INVESTING Exclusives

India’s IPO market is sizzling hot, but the message is worrisome

Synopsis

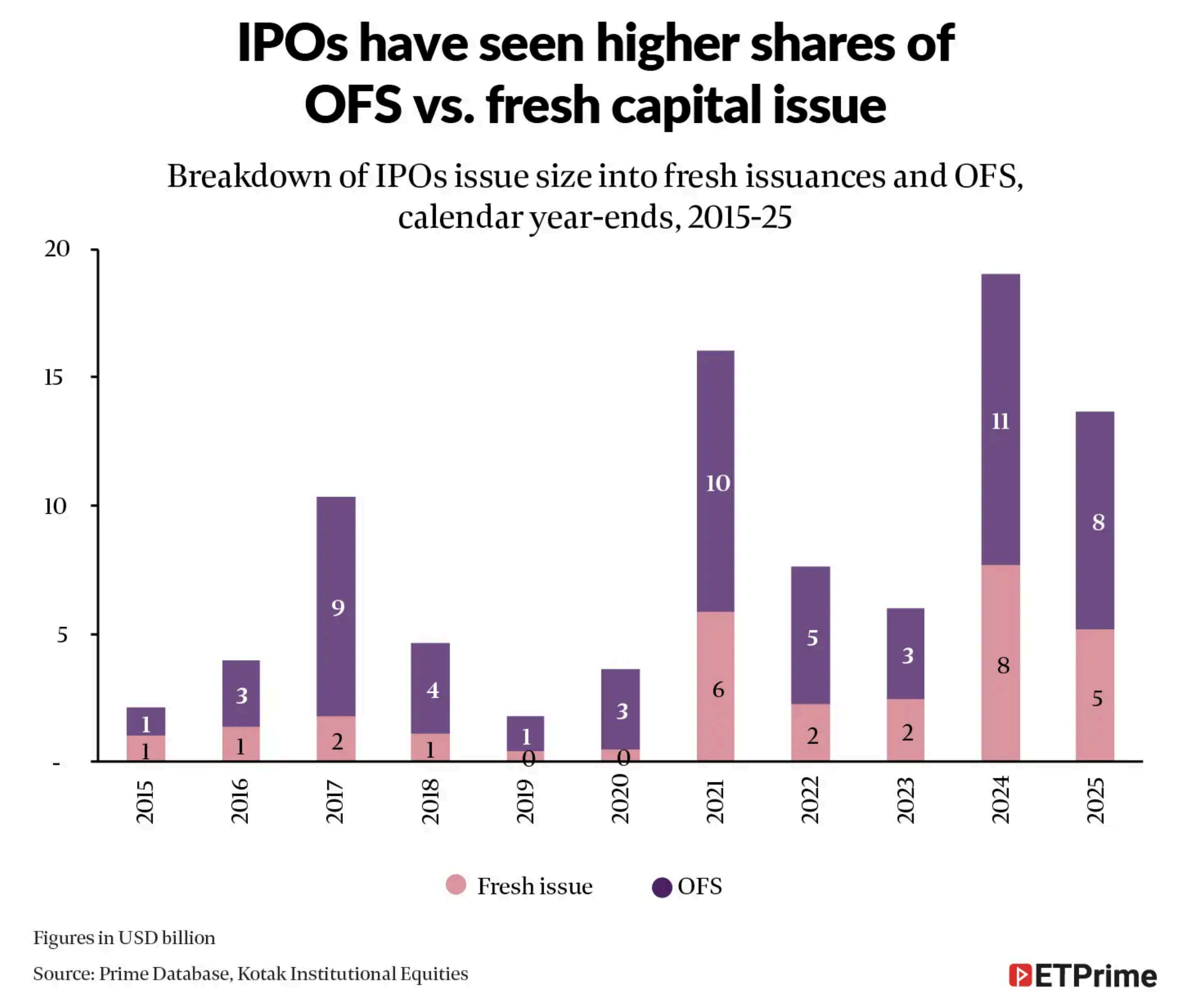
This month has been a record of sorts for the Indian primary market. But an increasing number of IPOs have witnessed tepid listings this year.

