Grey areas in IPO process on Sebi radar

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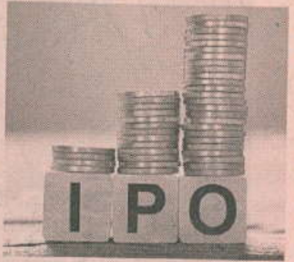

A BIG DRAW AMONG MFs EYEING SMART GAINS

Recent IPOs	Issue price (₹)	Listing price (₹)	% gain
IRCTC	320	644	101
CSB Bank	195	275	41
Ujjivan Small Finance Bank	37	58	56
Affle India	745	929	24

Compiled by BS Research Bureau

Sources: PRIME Database, Exchanges

The Securities and Exchange Board of India (Sebi) wants to address grey areas in the initial public offering (IPO) process that mutual fund (MF) houses' arbitrage schemes misuse to the advantage of one scheme's investors over others. Towards this end, the market watchdog wants to make pre-trade allocations mandatory for all institutional investors.

"Such a practice is unfair to investors of other schemes belonging to the same fund house. If the investor appetite is strong, the fund house after allocation may decide to transfer the shares to arbitrage schemes which can make strong short-term gains in the IPO investment," said a senior executive of a fund house.

Arbitrage schemes have gained significant investor interest in recent months.

In 2018-2019, these schemes garnered over ₹33,500 crore of inflows, as steady returns given by these schemes have attracted flows exiting schemes exposed to credit risks.

"By not informing in advance which scheme would get what allocation, there is a gap in the system that can be easily misused. After allocation, some fund managers can take a call on which scheme should get the allotted shares, depending on their view of the firm and investors' demand," said another executive.

Apart from IPOs, similar issues have cropped up during qualified institutional placements and also bulk deals.

Some fund houses do inform investors in advance about which scheme would get how much allocation, but the regulator wants uniformity in practices across the industry.

In the case of foreign portfolio investors, the problem is likely to arise from the regulations that they are already required to adhere to.

"The proposal would mean placing orders directly in the name of each account. This would lead to different execution prices as orders get filled at a different time. The fund manager would then be forced to allocate at different prices into different funds, which would again be in breach of the fiduciary duty of equitable pricing," said an official of an industry body.

The proposal on pre-trade allocation was also being mulled over by Sebi in the past, but the regulator was unable to implement it back then.

Industry sources said that there have also been cases of MFs taking advantage of this lacunae to the advantage of their flagship schemes.

"A flagship scheme is also an important scheme for a fund house as it accounts for the largest chunk of assets and a lot of investor money is riding on it. However, it means that a fund house is giving preference to one scheme over the other, which is not fair to the other investors," said a fund manager.