Educate retail investors

Enough guidelines to curb market speculation exist; we need awareness drive to not always bet on quick returns

INVESTMENT GURUS, ESPECIALLY mutual fund managers, have spent decades explaining the benefits of long-term investing. This is sound advice as many top mutual fund schemes have delivered stellar returns of over 20% compound annual growth rate (CAGR) over the past two decades or even more. But an ever-growing number of investors seem to have little patience for this long-term story. As a study by the Securities and Exchange Board of India (Sebi) for FY23 reveals, 54% investors, excluding anchor investors, have sold their shares allotted in the initial public offering (IPO) in the very first week. More importantly, 67.6% retail investors (by value) exited in the first week with profits of over 20%, but 23.3% sold even if they were in losses.

What is interesting is that almost a quarter of the retail investors are playing the IPO market for quick gains and do not mind incurring losses in the short term. In fact, they could possibly be deploying the funds in the next IPO, hoping to make up for the losses. They don't seem to be deterred by the short-term capital gains tax of 15%. So, instead of waiting for over 20%-odd CAGR for over 20 years, they are happy earning 17% post-tax within days. The IPO boom is also supporting the "quick buck" phenomena. In FY24, 36 out of 76 mainframe IPOs returned over 20% in the first week. The numbers have only become better in FY25, with 16 out of 25 IPOs returning over 20%, according to data from Prime Database.

The flood of liquidity has clearly overshadowed the pitfalls, resulting in complacency. Consider the frenzy in the small and medium enterprises (SME) IPO market. Recently, an auto dealer's ₹12-crore IPO received bids of over ₹5,000 crore. No wonder, Sebi is worried. In the past couple of weeks, its wholetime member Ashwini Bhatia has spoken about stricter guidelines for SME IPOs by the year-end. The market regulator has also taken the unusual move of issuing an advisory to investors asking them to be careful as promoters seem to be painting an unrealistic picture to garner more bids. Last October, it also asked the two exchanges — BSE and NSE — to put these stocks under additional and graded surveillance measures.

But one doubts whether all the advisory or stricter rules will have a significant impact on investor frenzy for IPOs — both SME and mainframe — when sheer greed is the main driving force. With 80% of mainframe IPOs closing above listing price after a week, the roll of the dice is heavily in favour of the investor at this point. To curb speculation, Sebi has already floated a consultation paper which, if implemented, will make things difficult for retail investors in the derivatives market. The Union Budget has also increased the securities transaction tax on options and futures, which will be implemented from October 1. But one doubts whether additional guidelines to curb speculation in the IPO market would serve any purpose — after all, enough of them exist already. What is required is a concerted effort to educate retail investors that they should not confuse stock markets with gambling dens. Education is a long-term and a more difficult process than issuing more guidelines, but that seems to be the only way forward. We have for long believed in the maxim that market is the best teacher, but it's time to change that belief. Quick returns can never be taken for granted.