Few things in the capital markets are as exciting as initial public offerings (IPO). It is believed to be a sure shot bet to make gains that are impossible in the secondary market. The dynamics in the primary markets are different in a sense that it could be managed well with the aid of regulations, unlike the secondary market where the demand-supply dynamics determine stock prices.

This month has been a record of sorts for the **Indian primary market**. The IPO of LG Electronics received the highest demand ever at INR4.4 lakh crore. It didn’t stop there. It soared more than 50% in a matter of days for those LI (lucky investors) who were allotted the shares. The long-awaited listing of Tata Capital also materialised.

Promoters are happy. Private equity investors making manifold returns are laughing their way to the banks. Those with ESOPs are cheering, and the investment banking community is celebrating. Why not? The average expense on an issue is about 9%, much of which goes to bankers as fees. But what's in store for the economy in general and investors (including in mutual funds that buy these IPOs) in particular?

Elementary economic theory is that capital markets channelise savings of citizens into productive purposes. This is the underlying belief with which governments and regulators craft the rules of the game.



In the last few years when the **capital market** is buzzing, one missing link for the economy has been the lack of investments by companies in raising their capacity. IPOs alone raised more than INR5 lakh crore in less than five years. Despite this, policymakers from finance minister to the RBI governor are hopeful that industry eases the purse strings on investment as data still show a tepid outlook.

“The analysis of project finance data points to lower investment optimism as reflected in tepid total cost of projects during 2024–25 as compared to previous year,” said a research paper published in a recent RBI bulletin. “The **investment outlook** remains cautiously optimistic. While external risks such as geopolitical tensions, global uncertainty and demand slowdown may influence **investment sentiment**, the domestic fundamentals appear robust.”

Policymakers are looking for an answer as to why investments aren’t coming through despite a buoyant capital market, they need to look at where these funds are going.

Of the more than INR5 lakh crore raised in the past five years, nearly INR3.3 lakh crore has gone to promoters and private equity investors and in many cases the IPOs were priced at more than 25 times their cost of acquisition with significant returns, while returns for public market investors are flagging.

What is more revealing is how much proportion of the funds that companies raise were being utilised for capital equipment or capacity expansion. Of every INR100 raised, just about INR19 went to capacity expansion or spent on plant and machinery. A similar amount was declared to be going for working capital, and a third to repay debt, data from Kotak Institutional Equities (KIE) shows.

Debt payment, working capital and expansion are the key objects of the fund raising

IPO fund utilization objects, calendar year-ends, 2021-25

Fund requirements	2021	2022	2023	2024	2025
Retirement of debt	17	20	22	18	32
Capital enhancement/Working capital	17	14	34	15	19
Expansion/new project/plant & machinery	25	18	15	8	19
General corporate purpose	16	13	11	14	11
Issue expenses	5	9	9	6	9
Investment in subsidiary/joint venture /associate companies	2	4	6	27	5
R&D	—	2	—	3	2
Acquisition/strategic investment	12	22	2	5	1
Other	7	—	1	5	1

