Kick-Starting the IPO Market : Some Suggestions

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BACKGROUND

As the title of this paper suggests, I am going to attempt to offer some suggestions for kick starting the IPO market which is at present in a state of coma in Hindustan. But before that, let me clarify that though technically the term IPO refers to the first ever public issue of a company, it is popularly used in the capital market to denote Public Issues which include IPOs as well as FPOs. This paper uses the term in its larger popular version and should be interpreted accordingly.

PRESENT STATE OF THE IPO MARKET

As I wrote above, the IPO market is at present in a state of coma. I'm providing hereunder some data to support my statement.

1. IPOs Floated Over the Last 5 Years

The table 1 below provides information on IPOs floated during the 1st quarter of the current year as well as for the 5 preceding years. The information has been extracted from the website of PRIME 'www.primedatabase.com' on 5th July, 2012.

Table 1

IPOs Floated Over the Last 5 Years

	Year	No. of Issues	Amount (Rs. crore)	5 Year Average (No. of Issues)	Average Amount (Rs. crore), Per Issue
1	2007-08	90	52,219.00	.....	580.21
2	2008-09	21	2,034.00	.....	96.86
3	2009-10	44	46,941.00	.....	1,066.84
4	2010-11	57	46,182.00	.....	810.21
5	2011-12	36	24,930.00	.....	692.50
	Total.........	**248**	**1,72,306.00**	**49.60, say, 50**	**694.78**
6	2012-13 **(As on 30/06/12)**	5	608.00	.....	121.60

As the readers will notice, the data is quite revealing and self explanatory..

2. IPOs Floated During 2011-12

In the above background, the peculiarities of the 2011-12 down fall are vividly brought out in the prime database's press release dated 29-03-2012 on annual review of IPO market. It is pertinent here to quote the following extracts:

- The raisings in 2011-12, according to Haldea, would have, in fact been much lower but for the two Offers for Sale (ONGC and Wipro) done through **stock exchange auction system**, which only technically be public issues. These 2 offers accounted for Rs. 13,517 crore of the total Rs. 23,969 crore (*24,930 crore finally*).
- According to Haldea, **PSUs** and PSU banks dominated the year with a total fund raising of Rs. 17,453 crore or 73 per cent of the total amount. This was, however, lower than Rs.27,537 crore raised by them in 2010-11. Of the total amount Rs.14,019 crore was through **divestments** (*significantly lesser than the divestment target of Rs.40, 000 crore*) and Rs. 3,434 crore through fresh capital. Only 3 PSUs entered the market, the IPO of NBCC (Rs.108 crore), FPO of PFC (Rs.4, 578 crore) and OFS of **ONGC (Rs.12, 767 crore**).
- The response from the public to the equity issues of the year was on the whole **very moderate**, according to Haldea. 7 issues were oversubscribed by more than 3 times. The highest oversubscription was received by MCX at 45 times, followed by Muthoot Finance at 21 times. At the other extreme were 3 IPOs that failed to elicit response from the public and had to be **withdrawn** (*Galaxy Surfactants, Goodwill Hospital* and *Swajas Air Charters*). What emerged clearly was the **selective interest**, and not frenzy, of the retail investors.

What then lies ahead in the future?

3. IPOs in the Pipe Line

Numbers of red herring prospectuses filed with ROC and draft offer documents filed with SEBI point towards the activity expected in the primary market in the near future. The following data from 'www.sebi.gov.in' on 5th July, 2012 for the 1st quarter+ period of the current year again portrays a dismal picture.

3.1. Red Herring Prospectuses Filed with ROC

Details are as under:

Table 2

Red Herring Prospectuses Filed with ROC

	Date of Filing	Company	Amount (Rs. crore)
1	Jun 25, 2012	VKS Projects Limited	55.00
2	May 14, 2012	Speciality Restaurants Limited	73.08
3	May 04, 2012	**Plastene India Limited**	**74.97****
4	Apr 26, 2012	**Samvardhana Motherson Finance Limited**	**1,665.00**
5	Apr 17, 2012	Tribhovandas Bhimji Zaveri Limited	200.00
		Total.......	**2,068.05**

- **At floor price.
- Amount (Rs. crore) has been culled out from 'www.nseindia.com'.

The website of NSE 'www.nseindia.com', accessed the same time on 5th July, 2012 reveals that IPOs of **Plastene India Limited** and **Samvardhana Motherson Finance Limited** have been withdrawn during May 2012. And for obvious reason, i.e., poor public response. Interestingly they had a respectable grading of **3/5** and **4/5** respectively. Thus out of total Rs. 2,068.05 crore, IPOs worth Rs. 1,739.97 crore (a staggering **84.14 %.)** could not sail through, that too, despite respectable IPO gradings. Rests of the three have already closed and number 2 and 5 listed as well.

