

SME IPO framework overhaul: Can SEBI deepen liquidity, protect investors without shutting out growth-oriented SMEs?

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Synopsis

As SEBI plans to overhaul the SME listing framework, the key challenge for the regulator will be strengthening investor protection while improving liquidity and keeping public-market access viable for growth-oriented SMEs.



The real test for SEBI will not be whether it can make the segment stricter, but whether it can make it smarter, more liquid, and more credible.

India's SME (small and medium enterprise) capital market is heading for a regulatory reset. Recently, Tuhin Kanta Pandey, Chairman of the Securities and Exchange Board of India, indicated that the regulator is preparing a comprehensive consultation paper to overhaul the SME listing framework after noticing ongoing issues with trading liquidity, market making, underwriting costs, and migration to the main board.

The real test for SEBI, however, will not be whether it can make the segment stricter, but whether it can make it smarter, more liquid, and more credible without shutting genuine small companies out of public markets. Striking that balance will be no easy task.

The review comes at a critical moment for India's SME ecosystem. While the platform has emerged as an important fundraising avenue for smaller businesses, it has also drawn scrutiny regarding its governance practices, speculative trading, and inadequate investor protection.

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At the heart of the debate is a contradiction. Rules introduced to protect investors, especially higher application sizes and larger trading lots, may have inadvertently reduced liquidity by limiting participation in the secondary market. The challenge before SEBI, therefore, is not simply to tighten regulation but to redesign the market so that investor protection and capital formation reinforce, rather than undermine, each other.

Liquidity is the first test of reform

Liquidity is the biggest structural weakness in the SME market, according to experts. Large trading lots, limited participation, and shallow secondary-market trading make it difficult for investors to buy or sell without moving prices. SEBI has flagged odd-lot trading and poor liquidity for review. For participants, thin liquidity can distort price discovery, raise volatility, and increase manipulation risk. A market where even small trades can swing prices sharply may struggle to build long-term investor confidence.

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SME IPOs 1.1.2015 ONWARDS						
CALENDAR YEARWISE SUMMARY						
YEAR	NSE			BSE		
	NO.OF ISSUES	ISSUE AMOUNT (Rs.crore)	AVERAGE OF % GAIN / LOSS CLOSE PRICE ON LISTING V/S OFFER PRICE	NO.OF ISSUES	ISSUE AMOUNT (Rs.crore)	AVERAGE OF % GAIN / LOSS CLOSE PRICE ON LISTING V/S OFFER PRICE
2015	6	45	6.12	37	216	6.64
2016	24	186	7.09	43	351	3.86
2017	78	1,193	8.94	55	486	4.74
2018	78	1,325	4.80	63	962	3.52
2019	15	178	2.60	36	446	2.08
2020	7	51	1.09	20	108	0.86
2021	24	351	23.96	35	395	10.55
2022	56	1,162	40.95	53	712	24.17
2023	120	3,376	42.85	62	1,310	27.56
2024	174	6,837	64.55	66	1,924	47.41
2025	117	5,490	15.64	150	5,965	10.03
2026 (listed till 21.8.2026)	43	2,348	10.77	73	3,013	11.23

Source: primedatabase.com

NO.OF SME IPOs MIGRATED TO MAINBOARD			
YEAR	NO.OF ISSUES	YEAR	NO.OF ISSUES
2015	10	2021	65
2016	11	2022	62
2017	21	2023	38
2018	18	2024	14
2019	38	2025	22
2020	56	2026 (till 21.8.2026)	7

Source: primedatabase.com

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Shekhar Bhandari, Head of SME at [Kotak Mahindra Bank](#), says the proposed review presents an opportunity to address the difficult balance between the cost of listing and efficient trading after listing. “SEBI’s proposed review is timely, as the current framework involves a difficult trade-off between the cost of listing and the ease of trading after it. Reviewing lot sizes, market-making, and underwriting requirements, along with creating a clearer path to the mainboard, could make the platform more efficient for credible, growth-oriented SMEs. The focus should be on improving access to capital and market liquidity while keeping governance, disclosures, and investor protection at the centre of the framework.” The liquidity gap has widened as SME listings surged. While primary issues have drawn strong interest, the secondary market hasn’t kept pace in depth, prompting SEBI to examine whether the current structure can support sustained trading.

Can this overhaul unlock genuine liquidity?

