

Stop Being an IPOcrite



M C Govardhana Rangan

The listing of Hyundai Motor Co's India unit next week, reversing the trend of global firms pulling out of domestic stock exchanges, is set to create history. It's no surprise that Hyundai is receiving investor attention in a market humming with activity as savers chase stocks as if there is no tomorrow. Fledgling companies with not much to show by way of profitability are getting valuations that would make sellers anywhere in the world salivate.

India's 64 major IPOs raised as much as \$9.8 bn. That's more than a third of the \$28.4 bn raised in the Asia-Pacific region, going by Reuters-Prime Data-base data.

Hyundai is being priced to yield a valuation as high as ₹1.6 lakh cr (\$20 bn). Its market cap in South Korea is about \$40 bn. If Hyundai's market cap ends up at \$18-20 billion, the value of the Indian entity would represent 45-50% of its consolidated market cap, according to Nomura Securities. This is when Hyundai Motor India's earnings contribution to parent has declined to half of what it was in 2019.

All this makes it tempting to conclude that everything is hunky-dory. But what are the chances of something distorting the markets, especially primary markets?

The rules governing IPOs are skewed in favour of steep valuations helping sellers — promoters and PE funds. The strength of any market — primary or secondary — is its depth, or the liquidity that determines whether the price discovery is fair and



Easy with your mountains, moles

a reasonable outcome of market forces. The government of the day decided that at least 25% of a company's shares must be with public to be traded on the stock exchange.

Sebi also mandates this for all listed companies. But it's twisted when it comes to IPOs, where listing could be done with just a 10% sale or even less. The reasoning behind regulations between listed companies and those headed to markets are inconsistent, even contradictory.

Economics 101 tells us that supply-demand determines price. What would be the price of a stock when the promoter or a PE sold 25% in an IPO instead of the restricted 10%? Obviously, the sale price will have to be far lower than what it is.

When GoI proposed a 25% float about 15 years

Rules governing IPOs are skewed in favour of steep valuations helping sellers — promoters and PE funds



ago, some argued that the Indian market is shallow and can't absorb such a huge sale. Furthermore, it was peddled that those which could command a valuation of \$1 bn need to sell only 10%. Both reasons were fallacious.

Bajaj Housing Finance received bids for ₹3.2 lakh cr last month. Coal India in 2010 got ₹2.3 lakh cr for its IPO. Only an ignoramus would believe that Indians don't have an appetite for big share sales. Since the billion-dollar valuation argument, the rupee has lost value by nearly half. Assuming the same reasoning holds, the minimum valuation should be ₹3,200 cr for a 10% float. Primary market rules make it easier to create artificial demand for the stock with much of the shares sold being locked in for a month, even for six months in some cases.

If one considers anchor allocation that can't be sold for as many as 90 days, pre-IPO placements that can't be sold for a year, and the ultra-HNIs who are advised by funders to hold on, the actual float on debut could be as low as 3% of the company, instead of the 25% flo-

at, which is the spirit of the regulation.

In the recently concluded blockbuster Bajaj Housing IPO, where the sale was about 10%, parent Bajaj Finance sold 93 cr shares at ₹70 a piece. The low float and get-rich-quick greed of investors led to doubling of its price at listing. Within a few days, even Bajaj Finance couldn't resist the temptation to sell. It sold 42 cr shares in the market to raise about ₹7k cr, more than what it raised in the IPO.

Yet another aspect of IPO rules that's strange is the quota system — institutional, individual, HNIs. This was born at the turn of the century when the regulator decided to 'protect' middle-class investors when offer documents were half-baked and stock exchanges weren't even disseminating earnings through websites.

When the governing principle behind the market is democratisation, should there be a stratification of investors — institutional, individual, HNIs? Institutional money is, after all, from individuals. How can losing money through an institution be justified when the same can't be for individuals?

Sebi's IPO rules are nearly 20 years old. Much has happened

When the governing principle behind the market is democratisation, should there be a stratification of investors — institutional, individual, HNIs?



in Indian markets since. The regulator has been active in investor protection in many segments — be it derivatives market or mutual fund investments, or choosing AIFs. But IPO rules remain a neglected area.

Retail individual investors are stacked up against sophisticated PE investors, and opportunistic investment banks. Restrictive rules are leading to the transfer of savings of the common man to the super rich. Scrapping of the quota system and lifting the minimum IPO float mandatory for listing to 25% will go a long way to improve returns for retail investors.