3.2 Draft Offer Documents Filed with SEBI

Details are as under:

Table 3

Draft Offer Documents Filed with SEBI

	Date of Filing	Company	Amount (Rs. crore)
1	May 18, 2012	Rashtriya Ispat Nigam Limited	2,500.00
2	May 08, 2012	Goodwill Hospital and Research Centre Limited	98.00
3	May 07, 2012	Fast Train Cargo Limited	55.00
4	Apr 13, 2012	Ace Tours Worldwide Limited	35.00
5	Apr 03, 2012	Tristar Retail Limited	25.00
6	Apr 02, 2012	C.Mahendra Infojewels Limited	135.00
		Total.......	**2,848.00**

- Amount (Rs. crore) of IPO no. 3 to 6 as per PRIME.

Even assuming optimistically that all these issues will materialize, still a fund raising of a meager Rs. 2,848 crore only is expected in the near future in the current year.

REASONS FOR DEBACKLE AND GLOOMY OUTLOOK

What are the reasons causing this debacle and further gloomy outlook? Let me make an attempt which by no means should be construed as comprehensive. Of course, the main burning issues are covered.

1. Greedy Over Pricing

Free pricing is the topic of most hated as well as most loved, yet never concluding, debate. Investment bankers are accused of advising their clients, and in connivance with them, fixing unjustifiably high prices for fetching more assignments due to tough competition among themselves which causes, huge losses, to the investors.

1.1 Losses in Recent IPOs

The pages 1 & 2 of the table **'IPO Performance Tracker'** from the site 'www.chittorgarh.com' provide details of profit earned/loss suffered by investors in IPOs listed since April 1, 2011 up to July 10, 2012. A summary :

Table 4

Profit/Loss in IPOs Listed Since April 1, 2011 up to July 10, 2012

A.	All IPOs:		Issue price (Rs.)	Traded price (Rs.)
1	No. of IPOs listed	39		
2	No. of IPOs providing gains	12		
3	No. of IPOs inflicting losses	27		
4	**No. of IPOs inflicting losses(%): 3/1**	**69.23%**		
5	**Highest loss (Taksheel Solutions Ltd)**	**(91.89%)**	**150**	**12.16**
6	Highest gain (Onelife Capital Advisors Ltd)	270.09%	110	407.10
7	Lowest loss (Innoventive Industries Ltd)	(0.30%)	117	116.65
8	**Lowest gain (BCB Finance Ltd)**	**0.20%**	**25**	**25.05**
9	**No. of IPOs inflicting losses in different loss brackets:**			
	• =<10%	6		
	• >10%=<40%	8		
	• >40%=<80%	5		
	• **>80%=91.89%**	**8**		
B.	**PSU IPOs:**			
1	No. of IPOs listed	2		
2	No. of IPOs inflicting losses:	2		
	• **NBCC**	**(4.95%)**	**106**	**100.75**
	• **PFC**	**(7.04%)**	**203**	**188.70**
3	**No. of IPOs inflicting losses(%): 2/1**	**100%**		

The site has not covered ONGC OFS, eventually, which also has inflicted losses as we will see later. **Clearly the public sector is no different than the private sector.**

1.2 IPO Losses Over Long Term

BSE IPO index, launched in the month of August 2009, is a measure of profit/loss on IPOs in both short as well as long term. The movements in the index since its launch vis-à-vis BSE Sensex are as under:

Table 5

IPO Losses Over Long Term

As at close of....	BSE IPO Index		BSE Sensex	
	Index	Rise/(Fall)	Index	Rise/(Fall)
August 2009	2009	...	15,667	...
March 2010	2014	0.25%	17,528	11.88%
March 2011	1748	**(13.21%)**	19,445	10.94%
March 2012	1538	**(12.01%)**	17,404	**(10.50%)**
June 2012	1400	**(8.97%)**...3 months	17430	0.15% ...3 months
Data source: www.bseindia.com.				

BSE IPO is thus regularly reporting losses ever since its launch 35 months ago.

Why perennial losses to the IPO investors?

