TUG OF WAR

Asian Paints, Jindal Group promoters vs minority investors: the fault lines in delisting

Promoters want to use a volatile stock market to take their companies private. But other shareholders are fighting tooth and nail to get their due

Anand Kalyanaraman, Anirudh Somani, 2 Sep 2022

Delisting proposals have shot up in the past couple of years. Promoters and minority shareholders have been clashing over the fair price, though

Elcid Investments—where the delisting failed—and Hexa Tradex—where it succeeded despite protests—highlight many contentious issues

Promoters say they follow Sebi's rules. Minority shareholders want these rules overhauled—to include more parameters for the right price

Minority shareholders allege collusion between promoters and friendly shareholders to push delistings at less than fair value

In May, the delisting proposal of Elcid Investments Ltd, a promoter entity of paints major Asian Paints Ltd, failed to win the confidence of its minority shareholders. But a month later, a similar proposal by OP Jindal Group company Hexa Tradex Ltd managed to sail through.

Though the outcomes of these two high-profile delisting proposals stand in stark contrast, they share a common thread—pitched battles between promoters and public (minority) shareholders over the fair price of shares.

Prima facie, both companies seem like minnows. The current market capitalisation of Hexa Tradex, which is into the trading of industrial materials, is less than Rs 1,000 crore ($126 million) with a share price of Rs 168 (~$2). The market capitalisation of Elcid Investments, an investment holding firm, is just Rs 5 lakh ($6,300) with a share price of Rs 2 ($0.03).

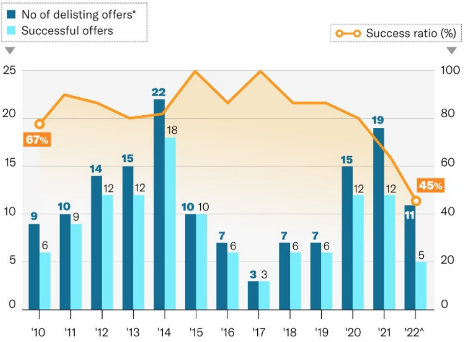
But size and numbers can be deceptive. Warring minority shareholders have claimed that the book value of each Hexa Tradex share is over Rs 400 ($5), while the intrinsic value of each Elcid share is, hold your breath, over Rs 6 lakh ($7,500). Elcid holds a 4.3% stake worth about Rs 14,000 crore ($1.76 billion) in Asian Paints. Minority shareholders hold about 37% stake in Hexa and 25% in Elcid.

These battles could have significant ramifications for future delistings—the removal of shares of a listed company from a stock exchange. Delisting can be voluntary—by the company's promoters or involuntary—on the directions of the market regulator Securities and Exchange Board of India (Sebi). In voluntary delisting, the promoters offer to buy shares from the minority shareholders at a price discovered through a bidding process.

The Covid-19 pandemic-hit two years have seen a record 41 voluntary delisting proposals since June 2020—nearly 30% of the 149 proposals seen since 2010, shows data from market information provider Prime Database. "Many promoters used the stock market volatility opportunistically to try and delist at a low price," says a market watcher. They and some of the minority shareholders *The Ken* spoke to for this story requested anonymity as they did not want to be seen commenting on the matter.

More offers, less okays

The number of delisting offers have shot up in the past couple of calendar years but the success ratio has fallen



*Does not include cases where shareholders did not allow the delisting proposal to proceed to the bidding stage itself, ^Upto Aug 2022

THE KEN Graphic by Adhithi Priya R, 1 Sep '22 Source: Prime Database

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But many proposals fell through.Out of the 16 recent delisting proposals analysed by law firm Cyril Amarchand Mangaldas, only six crossed all the hurdles.

For instance, despite a section of minority shareholders objecting to the delisting price, the promoters of Hexa Tradex managed to get enough shares to take their shareholding to at least 90%—the threshold for a successful delisting. On the other hand, the Vakil family, Elcid's promoters, failed to get past the first hurdle. While they got more than three-fourths of the total votes as required by the Companies Act, they didn't get two-thirds of minority shareholder votes as required by the Sebi regulations to start the delisting process.

In both cases, the root of contention was the share price.

"Even the biggest of promoters rarely let go of any opportunity to penny-pinch," says Dhiraj Mittal, an Elcid shareholder who led a crusade of sorts against the price offered in the delisting. The floor price, he contends, was far lower than the intrinsic value of Elcid's shares. But the floor price was nearly 9,500X the stock's then market price of Rs 17 ($0.2). So, were the promoters being stingy or generous?

