available a large set of young investors who are willing to invest through tech-enabled platforms. These platforms can now start an AMC to service their existing customer base. SEBI's rule about doubling the net worth requirement for the new entities — to be maintained at ₹100 crore until the AMC makes profits for five consecutive years — is a good decision, but the regulator also need to screen the experience, intent and past record of the promoting entity closely. The other important change relating to mutual funds — ring-fencing assets and liabilities of mutual fund schemes — will also protect investor assets. While the schemes are currently required to maintain segregated bank and securities accounts, this proposal will make fund houses adhere to this rule and not retain securities in pooled accounts. Segregating liabilities will ensure that assets of one scheme are not utilised to settle borrowings of others.

The other important change seeks to reduce price volatility in stocks that list following the implementation of a resolution plan under the Insolvency and Bankruptcy Code. Mandating such companies to have 5 per cent public shareholding at the time of re-listing will ensure that lack of public float does not result in a sharp upward spiral in stock price. The graded improvement in public holding to 10 per cent in 12 months and 25 per cent after three years will give promoters ample time to sell their shares without disrupting the price. Additional disclosures — regarding the resolution plan including details of assets after the resolution, details of the lien on the companies' assets and other material liabilities imposed on the company, steps to be taken by the investor for achieving the minimum free float — will help provide guidance to investors who may find value in such shares and may want to invest.