2. PSU Disinvestment

As noted earlier, PSUs have not only failed to achieve the disinvestment target of Rs. 40,000 crore set for the year 2011-12, their performance (Rs. 17,453 crore) per se against 2010-11(Rs. 27,537 crore), leading to under procurement of Rs. 10,084 crore, has also been dismal. Their absence from the primary market in fact is responsible for close to 50% of the gap (Rs. 21,252 crores) in 2011-12 IPO proceeds (Rs. 24,930 crores) compared to 2010-11 (Rs. 46,182 crores). In terms of numbers only 3 PSUs, National Buildings Construction Corporation Ltd. or **NBCC, PFC** and **ONGC**, approached the IPO market during 2011-12. PFC and ONGC were listed during the year itself whereas NBCC recently in 2012-13. Tragically, all the three PSUs, known to be the leaders in their respective businesses, have inflicted losses on the investors. **NBCC**: **4.95%** in just 3 months since its listing on 12 April, 2012, **PFC: 7.04%** even after investor holding the share for 13 months since 27may, 2011(**Source:** http://www.chittorgarh.com. **Accessed** on: **10** July, 2012) and **ONGC: 7.86%** in just 4 months (1 march, 2012 to 10 July 2012). The offer for sale opened on 1 march, 2012 at a floor price of Rs. 290, which was at a premium to the then trading price, allotment took place at an average Rs. 303.67 per share (**Source:** The Economic Times, 4 March 2012) and the share declined to Rs. 279.80 on the BSE on 10th July. Again, only one PSU, i.e., **Rashtriya Ispat Nigam Limited** has filed its offer document with SEBI till 10th July 2012. The OD was filed on 18 May, 2012 (**Source**: www.sebi.gov.in).

Clearly the government of India, responsible to promote the IPO market through its regulatory wing SEBI, herself is not confident of raising resources from the market. But, why?

3. IPO Grading

As noted earlier, the IPOs of **Plastene India** and **Samvardhana Motherson Finance** had to be withdrawn during May 2012 despite having respectable gradings of **3/5** and **4/5** respectively. Again during 2011-12, 3 IPOs: **Galaxy Surfactants (4/5), Goodwill Hospital (3/5)** and **Swajas Air Charters (2/5)** were withdrawn, the first two with respectable gradings. Again, out of the 27 recent issues that inflicted losses, as noted earlier, 10 IPOs had respectable gradings: **L&T Finance 5/5, Muthoot Finance** and **NBCC 4/5** both**, Tribhovandas Bhimji Zaveri, Indo Thai Securities, PG Electroplast, SRS, Sanghvi Forgings, Innoventive Industries** and **Future Ventures 3/5** each. Interestingly, Multy Commodity Exchange of India Ltd. **(MCX),** despite the highest grading of **5/5**, could **gain only a meager 12.12%** for the investors over 4 months.

(**Source of grading and MCX gain**: http://www.chittorgarh.com)

Has the IPO grading become redundant, irrelevant?

4. Very Moderate Public Response

As a result of the aforesaid problems and as noted earlier the public response to IPOs of 2011-12 has not been enthusiastic at all. Retail investors are not really interested much. Only 7 issues, out of 36, were oversubscribed by more than 3 times. Within that only 2 IPOs were received overwhelmingly, **MCX** at 45 times, followed by **Muthoot Finance Ltd**. at 21 times. At the other extreme there were 3 IPOs, Galaxy Surfactants, Goodwill Hospital and Swajas Air Charters, that failed to elicit response from the public and had to be withdrawn. *Clearly, IPO investors have learnt some of their lessons, if not all.* They have become choosy and selective. Frenzy of the yester years seems to have taken a backseat at least for the present if not for ever.However one wonders whether the investors' judgement goes wrong or the IPOs tend to be not as strong as they seem to be, or are made out to be, even in the cases of heavily oversubscribed issues like MCX and Muthoot Finance. **MCX** has returned a **gain of just 12.12%** over 4 months of its listing. ***Muthoot Finance** has caused a **loss of 20.97%** to the investor even after him holding the share for 14 months of its listing. The share issued for Rs. 175 is currently trading at Rs. 138.30.*

Obviously the investors have not learnt all their lessons.

SUGGESTIONS FOR KICK STARTING THE IPO MARKET

What to do to set the things right? Here are a few suggestions which by no means are exhaustive. All of them warrant a will at the end of SEBI to reframe its existing policy framework.