In the case of Hexa Tradex, the floor price and the final discovered price are far lower than the book value, says a minority shareholder in the company.

Calls for rule change are getting louder. Minority shareholders in Elcid, like Mittal and investment firm 3A Capital Services' Rajan Shah, have been asking for the removal of circuit filters that they say prevent the stock's true price discovery. Mittal also demands that the intrinsic value of a share should be considered in the delisting process.

The Hexa Tradex minority shareholder says that "Sebi should mandate the stock's book value in the floor price calculation", in addition to the average market price. They think minority shareholders have been shortchanged, adding that their complaint to Sebi has not yielded results.

Hexa Tradex has rubbished the allegations. The delisting price is as per Sebi's rules, and enough minority shareholders have offered their shares for delisting at the discovered price, the company countered in a 14 July letter to Sebi, seen by *The Ken*.

However, the dissenting minority shareholders reject this argument, alleging collusion between the company and some minority shareholders to reach the 90% threshold. While Hexa Tradex has refuted the claim, some conspicuously odd foreign portfolio investor (FPI) names among the assenting minority shareholders raise eyebrows.

Elcid, too, saw oddball happenings just before the delisting proposal in March. And then some more when the proposal went to vote. Hexa Tradex and Elcid Investments did not respond to queries from *The Ken*.

It's not all black and white, though. Commercial instincts and interests guide promoters as much as they guide minority shareholders. It's good to be pragmatic in market matters, say experts.

The right price

The right price can be a matter of perception, which can vary widely.

Consider this. Just 276 minority shareholders hold about 25% of Elcid Investments, which derives its value primarily from its 4.3% stake in Asian Paints. "Based on this, each Elcid share was equal to 203 shares of Asian Paints, and the true intrinsic value of each Elcid share was about Rs 6.3 lakh (~$8,000)," says Mittal. As against this, the floor price offered by the promoters was Rs 1,61,023 ($2,000). But the floor price, at a nearly 75% discount to the intrinsic value, was at a huge premium to Elcid's market price of just Rs 17 or so ($0.2).

The trouble is, the market price is meaningless here—the stock hardly trades on the bourses, and understandably so. Who would sell a stock worth lakhs for a mere few rupees? The stock is subject to circuit filters and can't move beyond 5% on either side each day. So, the best price for even a willing seller would fall far short of the stock's real worth. Ergo, no deals.

Now, Elcid's promoters have been trying to delist the company for quite some time; the first attempt was made in 2013. That time too, the big gap between the floor price and the intrinsic value rendered the offer unsuccessful.

Similarly, in Hexa Tradex delisting, there was a huge gap in the perception of the right price. The floor price of ~Rs 153 (~$2) was far lower than its book value of about Rs 400 ($5) a share, say two of its minority shareholders, including one quoted above. So was the discovered price—the price at which the delisting will eventually be done—at Rs 172 (~$2).

"In delistings, minority shareholders should be entitled to the full worth of their shares," says the first Hexa Tradex minority investor. They add that only looking at the market price in such cases for floor price calculation is not correct and that the book value of the share should also be taken into account.

The trouble is Sebi's elaborate rules for delisting—which underwent a makeover in 2021—do not consider the shares' book value or intrinsic value in the delisting price calculation matrix.

The floor price is determined by a long formula from Sebi's takeover code. Among other things, it considers the weighted average traded price of the stock in the 60 days before the delisting offer. It also considers the latest negotiated or acquisition price paid for the shares. And if the shares are not frequently traded, an independent valuer must determine the floor price. That's how Rs 1.6 lakh ($2,000) came about as Elcid's floor price.

The indicative price—that promoters have the choice to initially offer—is generally marginally higher than the floor price. It was just ~Rs 3 ($0.03) higher in the case of Hexa Tradex.

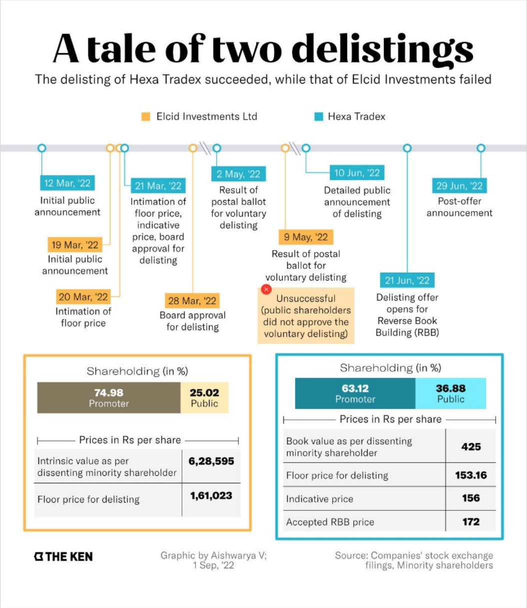
Then comes a key piece—the discovered price. This is found through the 'reverse book building' process in which public shareholders bid their price for submitting shares. The discovered price is the one at which the 90% threshold for promoter shareholding is met.