One of the central pillars of the SME framework has been compulsory market making. The idea was straightforward, i.e., designated market makers would provide continuous buy and sell quotes, helping investors trade even when natural market activity remained limited. However, the effectiveness of this mechanism is now under scrutiny.

Prahlad Krishnamurthi, Chief Executive Officer of data intelligence platform Probe42, argues that market making is an important safeguard but cannot substitute for genuine demand. “The success of SME listing has not been matched by improvements to the secondary-market infrastructure, which continues to lag. The market suffers from illiquidity characterised by large lot sizes, thin market making, and irregular investor participation.”

He says market making should be viewed as support infrastructure rather than the source of liquidity itself. “Market making serves as a safeguard but not as a substitute for real buyer and seller demand. Migration to the Main Board must be made more clear-cut and transparent.”

The distinction is significant. A market maker can provide quotes, but sustainable liquidity ultimately depends on a broad investor base willing to participate because they have confidence in the underlying company and sufficient information to assess the risks. That is why several experts believe SEBI’s reforms must address the broader ecosystem instead of focusing exclusively on market-making obligations.

JPD Precision Fasteners Founder & Director Ramesh Goyal, however, believes market making has contributed meaningfully to the growth of the SME platform and should be strengthened rather than diluted. “Liquidity is important for building sustained investor confidence in SME stocks. SEBI can further strengthen the existing market-making framework and look at trading mechanisms that improve price discovery and ease of transactions,” says Goyal.

According to Goyal, the market should become more outcome-oriented, measured by the quality of liquidity it generates rather than merely by compliance with formal obligations.

Investor protection must go hand in hand with wider participation

The most contentious reform may be application size and trading lots, according to experts. SEBI had raised the minimum threshold to curb retail speculation and volatility, aiming for more informed participation. But some argue it targets the wrong variable.



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SEBI had earlier raised the minimum application size from Rs 1 lakh to Rs 2 lakh to curb speculative activity.



“A higher entry threshold does not in itself ensure that an investor is better informed or that the decision is based on a more rigorous assessment of fundamentals,” says Yogesh Chande, Partner at Shardul Amarchand Mangaldas.

“The focus may need to move beyond ticket size and towards broadening the market. The objective should be to avoid a framework in which measures designed to deter speculation inadvertently reduce liquidity,” he says, noting high minimums narrow the investor base and concentrate allotments.

“Maintaining a higher trading lot may create a significant capital barrier for investors seeking to enter or exit, resulting in reduced trading frequency and impaired liquidity,” Chande adds.

Ritaban Basu, CEO of B2K Analytics, says, “The core problem with a blanket Rs 2 lakh entry ticket is that it filters investors by purchasing capacity, not judgment. It shrinks the pool of natural buyers and sellers, which feeds the odd-lot problem.

Notably, SEBI had earlier raised the minimum application size from Rs 1 lakh to Rs 2 lakh to curb speculative activity and limit participation to investors with greater financial capacity.

Basu suggests a risk-based approach—grade SME issues on financial and governance strength and allow smaller lots and limited retail participation for stronger issuers.

An email has been sent to SEBI seeking its response. The story will be updated as and when a response is received.

Better information may matter more

For stakeholders, illiquidity is linked to information asymmetry. With shorter track records, little analyst coverage, and fewer data points than mainboard firms, SMEs are harder to evaluate on financials, ownership, litigation, and governance.

“Information asymmetry is particularly significant for SMEs, since investors have less public information and firms have limited history. Improving accessibility and comparability may be a valuable supplement to trading reforms,” says Krishnamurthi.

He notes data is fragmented across hundreds of government and regulatory databases, forcing expensive, repetitive manual checks and often relying on year-old financials. Ownership, litigation, and charge details must be pulled from

multiple sources.

“The challenge is to streamline without lowering the regulatory bar. Consistency of verified information would make the due diligence easier and address cost issues,” he says. That logic extends to underwriting—verified, reusable data could cut duplication and improve disclosure reliability.



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The migration to the mainboard has been uncertain, with differing eligibility across exchanges and low predictability.

Simpler regulation should not mean weaker regulation

The SME platform was designed with regulatory concessions because smaller firms cannot meet every requirement for large listed companies. But experts warn lower compliance costs should not mean lower transparency.

