Road Ahead in Indian IPO Market

Indian IPOs-Well poised in emerging markets

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Public Offerings is a strategic tool to enhance brand / organizational visibility or to create currency for acquisitions and not just about raising capital funds. It is years of strategic planning and hard work that culminates a desired successful listing of private enterprises on exchanges. A successful IPO plan improves perception about businesses and brands in the minds of customers, suppliers and employees. IPO's also have another dimension – they are transformation from private to public with added responsibility and accountability towards new co-owners.

In 2007, global IPO activity reached an all-time high with fund raised close to US$287 billion. BRIC countries accounted for approximately 40% of such proceeds. In the first quarter of 2008, 236 global IPOs raised US$40.9 billion. The top 3 IPOs were US$19.6 billion offering of Visa Inc., the US$5.5 billion IPO of China Railway Construction Corp. Ltd., and the US$2.9 billion listing of Reliance Power in India. Notably, eight out of the top 10 IPOs represented companies from the emerging markets. Most of the emerging markets continue to prosper and produce quality IPOs, bolstered by their robust economic growth.

Capital markets have played a significant role in our country's capital formation plan. This is evident from the fact that in fiscal 2008 about 92 issues from Indian Companies raised 13.6 USD billion from the primary markets depicting an average of 578.48 crores. The first three quarters of FY08 saw primary markets achieve new heights. The sensex surged from 12,455 in the beginning of FY 08 to 20,286.99 when the third quarter was over. The outlook of Indian Capital Markets have undergone a significant change over the years with respect to qualities of issuances made, corporate governance, increase in access to investible funds both domestically and international, global reach of Indian corporate among others. Significant issuances, across sectors, were made in this year including follow on issue of ICICI Bank which raised $2.5 billion which was oversubscribed 10.39 times; Reliance Power, the largest ever IPO on the Indian Bourses saw itself getting oversubscribed 73 times and raised $190 billion showing investor's resilience in participating in country growth story.

The rapid growth in emerging market economies like our's has resulted into a shift of capital from developed economies as was shown by the fact mentioned by me earlier. The corporate sector's growth projections and requirements have led to increased fund requirements which has inturn resulted in significant capital raising trends locally as well as globally. But with sudden and deep turmoil in the global markets in last quarter of fiscal 2008, the activity in Indian IPO and secondary markets have also slowed down. India, still well poised among the emerging markets, remains the wellspring of the most vibrant growth stories.

In last five years Indian IPOs have grown exponentially in size and quality , shown by the fact that the average issue size of FY08 was equivalent to the total amount raised in FY03 (Rs.573 crores); thanks to increased movement of savings into equities, greater institutional depth, support from private equity and venture capital firms and stringent corporate and regulatory standards. With transition happening across all our financial products in line with global best practices whether it is settlement mechanism, automatic lending borrowing mechanism, depository mechanisms, investors protection measures, grading of IPO's, we still have some way left to reach upto the maturity point.

Both our capital markets regulator SEBI & RBI, have been empathetic towards regulatory measures and changes in the system to ensure greater transparency, accountability and easier norms of entry, thereby supporting corporates in smooth mobilization of funds. Emphasis has been to simultaneously make both procedures and systems investor and corporate friendly without forgetting and giving primary importance to investor's protection. Some of the significant changes like the allowing of fast track issues of sizeable companies with minimum disclosure requirements, easy and fast registration of FIIs, mandatory PAN requirement for investors, and exit options to investors through dual fungability have immensely benefited the markets.

Among significant changes that have bolstered the market responses to IPOs are the increase in FDI and FII investment limits in various sectors like radio and print media. This has enabled the new emerging sectors to secure seed funding in initial stages and provide size and quality at the time of IPOs. Such increased participation of foreign investors has not only allowed them to participate in respective corporate growth stories but also Indian economic growth. The total foreign direct investment inflows were 25.07 billion USD in FY 08 as compared to 16.48 billion USD in FY07. SEBI further took initiatives of easy and fast registration of non registered FIIs who used to earlier either avoid or participate through P-notes. About 322 FIIS got registered in last fiscal thereby getting direct access to Indian equity markets. The definition of entities eligible for registration has been further widened to include foreign individuals, corporates, charitable funds and institutions. Such a move will enable Indian corporates to tap wide large variety long term investors which will provide further stability to equity markets.

FII participation in IPO's has enabled the market to correctly discover the price of issuances, bring about the transparency in corporate disclosures and sequentially provided continuous support in the growth of corporates in value chain. Government has recognized and facilitated increased foreign participation by way of liberalization of FDI norms, easy FII registration and others. All measures are being indicative towards full capital convertibility regime thereby allowing Indian companies to have easy access to global funds. Several regulatory and procedural measures undertaken by our Apex bank has resulted in multi fold increase in liquidity and depth of the secondary markets. This has created platform for absorbing big ticket issues without impacting liquidity.

Regular reviews of all policies and framework affecting foreign inflows have been made to consistently evolve our systems in line with some of major developed economies. Systematic checks and balances by the regulators have enabled the market to develop and grow in an orderly manner like capping the issuance limit of offshore instruments by FIIs.