Promoters can accept or reject the discovered price. They can make a counteroffer if they think it is too high, but the price should not be less than the book value. Essentially, a deal or no deal depends on whether the promoters and most minority shareholders agree on the price.

"If promoters' counteroffers cannot be at less than the book value, why can't the book value also be considered in the initial floor price calculation, along with other parameters," asks the first Hexa Tradex minority shareholder. The second minority shareholder in the company thinks that the book value parameter should be considered, especially in thinly traded stocks like Hexa Tradex, where market price discovery may not be efficient.

Others make a case for intrinsic value to be factored in too. Mittal had got a fair valuation of Elcid done by an independent valuer that showed the share's intrinsic value at about Rs 6.3 lakh ($8,000)—far higher than the company-appointed independent valuer's estimate of Rs 1.6 lakh ($2,000). "In delistings, the intrinsic value that is fairly calculated should also be used," he argues.

Now, despite the huge gaps in the perception of the right price, the delisting of Hexa Tradex succeeded, while that of Elcid Investments failed. What gives?



A tale of two delistings

The delisting of Hexa Tradex succeeded, while that of Elcid Investments failed

Elcid Investments Ltd
Hexa Tradex
12 Mar, '22 Initial public announcement
19 Mar, '22 Initial public announcement
20 Mar, '22 Intimation of floor price
21 Mar, '22 Intimation of floor price, indicative price, board approval for delisting
28 Mar, '22 Board approval for delisting
2 May, '22 Result of postal ballot for voluntary delisting
9 May, '22 Result of postal ballot for voluntary delisting
Unsuccessful (public shareholders did not approve the voluntary delisting)
10 Jun, '22 Detailed public announcement of delisting
21 Jun, '22 Delisting offer opens for Reverse Book Building (RBB)
29 Jun, '22 Post-offer announcement

Shareholding (in %)

Promoter	Public
74.98	25.02

Prices in Rs per share

Intrinsic value as per dissenting minority shareholder	6,28,595
Floor price for delisting	1,61,023

Shareholding (in %)

Promoter	Public
63.12	36.88

Prices in Rs per share

Book value as per dissenting minority shareholder	425
Floor price for delisting	153.16
Indicative price	156
Accepted RBB price	172

THE KEN

Graphic by Aishwarya V; 1 Sep, '22

Source: Companies' stock exchange filings, Minority shareholders

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Hand-in-glove?

The difference, it would seem, between the success of the Hexa Tradex delisting and the failure of the Elcid Investments delisting, lay with a few key investors in these companies.

Some dissenting minority shareholders in Hexa Tradex have alleged collusion between the promoters and a few minority shareholders. This helped take the promoter stake to at least 90% and delist at a low price, they say.

"These shareholders were working in cahoots with the acquirers, and the delisting was a fixed match in which the retail investors have been shortchanged," says a complaint to Sebi and stock exchange officials by Vidit Choudhary, chief executive of Jai Vinimay Pvt. Ltd, a minority shareholder in Hexa Tradex. *The Ken* has seen a copy of the letter.

The letter refers to two FPIs, Albula Investment Fund and Cresta Fund, which appeared in *The Ken*'s April 2021 story on Adani Total Gas. They were part of a group of FPIs that invested across Adani stocks and stayed put for a long time. Their accounts were frozen by Sebi reportedly due to insufficient disclosure of information related to the beneficial ownership of the accounts.

There have been allegations that Albula, Cresta, and a few other FPIs are used for round-tripping funds. Together, these two held about 19% stake in Hexa Tradex as of June 2022, and their bids in the delisting would have tilted the scales toward the discovered price of Rs 172 ($2). "There should be an investigation into this," says the first Hexa Tradex minority investor.

Hexa Tradex has dismissed the allegations as baseless, saying that it was not privy to the decision-making process of any of the company's shareholders.

