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## Margin mayhem: Iron out pain points for delivery-based investors



**While SEBI's new margin rules are undeniably well-intentioned and designed to protect retail investors from the consequences of broker fraud or misinformed trades, they do have a flip side**

Despite multiple deadline extensions, the stock market's transition to SEBI's new framework for upfront collection of margins on cash trades and security pledging was marred by a rocky start last week. With tech glitches holding up execution, investors reported unprecedented delays in pay-ins and pay-outs from their trading accounts for the first time in years. As cash market volumes fell by 10-20 per cent, brokers, depositories and exchanges engaged in an acrimonious round of finger-pointing. This glitchy start has led to demands that SEBI recall its November 2019 circular, which ushered in the new margin rules. Conceding the demand would be akin to throwing the baby out with the bathwater, as it had many welcome elements.

The changes from September 1 contain two essential elements to protect investor interests in the aftermath of the Karvy controversy. SEBI has now allowed investors to directly pledge their shares with the Clearing Corporation, thus doing away with the earlier practice of investors lodging their shares with their brokers towards margins, rendering them vulnerable to misuse. SEBI has also disallowed the practice of brokers treating stocks in client demat accounts for which 'power of attorney' has been given, as collateral for trading purpose. It has also asked brokers to levy upfront margins on transactions in the cash segment just as they were doing on derivative trades, to discourage highly leveraged bets in these uncertain times. While SEBI's new rules are undeniably well-intentioned and designed to protect retail investors from the consequences of broker fraud or misinformed trades, they do have a flip side. For one, they introduce irritants for long-term investors effecting delivery-based transactions. With both buy and sell trades attracting upfront margins now, even investors holding securities in their demat account are obliged to either cough up an advance in cash or enable early pay-in of their securities

before initiating sell orders. With a significant section of brokers not yet geared for early pay-in, they've been requesting clients to deposit cash margins with them, resulting in undesirably high floats with the broker. Given the extant T+2 regime, the new margin rules also prevent investors from immediately using the full proceeds from the sale of shares towards new purchases or deploying intra-day profits in new trades. The new mechanism to pledge and re-pledge shares used as collateral is an improvement as the shares remain in client account and a clear trail is available. However, SEBI should see if there is scope for further simplification to smoothen the order execution process.

SEBI must try and iron out impediments for delivery-based investors by actively engaging with market participants and over time pushing for real-time settlement. It must also recognise that writing new regulations for the market at large cannot substitute stringent enforcement actions against specific brokers or market participants found to be perpetrating, aiding or abetting in securities fraud. Finally, given that the bulk of trading activity in any market originates from speculative rather than long-term investors, SEBI needs to strike a balance between protecting small investors and curtailing speculation, as the latter has adverse consequences for market depth and liquidity.

## **Too close for comfort: On India-China border row**

### **India and China must lose no time in finding a diplomatic solution to their border disputes**

Following Friday's talks in Moscow between the Defence Ministers of India and China, the prospects of an imminent diplomatic solution to the continuing stand-off along the LAC do not appear bright. The statements issued by the two sides have underlined the sharp differences in how New Delhi and Beijing have continued to view the unprecedented developments along the border since May, when China deployed troops in large numbers and sought to unilaterally redraw the LAC in several areas. Defence Minister Rajnath Singh "categorically conveyed" India's stand, emphasising that China's actions "were in violation of the bilateral agreements". He also expressed hope that both sides would be able to resolve the ongoing situation "peacefully through dialogue". His Chinese counterpart, General Wei Fenghe, appeared to only reiterate the stand conveyed by China in recent statements that it had no blame to bear for this summer's developments. He said "the responsibility lies entirely with the Indian side", while China "kept maximum restraint to prevent potential escalation". He called on India to "immediately withdraw its troops". He did, also, add that both sides should "stay committed to resolving the issue through dialogue and consultation" and "make joint efforts to meet each other halfway".

As External Affairs Minister S. Jaishankar said last week, diplomacy is the only way out of the crisis, and that can only happen "if both sides understand that it is in each of their best interests if the events of this summer are not repeated". The problem, so far, has been a stark mismatch between China's statements and the actions of its troops. Its consistent labelling of India as the aggressor this summer contradicts the reality that India

has, since May, ceded about **1,000 square kilometres in Ladakh to Chinese control**. If China's diplomats have spoken repeatedly of the need to keep in mind "the big picture" of bilateral ties, the actions of its military on the ground have suggested an intent that is precisely the opposite, emphasising achieving tactical gains at the border over the broader strategic relationship. Until that calculus changes, India will have to be prepared to be tested along the border and to stand its ground over the long haul. India has signalled its intent to do so with the latest **developments on August 29** in Chushul. If the statements following the Moscow meet did not exactly inspire confidence, both sides will have the chance to reassess the situation when Mr. Jaishankar will likely meet his counterpart, Wang Yi, at a meeting of SCO Foreign Ministers on September 10. Military talks can occasionally help to avert a flare-up, but the two neighbours need to work toward a diplomatic solution to ensure undisturbed peace and quiet along the border.

## **Mixed messaging: On India as an investment destination**

**India's efforts to attract capital will not result in a flood of FDI till investors see policy stability**

Prime Minister Modi last week elaborately **pitched India as an investment destination** that could serve as a manufacturing hub at the heart of global supply chains. The pitch made at the U.S.-India Strategic Partnership Forum comes in the backdrop of the government's keenness to use the disruptions the COVID-19 pandemic has caused to the cross-border movement of goods as an opportunity to lure potential investors, especially those looking to relocate from China, to India. This tack is consistent with recent initiatives to explore supply-chain synergies with other economies, including Japan, as an escalating border feud casts a shadow over India's economic and trade ties with its northern neighbour. The reasoning appears to be that if even a few multinational enterprises can be drawn to set up manufacturing bases, either by shifting facilities or as new additional plants, then not only does the Indian economy stand to gain FDI, new jobs and tax revenue but it also makes a statement. Clearly, officials must have advised Mr. Modi that U.S. businesses were the ideal target given the worsening relationship between Washington and Beijing and the ongoing trade stand-off between the world's two largest economies. On the face of it, the approach seems inarguably sound. The rub, however, lies in the government's recent 'Aatmanirbhar Bharat' initiative, of making India more self-reliant.

Over the decades, it has been established that global FDI investors prioritise and are even willing to pay a premium for policy stability and largely barrier-free access to local and international markets. The drive for self-reliance has spurred several Ministries to urge companies and industry sectors to replace imports with 'Made in India' substitutes. From the Shipping Ministry's call for the design and manufacture of indigenous tugboats to auto component makers being told to abjure foreign parts, the thrust of the initiative is evidently 'import substitution'. It is hard to imagine any potential foreign investor in manufacturing being ready to source capital goods locally — assuming they are available — even at the

cost of possibly compromising on quality or price or both. Betraying the government's anxiety, Mr. Modi took pains to stress that the push for self-reliance should not be interpreted as India turning its back on the world. Separately, from the market access perspective, India's decision to not join the RCEP multilateral trade pact would put investor companies seeking to tap consumers in RCEP member countries at a tariff disadvantage. Interestingly, most of the recent FDI announcements have been by way of stake acquisitions in existing businesses, and predominantly in the services sector. Attracting FDI into manufacturing will require the government to convince investors that it is committed not merely in words but in deeds as well to an open, barrier-free global trade and investment order.