Figures in percenr

Source: Prime Database, Kotak Institutional Equities

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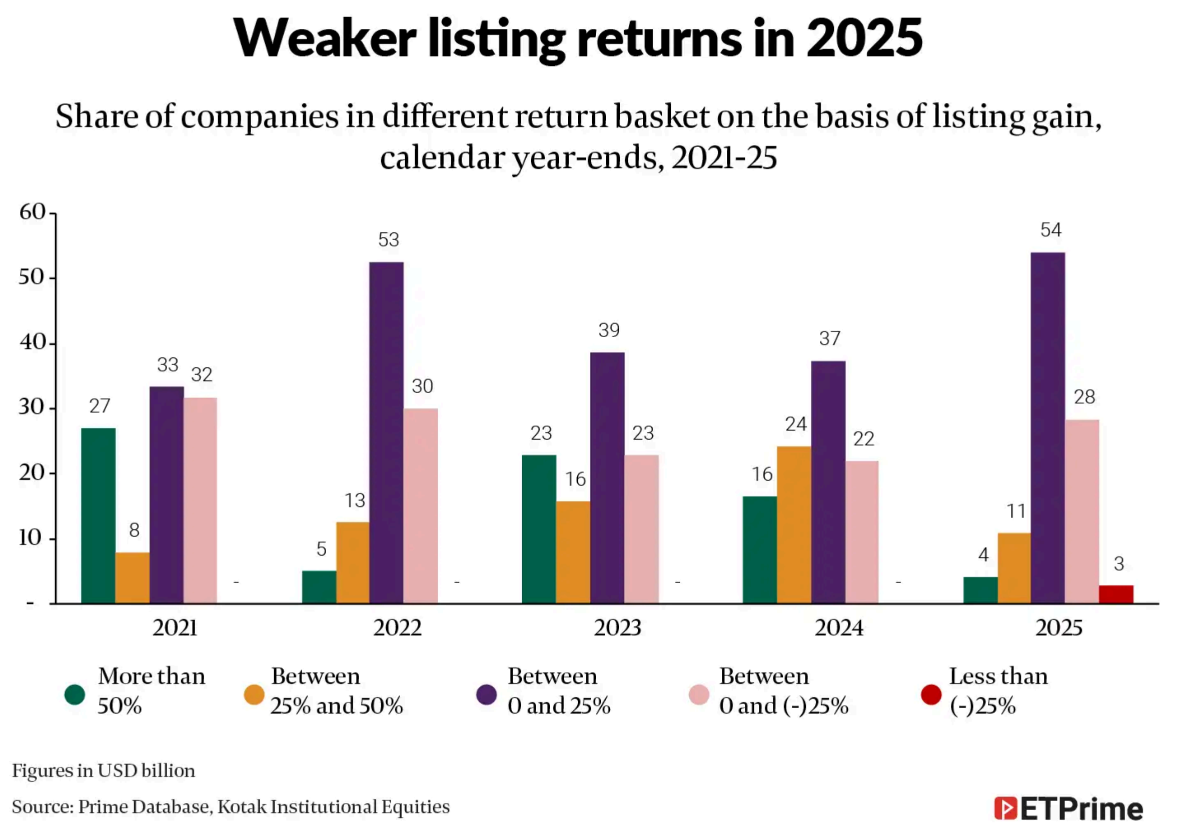
Conventional textbook argument could be that the promoters and private equity investors would reinvest the money in building other businesses, but the composition of the 'exits' and the capital outflow could convey a different story.

In the current fiscal year, net foreign direct investment (FDI) saw an outflow of USD616 million for the first time in August as repatriation was more than the inflows. It may not just be the private equity that is reaping a rich harvest, but even companies such as Hyundai and LG are capitalising after remaining invested for more than two decades.

In a market economy, the forces of supply and demand determine the prices, but the sliding investments in capacity expansion and soaring **stock valuations** are beginning to tell on the returns.

"An increasing number of IPOs have witnessed tepid listings in 2025, with only 15% of companies delivering more than 25% return compared to 41% in 2024," KIE strategist Sanjeev Prasad said recently.



"Furthermore, over 2021-25, almost 27% of companies listed below their issue price. Data shows that a significant proportion of companies failed to maintain their gains even after a decent listing."

Much of these gains are also based on a short term where the market hasn't witnessed a bear market, which is measured as a 20% fall from the peak for key indices. Historically, IPOs in the bull markets have had poor returns over a longer term, or in some cases like Reliance Power and Punj Lloyd led to wiping out of investments.

There are some murmurs on how valuations of companies such as LG and Hyundai are defying logic when compared to their parent firms.

“Institutional investors appear increasingly selective, favouring issuers with strong fundamentals and issuances with reasonable valuations,” says Kotak’s Prasad. “Retail investors may also turn more selective given the recent underperformance and limited listing gains.’”

While the music is on for those looking to exit through IPOs, policymakers looking for investment by companies and public market investors may be less fortunate.

(*Graphics by Sadhana Saxena*)

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