Our regulators have been the most active and stringent in these volatile markets to provide security and safety of capital to all classes of investors. The changes in our policies, systems and outlook of our regulators has been the most dynamic whether it is in relation to corporates, intermediaries or investing class in comparison to any other country in the world. Mandatory disclosure requirements for offerings have undergone significant changes to ensure that investment case with all due disclosures should be presented to enable investors to take an informed decision. IPO grading has been made mandatory for all public offerings thereby allowing small retail investors to to take the advantage of knowledge of Grading Institutions like CRISIL, ICRA in relatively assessing the fundamentals of the issuer company with relation to comparable peers. Permanent Account number has been made mandatory in all capital market transactions to avoid fraudulent and illegal transactions. This has also enabled to curb multiple application practices in IPOs thereby giving fair chance to small investors to participate in public offerings and better price discovery. Detailed disclosures pertaining to utilization of funds, promoters and litigations and other aspects such as 75% tie up requirement for objects, have come a long way in order to provide investor's education on the issuer and help investors take relevant investment decision. However, still there are few aspects like electronic public offerings, Indian depository receipts where further clarity and policy measures are required so as to enhance and further deepen our markets to investing class. Though overall, evolution of our markets has been in line with global practices, there are certain challenges which we still need to resolve like minimizing time gap between allotment and payment.

In the recent times we have seen huge oversubscriptions in public offerings, among the bigger issues like MPSEZ, Reliance Power demonstrating investor's confidence in upcoming corporate growth stories.

But this has also had another side; these levels of high oversubscriptions have put stress on the systems for refunds leading to delays and investors grievances. Primary sufferers of such delays are the small investing class. Despite our transition to electronic system of refunds like Electronic Credit System (ECS), Real Time Gross Settlement (RTGS), Direct Credit, retail investors are still not able get the refunds on time, which has impacted their confidence in the system. SEBI has already initiated several measures to overcome the process delay in refunds. Certain measures have been prescribed by Smile Committee, which are under discussion, like ASBA (Application Supported by Blocked Amounts) wherein charge will be on investor's bank account till the time of allotment and usage of money will be allowed only at the time of allotment. Efficiency of such system can only be determined only after adequate infrastructure has been built in and role of various intermediaries (brokers/sub-brokers) and their alignment in the new system has been properly addressed.

SEBI has also undertaken steps to reduce cost and time involved in fund raising activities for small and medium enterprises. Such steps includes thoughts on setting up of separate exchanges, trading platform etc.; thereby helping growing companies to raise fast capital required for immediate growth.

Trading platforms significantly affects the issuing company's decision for listing. As the trading platforms and available mechanics determines the quality and size of investors in the particular market and also helps in determining the mode and manner of secondary markets. Over the period our exchanges namely The Stock Exchange, Mumbai (BSE) and The National Stock Exchange (NSE) have transformed themselves to become a world class exchange. With adoption of international corporate governance standards, robust risk management systems and new trading technologies, our domestic stock exchanges continues to become liquid and transparent which has helped us in retaining the Indian corporate issuer to Indian markets and attracting almost all global funds to India. Significant interest has been shown by global exchanges and world renowned funds in acquiring stakes in our national exchanges and they now own approximately 20% stake in these exchanges. Such investments by global established exchanges will further help us in aligning to matured market platforms. The transformation of our stock exchanges is further evident from the average turnover on our national exchanges which is currently Rs.62,988.48 million on a daily basis which are comparable any developed exchanges. Such high liquidity markets assist in better price discovery for issuer companies. With settlement regime of T+2, introduction of Automatic Lending and Borrowing Mechanism, demutualization of local exchanges and adopting such other measures, the markets have become more transparent and sustainable thereby leading to greater investor's confidence.

Inspite of having moved up to the current levels of modernization in our Public Offering systems, still some way is left to reach upto maturity. Although all possible steps have been initiated by our regulators, gaining participation of common masses in Indian Equity markets through diversion of savings has been the primary task for all capital market intermediaries, also thereby allowing them to participate in prosperity of corporate and country in turn. This will only be possible when a full transparent, efficient market regime is available to investors to protect their financial interest and reduce their systemic risk. Also investors now have variety of geographies to invest in, which throws a challenge to instill confidence among investors and ensure sustainable and predictable investing environment in India.

In current scenario market turmoil triggered by the credit crunch has led to a sharp deceleration in many IPO markets around the world. Due to global uncertainty and extreme volatility, investor's confidence has taken a hit. Investor's outlook has undergone a change with key emphasis of predictability and sustainability of corporate earnings. Faced with more scrutinizing investors and stringent valuations, record numbers of businesses postponed their IPO plans. Even so, many more companies still wait in packed IPO pipelines, ready to go public when market conditions improve. High-quality enterprises, primarily from the emerging markets like ours, continue to be well received by the public markets. We believe that quality issuances with earning visibility and reasonable pricing will be the key to revive the investor confidence back into the primary markets.

Globally all regulators and central banks are taking all possible measures to address economic growth vis a vis inflation. These measures are likely to impact global liquidity movement in emerging economies versus developed economies. The liquidity flow coupled with corporate earnings outlook and emerging political scenario will hold the key to revive the primary market in near term.

(Vallabh Bhanshali is the Chairman of Enam Securities. The views are his personal views)