The events before and after the delisting proposal at Elcid are no less intriguing.

Just a couple of days before the proposal in March, Hydra Trading—an investment entity controlled by the Danis, another promoter group of Asian Paints—bought about 9% in Elcid from Rajan Shah of 3A Capital.

The deal was said to be warehousing Elcid's shares with a "friendly" party to see the delisting through. The price of the Hydra-Shah deal is not known. Both Shah and Hydra Trading later claimed ignorance of the impending delisting proposal at the time of finalising the deal. Shah says that for him, it was a matter of an exit after a long delay and protracted legal battle.

Be that as it may, what followed was a curveball. Hydra Trading voted *against* the Elcid delisting proposal, say more than one minority shareholder. This was even as many dissenting minority shareholders voted *for* the proposal in the hope of bidding up the discovered price and getting relief from the powers that be.

Why Hydra Trading did what it did is unclear; it did not respond to questions sent by *The Ken*. Minority shareholders think Hydra Trading may have become wary of the possible blowback from supporting the delisting proposal soon after picking up a major stake—a smoking gun, so to say, of collusion with the promoters.

Tushaar Talwar, a lawyer-cum-investment expert who analyses delisting situations, thinks Hydra's "against" vote may only be a "strategic retreat". "Having bought 9% of Elcid's shares and seeing the public attention, they may have considered it better to back off now and try again later from a much stronger position. With a chunk of shares now in friendly hands, getting the delisting done on their terms will be far easier for the promoters in the future," he says.

Talwar adds that promoters generally have a forte—patience. Expect another shot at delisting Elcid sooner or later, he quips.

There was more irony to come. After the delisting proposal fell through, Bharat Talati, who resigned as an independent director in Elcid on 5 August, sold his and his family members' shares in off-market transactions on 17 August. The price? Rs 1,18,000 ($1,500) a share—far less than the delisting floor price of Rs 1,61,000 ($2,000). "Maybe, the insiders thought that with the delisting can kicked down the road again, this lower price was a fair price," says an Elcid minority shareholder.

Or maybe, they just wanted to monetise their investments quickly and move on. Either way, it signalled the perils of a failed delisting for minority shareholders. When it comes to delistings, practicality eventually trumps posturing, say experts. Rule changes, if and when they happen, will need to consider this, they add.

Practicality over posturing

The 2021 change in the Sebi rules for delistings had its heart in the right place. For instance, it streamlined timelines and introduced recommendations from independent directors to get the best deal for minority shareholders. But clearly, the arguments continue thick and fast, and many delistings are in limbo.

"The delisting process hinges on the board being truly independent and doing its job well to protect the interests of all stakeholders, especially minority shareholders who are vulnerable. That doesn't always happen," says Murali Neelakantan, principal lawyer at law firm amicus.

He explains the apparent contradiction in the Companies Act and the Sebi rules in this matter. "Under the Companies Act, there is a clear duty on directors to get the fair value for shareholders. Fair value should ideally be found by utilising the appropriate method of valuation after considering all methods of valuation," he says.

But Sebi has prescribed a formula for the floor price that lays store mostly on the past price of the stock, he adds. The wisdom of the market, while being a good indicator of fair value, may not be suitable in all cases. "When shares are required, under the Companies Act, to be issued at the fair price, shouldn't they also be bought back or delisted at the fair price," he asks.

> Sebi needs to update the delisting and the preferential allotment regulations to align with the Companies Act, 2013
>
> **MURALI NEELAKANTAN, PRINCIPAL LAWYER AT AMICUS**

Sebi didn't respond to queries until the time of publishing this story.

Experts caution against broad strokes, though. Just because some minority shareholders sell at what others perceive to be a low price, it doesn't mean that they are acting at the behest of the promoters. Investors are unique, and so could be their motivations.

They also make a pitch for practicality. "Trying to get the full value of shares in a delisting is idealistic and may not work," says Rajan Shah. He explains that promoters would factor in their costs and taxes in the present and the future. So, while a 75% cut in the fair value may be taking it too far, minority shareholders should perhaps be ok with a 30-40% cut, he says.

Also, betting on delistings and high discovered prices is a high-risk game, and the payoffs may not always work in the minority shareholders' favour. For instance, many delisting candidates, such as Vedanta, crashed on the bourses when the offers failed. "Shareholders are people of the world; they must walk in with their eyes open and know the possible outcomes," says Neelakantan.

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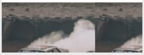

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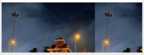

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