The Indian QIP and Block Deals Market- Prospects & Challenges

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Covid -19 pandemic has united the world in an unusual manner. Never before has the entire world been faced with a challenge so severe that has not only threatened human survival in a medical sense but has also had a far reaching impact on the world economies. We are witnessing dislocation across the globe at a scale never seen before. Nobody seems to be immune - all sectors, all industries, all geographies are impacted.

The US-China tension had already caused a lot of volatility in the global markets last year and coupled with the NBFC crisis had turned out to be a double whammy for the Indian equity markets. Some green shoots had begun appearing early this year with a few IPOs lined up for the first quarter of the calendar year, however under the looming shadow of Covid-19, only one IPO managed to get through.

What started off as a medical exigency in January-February 2020, unleashed its impact on the equity market in March 2020 when investors began grasping the severity of the pandemic. The confidence crisis along with the sharp correction in crude prices led to the markets in India correcting by ~25-35% from their peaks. The nationwide lockdown added to the woes of a struggling economy and, arguably, brought the economy to a standstill. The equity capital markets were not unaffected. There were no meaningful ECM transactions in March and April 2020.

However, the central banks across the world were extremely proactive in providing stimulus in the form of various, unprecedented, liquidity measures. The US Federal Reserve took a broad range of measures including infusing upto USD 2.3 trillion into the economy, resuming purchase of long term securities, lowering rates for lending. Reserve Bank of India also rolled out a slew of measures such as targeted long term repo operations of ~Rs. 1 lakh crore (~USD 13 billion), cutting the reverse repo rate to 3.75%, increase in ways and means advances limits of states by 30%, open market operations (purchasing long dated G-Secs and simultaneously selling short dated treasury bills). Japanese cabinet approved a record stimulus of 234 trillion yen (USD 2.18 trillion) or about 40% of its GDP. Bank of Japan proposed to issue an additional 31.9 trillion yen in government bonds and to endeavor to keep the interest rates low with aggressive bond buying. European countries also rolled out economic stimuli ranging from USD 200 billion to USD 500 billion each and the European Commission is hopeful of unveiling a recovery fund worth 750 billion Euros (USD 860 billion) meant to help rebuild the southern economies which have been the worst affected by the crises.

Aided by the unprecedented levels of liquidity, secondary market activity picked up soon enough and FIIs and DIIs were trading based on global cues with the DIIs supported by the resilient SIP inflow. After the severe net outflows from the equity markets in the months of March and April (~Rs, 70,000 cr / USD 9 billion outflow), FII/ FPIs have returned with modest net inflows in the months of May (~Rs. 14,500 cr/ USD 2 billion) and June 2020 (~Rs. 22, 000 cr/ USD 3 billion).

Securities market regulators have not been far behind and have been extremely prompt in rolling out measures/ relaxations to buttress some of the pain being felt by the corporates. Some of the notable measures taken by Securities Exchange Board of India include extending timelines for regulatory compliances, temporary relaxations in eligibility criteria to be eligible for fast track rights issues and FPOs, allowing shorter time frame for preferential pricing (albeit with additional lock-in requirement) and reducing the time gap between 2 QIPs to 2 weeks (from 6 months earlier).

Emboldened by these measures and with an eye to shore up balance sheets, many corporates approached capital markets in no small measure. Starting with the mammoth rights issue by Reliance Industries (~Rs. 53,000 cr/ USD 7 billion), the deal flow has picked up in an unexpected though highly welcome move. There has been a flurry of rights issues, with ABFRL (Rs. 1,000 cr/ USD 133 million), STFC (Rs. 1,500 crores/ USD 200 million), PVR (Rs. 300 crores/ USD 40 million) and MMFSL (Rs. 3,500 crores/ USD 467 million), to name a few, due to open in July – August 2020. Secondary offerings in the form of Qualified Institutional Placements (QIPs) and Blocks have not been far behind.

Some of the notable transactions include - Kotak Mahindra Bank QIP (~Rs. 7,500 cr/ USD 1 billion) and JM Financial QIP (Rs. 770 cr/ USD 100 mn), Hindustan Unilever – Glaxo Smith Kline Block deal (~Rs. 25,000 cr/ USD 3.35 billion), Bharti Airtel block deal (~Rs7,500 cr/ USD 1 billion), ICICI Lombard block deal (Rs. 2,250 cr/ USD 300 million), ICICI Prudential block deal (Rs. 840 cr/ USD 110 million). As is evident from this list, blue chip paper remains in high demand even in these troubled times as all the investors who had taken out money in the earlier months are now looking to invest again. Pedigree names with strong operating performance and stable liquidity position are likely to get preferred. The line-up of potential issuers is evidence of this – HDFC Ltd. (~Rs. 15,000 cr/ USD 2 billion), ICICI Bank (~Rs. 15,000 cr/ USD 2 billion), Axis Bank (~Rs. 14,000 cr/ USD 1.9 billion). Every investment opportunity is being put through a 'stress test' to evaluate resilience to any further negative impact. Debt servicing ability is a key metric to evaluate investment opportunities.

Further companies with a compelling story, operating in a niche, especially the ones that have benefited from the current pandemic (such as those in the pharmaceutical, personal care, specialist chemicals) are also likely to get interest e.g. Rossari Biotech. Rossari IPO (~Rs. 500 cr/ USD 67 million), the first one to launch after a four month Covid-19 induced hiatus, received ~80 times oversubscription. Yes Bank, with its FPO of ~Rs. 15,000 cr (USD 2 billion) may appear to be an outlier to the current theme but this was a much needed and long overdue fund infusion driven by SBI.

It cannot be disputed that building an anticipatory buffer capital is not only prudent, but an unavoidable need of the moment for India Inc. BFSI sector, as expected, has been and will continue to lead the way in this. While some of the larger players have raised/ in near future likely to raise a combination of risk, confidence and growth capital, many others are likely to follow in the next 12-18 months. The only financiers who may defer it by 3-4 quarters would include the ones that have recently tapped equity in last six months or are unwilling to dilute at extremely beaten-down valuations. A similar pattern is likely to play out in the non-BFSI space, with the issuers trying to balance the trade-off between the timing of the fund raise and the potential discount to the already impaired valuations.

Given the measures of liquidity, regulatory relaxations and the undeniable need for funds, we anticipate QIPs to continue, opportunistically at first, and then as the preferred mode of raising confidence capital by India Inc. Given the shorter to market timelines for this mode of fund raising and the possibility to tailor the product to suit the issuer's requirements (NCD + warrants for deferred dilution), QIP will remain an attractive means to raise funds.

Further with the markets regaining some of the lost ground and with the rally in the stock prices of some of the blue chip companies, blocks/ bulk deals will be undertaken prudently by the shareholders either to monetize holdings in the crown jewels or to divest non-core investments and as short term liquidity instruments.