

The quiet death of ADRs: Why investors no longer need Wall Street's window into India

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Summary

As India integrates deeper with global markets, the need for offshore access via ADRs is fading. Price discovery has moved onshore, reshaping how global capital engages with Indian equities.

MUMBAI: It was past 10:30 at night in India when HDFC Bank announced that its part-time chairman Atanu Chakrabarty had quit, triggering a scramble in New York where traders dumped its American Depositary Receipts (ADRs). For the first time in nearly four years, HDFC Bank ADRs traded at a discount to its shares in India. When Dalal Street opened the next day, HDFC Bank fell by more than 5%, and extended losses to more than 7.5% over two sessions.

As regulations eased, domestic liquidity deepened, and Indian markets integrated with global peers, the premium enjoyed by ADRs over Indian stocks has shrunk over the years, and often turned into a discount. The trend signals that the excitement for these instruments has faded, as direct access to Indian stocks became a breeze. Still, as the HDFC Bank episode shows, ADRs remain a flashing alarm bell for FPI sentiment.

Fading relevance

In the early 2000s, Indian markets were marked by sharp information asymmetry, and remained relatively isolated from their global peers. For foreign investors at the time, these US dollar-denominated certificates traded in American exchanges opened a critical but often congested lane connecting to Dalal Street.

Switch to present—the landscape has transformed. Multiple new routes have opened up for stock buyers, broadening foreign access, deepening liquidity, and wiring domestic markets far more tightly into global capital flows. Consequently, Mumbai now dictates price discovery, sidelining New York, with the allure of ADRs fading along the way.

Sample this: ADRs of Infosys, the first Indian company to issue them, traded at a 32% premium between 2001 and 2008. It has since slipped into a discount, while ICICI Bank ADRs, which used to have a 9% premium, has converged to parity with its domestic shares. The trend mirrors across other large-cap ADRs, suggesting that the need for offshore access to these stocks has faded.

Easing frictions

Experts say high ADR premiums typically reflect restricted domestic access or limited liquidity. With direct access to Indian markets cumbersome in the early 2000s, ADRs carried a scarcity premium, along with a convenience fee for trading in US dollars on US exchanges.

“For decades, fragmented KYC norms and rigid capital controls made US depositary receipts necessary as liquidity bridges,” Anubhav Ghosh, partner of financial regulatory practice at Trilegal, said.

That has since changed. The Securities and Exchange Board of India’s (Sebi) liberalized FPI regime has streamlined onboarding into a single-window, riskbased process. Meanwhile, the non-debt Foreign Exchange Management Act (Fema) rules have expanded foreign investment limits and removed the need for prior approvals from the government or the Reserve Bank of India (RBI). Together, these changes have made direct onshore access faster, simpler and more scalable for global investors.

“Most clients are now trading the onshore market directly on FPI IDs as the process of setting up a Sebi-registered trading ID has become consistently smoother and faster over time,” Gautam Chhacharia, head of global markets at UBS India, said.

As Indian markets have scaled up and gained weight in global indices, direct stock ownership has become more efficient than accessing stocks through ADRs or swaps, he added. As a result, even as foreign interest in Indian equities strengthened, demand for ADRs waned and premiums steadily compressed.

Globally connected

India’s weight in the MSCI Emerging Markets Index has risen from below 5% in 2001 to a peak of 21% in September 2024, and currently stands at about 14%. This has triggered large passive inflows, as funds tracking the index must own underlying Indian shares directly, where liquidity is deeper and tracking error is lower.

As India has opened up and integrated into global indices, its markets have also become more synchronized with global risk cycles, narrowing the gap between ADR and onshore prices.

Mint’s analysis shows a clear uptrend in the median 30-day rolling correlation of the Nifty 50 and the S&P 500 over the last 25 years, signalling deeper linkages between the two markets.

Post-covid, correlations have risen to around 0.6 from 0.55 since 2001-2008, often spiking during global shocks such as the pandemic and the Russia– Ukraine war. A correlation coefficient of 1 suggests perfect correlation.

At the same time, the rise of algorithmic and high-frequency trading has ensured that any price gaps are quickly arbitrated away, binding ADRs and domestic shares into near-parity.

Disappearing incentives

As arbitrage opportunities faded and capital flows into India became seamless, the appeal of ADRs also diminished, setting off a vicious cycle of declining relevance.

“Relatively lower volumes of ADR trades are further diminishing arbitrage opportunities. Hence, ADRs aren’t relevant anymore,” said Yatin Singh, CEO of investment banking at Emkay Global.

From a price discovery standpoint, the shift is clear. With the surge in domestic institutional liquidity, especially mutual funds, fair value is now being set on Indian exchanges rather than offshore markets, Singh added.

Deeper onshore liquidity and faster arbitrage have eroded the old ADR-led trade, where traders used New York’s cues to anticipate Mumbai’s moves.

That said, Chhaocharia of UBS India notes ADRs can still offer forward-looking signals for specific stocks, particularly when global events unfold after Indian markets close.

Sentiment barometer

Recent volatility has proven that ADRs’ capacity for stock-specific signalling is very much alive. During the first month of the ongoing West Asia war, ICICI Bank ADRs traded at a 1.2% discount to its Indian shares, while HDFC Bank held a 5% premium—both below their six-year averages—pointing to heavy FPI outflows through March.

One of the clearest signals flashed during the recent global IT stock sell-off. When the launch of Anthropic’s Claude AI tools wiped out 20% of the Nifty IT index between 31 January and 27 February, Infosys and Wipro ADRs slipped to discounts of -1.5% and -2.2%, well below their post-covid averages.

“Typically, we have seen ADR premiums go up significantly whenever the market is in a longer-term uptrend,” Chhaocharia said. “That’s when tourist investors come in via ADRs and push premiums higher.”

As India’s bull run stalled over the last two years, those tourists also disappeared, alongside FPIs with direct exposure, adding pressure on the rupee. The rupee has depreciated nearly 11.7% against the dollar in the last two years.

In theory, a weaker rupee should widen ADR premiums since ADRs are dollar denominated. That premiums have instead compressed or turned negative, despite the tailwind from a weaker rupee, underscores how sharply FPI sentiment has soured since India’s post-covid bull run peaked in September 2024.

Gilded cage

While demand for ADRs has declined, supply has also slowed to a trickle. This reflects the growing maturity of Indian capital markets and their deeper integration with the global financial system, said Karan Marwah, partner and leader of CFO and IPO advisory services at Grant Thornton Bharat.

“Indian companies are able to attract ample liquidity from around the world without having to list overseas,” Marwah said, adding that US compliance costs and litigation risks are also key deterrents.

Trilegal’s Ghosh noted that the heavy financial and compliance burden of meeting the Sarbanes-Oxley Act, along with complex multi-jurisdictional filings, has turned US listings into a “gilded cage” — prestigious, but often prohibitively expensive.

Passed in 2002 to curb corporate fraud, the Sarbanes-Oxley Act imposes rigorous and expensive financial reporting and auditing standards on all US listed entities.

“At the same time, it can be difficult for Indian companies to stand out in the US if their businesses are largely India-centric,” Marwah added.

As a result, ADRs are now increasingly part of a broader shift, with more Indian companies shelving US listing plans in favour of a deepening domestic capital market. Data from EY shows no Indian company has listed in the US since 2023. While Tata Motors delisted its ADRs in 2023, companies such as Rediff.com and Sterlite Industries (India) too delisted earlier.

Ghosh said that once Sebi allows direct listings of listed companies on GIFT City exchanges, it could deal a final blow to ADRs by offering similar benefits without the associated premiums.