

Safety Net : An Overview



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Safe indicates 'free from risk or danger'. The word 'safe' as appearing in the Oxford Dictionary associates it with the characteristics of a risk free situation and sort of a protection or maintaining a margin of security. It can be an adjective. Eg. Safety bill, safety catch, safety lamp, safety curtain, safety match, safety pin etc. The word "safety net" also finds a place which means to catch an acrobat in case of a fall from a height. Thus safety net in the capital market means to provide an investor a comfort from a fall in value of his initial investment.

Safety net is different from market making. The necessity for providing safety net has arisen due to the present market conditions and also due to the fact that the performance of the high premium issues in which the retail investor participated are today one third its issue price, a great erosion in value. There has also been a great fear and loss of confidence of the retail investors in the primary market. **Though it is accepted that equity market always contains an element of risk, it does not give authority to a corporate or to its Investment Bankers to price an IPO offering at an exorbitantly high price.**

A select list of IPOs which hit the market through 2010, 2011 & 2012 is given below which will indicate the loss of capital by investors.

2010

Sl.No	Company Name	Listed On	Issue Price	Current Price	Profit / Loss
1	Tarapur Transformers Limited	18-May-10	75	6.35	-91.53%
2	Parabolic Drugs Limited	1-Jul-10	75	5	-93.33%
3	Aster Silicates Ltd	28-Jul-10	118	12.15	-89.70%
4	SKS Microfinance Ltd	16-Aug-10	985	108.2	-89.02%
5	Indosolar Ltd.	29-Sep-10	29	2.15	-92.59%
6	Microsec Financial Services Ltd	5-Oct-10	118	27.5	-76.69%
7	Electrosteel Integrated Ltd (Electrosteel Steels Ltd)	8-Oct-10	11	3.99	-63.73%
8	Ramky Infrastructure Ltd	8-Oct-10	450	50.5	-88.78%
9	Bedmutha Industries Ltd	14-Oct-10	102	10	-90.20%
10	A2Z Maintenance & Engineering Services Ltd.	23-Dec-10	400	13.6	-96.60%

2011

Sl.No	Company Name	Listed On	Issue Price	Current Price	Profit / Loss
1	Acropetal Technologies Ltd	10-Mar-11	90	5.14	-94.29%
2	Sudar Garments Ltd	11-Mar-11	77	11.55	-85.00%
3	Fineotex Chemical Ltd	11-Mar-11	70	22.85	-67.36%
4	Shilpi Cable Technologies Ltd	8-Apr-11	69	13.8	-80.00%
5	Paramount Printpackaging Ltd	9-May-11	35	1.2	-96.57%
6	Timbor Home Limited	22-Jun-11	63	14.95	-76.27%
7	Bharatiya Global Infomedia Ltd	28-Jul-11	82	6.18	-92.46%
8	Inventure Growth & Securities Ltd	4-Aug-11	117	5.4	-95.38%
9	Vaswani Industries Ltd	20-Sep-11	49	2.9	-94.08%
10	Tijaria Polypipes Ltd	14-Oct-11	60	5.75	-90.42%

2012

Sl.No	Company Name	Listed On	Issue Price	Current Price	Profit / Loss
1	VKS Projects Ltd (Re.1/- face value)	18-Jul-12	55	2.45	-95.55%
2	Tara Jewels Limited	6-Dec-12	230	137.6	-40.17%
3	PC Jeweller Ltd	27-Dec-12	135	100.95	-25.22%
4	Bharti Infratel Limited	28-Dec-12	220	149.95	-31.84%

It can be thus noticed from the table of select IPOs that the investors have lost heavily on the investment made necessitating a thought process for providing safety net in IPOs.

The first 6 months of 2013 there has not been much activity in the primary market. The SME Exchange at the BSE had some amount of action and more than a dozen companies had obtained the listing status at the SME platform. The equities listed at the SME platform had also offered reasonable returns to investors. The pricing was reasonable probably because the issue had to be compulsorily underwritten and the market making was made compulsory. The retail investors did not have an opportunity to enter into scrips in SME due to restrictions on minimum level of investment. A minimum of Rs.1,00,000/- has been prescribed for any investor to participate in an SME issue. This is in contrast to the application by retail investor which can be of a size up to Rs.10,000/- to Rs.15,000/- in respect of main board issues.

Thrust by Securities & Exchange Board of India (**SEBI**) has always been to ensure that the retail investors get a reasonable amount of protection in the form of proper disclosures especially on the risk factors and correctness of financials of the Issuer Company. The complaints from the retail investors have forced the regulator to focus its direction on the pricing of issues especially after the analysis of issues which had hit the market. Investors and capital market participants at large agree with the regulators concern that had the pricing being done properly, great erosion in capital values would not have arisen. It is generally felt that the Investment Bankers are as much responsible as the corporate while pricing and marketing an IPO flotation. The debate has always been that the safety net should be compulsory or not. While one school of thought believes that while making an investment in equity an investor is definitely aware and has also read the 'General Risk' appearing in the front page of the Red Herring Prospectus / Prospectus. The prospectus contains the following paragraph :

"Investment in equity and equity related securities involve a degree of risk and investors should not invest any funds in this Issue unless they can afford to take the risk of losing their investment."

The other school of thought is that apart from the disclosure era and free pricing, it is the responsibility of the regulator to ensure that free pricing does not result in unfair pricing. It is difficult for the regulator to put any restrictions on price on the Issuer Company as the ICDR does not provide for the same. In certain cases it is apparently seen that the pricing is exorbitant but as long as an issue is successful the pricing is not criticized.

In contrast however fair the price is, if the issue fails, the criticism continues. May be a high price issue getting several times oversubscribed still results in criticism to the Investment Banker by the Issuer company of having underpriced the stock. Pricing is relative, subjective and directly related to situation in the capital market.

The factors which go in favour of introducing a safety net is always construed as being partial to retail investors and harsh on the corporate. There is always a strong resistance from the Issuer Company and sometimes from the Investment Bankers for providing safety net. It is always argued that the safety net will result in draining the resources of the corporate and make it difficult for them to achieve their business plan.

Though much can be said for and against the implementation of safety net, it is important that if the Indian capital market requires the retail investors support the safety net definitely needs to be looked at positively. Methods, ways and means have to be devised by the Investment Bankers and the Corporates to make this safety net workable, operational and investor friendly.