“Cutting the compliance load on SMEs doesn’t mean lowering the bar. Most of what companies struggle with isn’t the standard; it’s the repetition,” says Krishnamurthi, noting firms repeatedly submit the same ownership, financial, and litigation records to different intermediaries.

That distinction matters as SEBI reviews underwriting norms. A more efficient due-diligence ecosystem could cut issuance costs for credible issuers without diluting investor protection and make it harder for poor-disclosure companies to get through.

Governance remains the bigger risk

While liquidity dominates much of the policy debate, governance may ultimately prove to be the more important challenge.

Concerns over the SME platform, market manipulation, low liquidity, and weak governance have persisted over the years, says Pranav Haldea, MD of PRIME Database Group. While some frauds have come to light, many may remain undetected, denting investor confidence, he says. SME IPOs surged post-Covid, but hype-driven price spikes have raised concerns that promoters or connected investors exit at high valuations, leaving retail investors with losses.

Haldea flagged risks of insider trading, circular trading, and price manipulation in illiquid SME stocks and questioned the lack of credible institutional investors. SEBI has already passed multiple orders against SME firms for violations, he notes. On reforms, Haldea says the priority should be to restore greater sanctity and credibility. Companies tapping public money must meet stricter eligibility and higher disclosure norms.

He also backed the SME trading lot size increase to Rs 2 lakh, arguing higher entry barriers would shield small retail investors from speculation.

IPO proceeds need closer monitoring

SME issuers face less frequent post-issue monitoring than mainboard companies, with only half-yearly reporting versus mandatory quarterly monitoring-agency oversight for larger issues, notes Basu.

In the proposed overhaul, SEBI could mandate quarterly monitoring of proceeds above a defined threshold to give investors visibility on end-use, experts say.

Similarly, migration to the mainboard has been uncertain, with differing eligibility across exchanges and low predictability.

Meanwhile, the migration rules may also be reviewed.

According to market participants, SEBI should replace fragmented norms with transparent, measurable criteria covering public float, shareholder diversification, governance, financial performance, disclosure quality, and sustained liquidity, rather than relying primarily on capital thresholds. Migration must be made more clear-cut and transparent, says Krishnamurthi.

AI accountability will become the next regulatory frontier

Beyond SME listings, Pandey has also indicated that SEBI is examining accountability around artificial intelligence and machine learning in financial markets.

Siddharth Vishwanath, Partner and Risk Consulting Leader at PwC India, believes AI will become the next major inflection point in market regulation. "Like past triggers around ownership and cyber resilience, AI brings new risks to investor protection and market integrity."

The issue becomes particularly significant for SMEs because many are expected to adopt AI tools developed by third-party technology providers rather than building proprietary systems. "Since most SMEs will be using third-party AI solutions, a key regulatory focus will be on data. The use of AI by SMEs must not compromise the protection of business-sensitive information, customer data, personal information or other confidential data," adds Vishwanath.

He also expects greater scrutiny around bias and flawed decision-making within AI systems. "Regulators will have to make sure that SMEs relying on AI and taking AI-driven decisions do not inadvertently create regulatory, sanctions-related, compliance or conduct risks."

Need a flexible regulatory framework

The SME framework was designed with certain concessions, particularly in disclosure requirements, which were less stringent than those applicable to the main board, says a former SEBI Chairman. At the same time, the minimum investment or trading lot size was kept relatively high, effectively keeping smaller investors away and limiting

participation largely to bigger investors. There were also concerns over whether funds raised through SME IPOs were always being utilised for their stated purposes, he adds.

“Overall, the framework involves a trade-off between ease of doing business and investor protection. SMEs need a more flexible regulatory framework because they cannot be subjected to exactly the same requirements as larger companies. At the same time, there has to be adequate regulatory oversight to protect investors. The challenge, therefore, is to strike the right balance between these two objectives,” he notes.

“The liquidity situation may have improved to some extent in recent years. Over the last two or three years, particularly the last two years, mutual funds (MFs) have shown considerable interest in the small- and mid-cap segments. While foreign institutional investors (FIIs) tend to focus more on large-cap companies, MFs have increasingly invested in small- and mid-cap stocks,” he adds.

Broadly, the issue remains about finding the right balance between ease of doing business and sufficient regulatory oversight to protect investors. The regulatory pendulum can move in either direction, but the objective should be to find a middle ground, he says.