1. Free Pricing With Checks & Balances

Free pricing, which eventually which turned into overpricing, has been severely criticized by the investors ever since its beginning in 1992 and is the root cause of all the ills in the IPO market. It has caught the attention of all the SEBI chairmen, past as well as present, while being in the office. It is another story that all the SEBI chairmen themselves have done just lip service to the investors on this issue instead of trying to come out with concrete measures to fight the menace of overpricing. Free pricing having failed in Hindustan conclusively, it is high time that SEBI put some checks & balances in place. **The CCI valuation norms could be modified as per the present day circumstances.**

2. Self Control on the Vyaapaari Vritti of the Government

On one hand the government curses the investment bankers and businessmen for IPO investors' losses. On the other, when the side turns it becomes itself the businessman. Data presented above clearly brings out the greed of the government functionaries. The **'Jan Pratinidhis'** sell the shares to the **'Jan'** at abysmally high prices, inflict losses on them and thus drive them out of the market for long till the bad memories last. And the irony is that the milky **Public (Jan) Sector Undertakings,** whose shares are sold to the **public (Jan),** are said to be owned by the

public (Jan) only. **The Vyaapaari Vritti ('revenue alone' motive) of the rulers needs to be contained.** The problem is that they are not under the control of the **'Jan'.** Who will bell the cat than?

Their malpractices also become the talk of the town more often than not. Reportedly forcing the state run **LIC** to bail out the latest **ONGC** OFS on 1st March, 2012, in which LIC had to pick up 95% of the offer and the resultant huge losses to it, which mean ultimately to **'Jan',** is a recent instance of such malpractices of the state. The Economic Times reported on 4 March 2012, **'Value of LIC investment in ONGC slips by Rs 900 crore in 2 days'. (Source:** http://articles.economictimes.indiatimes.com/2012-03-04/news/31121408_1_ongc-shares-share-auction-floor-price**).** ONGC had announced to the NSE on 28-02-2012 to open its OFS on 01-03-2012. Its floor price at Rs. 290 was decided at **3.31% premium** to the prevailing listed price of Rs. 280.70 (BSE) as at the close of 27-02-2012. The government had come under heavy attack for not deciding the price below the listed price, and rightly so.

Why can not the government return the **wealth of the public to the public** to whom it belongs? Why can not the shares of the PSUs be sold to the **individuals alone** at through away prices? **If that is done, the faith and confidence of the investing public will get back to the primary market, the government will always be able to meet its targets and the market itself will get deeper penetration leading to its long term revival.**

3. IPO grading
In its present form it is only a half cooked cuisine since it takes into account the fundamentals alone devoid of pricing consideration. Why it cannot factor the issue pricing in deciding the grades? CRISIL itself cautions that a **5/5 graded IPO may be a bad investment if pricing is not justified. Data provided above testifies this caution.** Why not the investors be provided with a complete comprehensive guidance then to serve its real purpose? Abolition of CCI pricing, its non-disclosure in the offer document and adoption of unchecked free pricing further strengthen this argument. The move will also lead to more transparency in the market. **Comprehensive grading alone will serve the objective of investor protection and will eventually lead to more investor friendly pricing.**

4. Institutional Placement Programme (IPP) and Stock Exchange Auction System (SEAS)
These two innovations were introduced by SEBI; on 30 January 2012 and 1 February 2012 respectively, to enable the listed companies achieve minimum public shareholding to comply with the listing requirements. In the **IPP** the issuance is allowed to be listed even if allotment is made to just **10 investors**. In the **SEAS**, even this condition is not stipulated. All it requires is that minimum of 25% of the shares offered should be reserved for mutual funds and insurance companies and that no single bidder other than mutual funds and insurance companies shall be allocated more than 25% of the size of offer for sale. It implies that-

- Even if there are just **4 individual allottees**, the OFS will sail through.
- In case there is no individual bidder, and further assuming that just **one mutual fund** or **one insurance company** has bid in the OFS, it will still sail through.

This is exactly what happened in the recent OFS of ONGC as discussed earlier. LIC was reportedly forced to pick up 95% of the offer. It appears that SEAS was tailor made to suit the interest of the **'Jan Pratinidhis'** as ONGC issue had been deferred time and again before that. The recent ONGC offer was floated exactly within **one month** of issue of SEAS norms. It is thus more than clear that for all practical purposes **IPP** and **SEAS** are just technically public issues, but not in spirit. The government needs to involve the public at large instead of doing an eye wash.

In spirit, these two schemes should have been meant for the private sector companies, not for the government.

TO CONCLUDE………..Policy Issues
This paper has discussed the present state of the IPO market, its future outlook and, main reasons responsible for the gloom. Some suggestions have been made for its long term revival which revolve around Overpricing, Vyaapaari Vritti of the government, IPO grading and IPP & SEAS programmes. What emerges clearly is the need on the part of SEBI to introspect and carry out with determination an unbiased review of its IPO market policies to promote the market and ensure sustained interest, faith and confidence of the investors, the very objective behind its establishment as capital market regulator. Finally, 'Jan Pratinidhis' need to exercise self control on their Vyaapaari Vritti. They need to practice what they, and their regulatory agency, preach.

Views expressed are personal. Comments invited at ambrish@fsm.ac.in.