

LESSONS FOR INVESTORS

With initial public offerings galore, we give you a cheat sheet to score some good grades



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With the stock markets on fire, it's been raining IPOs in the past few months. About 14 initial public offerings were made in the second half of 2020, collectively raising ₹16,272 crore. Just short of two months into 2021, as many as five IPOs have hit the market and many more are in the pipeline. In most issues, retail investors have joined the IPO bandwagon by the droves, going by the subscription numbers.

But all the offerings are not worth your hard-earned money. Of the 142 stocks that launched their IPOs since 2015 (up to January 2021), about 55 now trade below their IPO ask price.

There have been some high points, definitely. Long-term investors have seen their money more than double in 49 issues. This list includes IRCTC, AU Small Finance Bank, CDSL, the second-order HDFC twins — HDFC Asset Management Company and HDFC Standard Life Insurance Company — and the recent issues of Happiest Minds Technologies and Route Mobile. The IPO investors of Dixon Technologies and Avenue Supermarts — launched in 2017 — saw the stock prices go up by 11 times from the ask prices, raking in gains of over 950 per cent, till date.

But there is still a 41 per cent chance of witnessing capital erosion. The cut can be deep. For instance, the offers of Ortel Communications and Adlabs Entertainment — launched in 2015 — have, till date, eroded more than 95 per cent of investor wealth. Not only this, stocks of Manpasand Beverages, Coffee Day Enterprises and Pennar Engineered Building Systems have now been suspended from trading, following troubled corporate governance.

This makes separating the wheat from the chaff a challenge for investors. Here are a few lessons investors can learn from history before jumping on to the IPO bandwagon.

Lesson #1 Following league investors doesn't always work

Recent IPOs such as that of Burger King and Indigo Paints have seen heightened institutional interest (subscribed more than 35 and 76 times, respectively).

If you have been investing in IPOs based on this trend, beware.

The idea, though seemingly smart, might not always work in your favour, especially if you don't track the exit of these marquee investors, as well.

Take for instance, the IPO of Capacit'e Infracore, that hit the markets in September 2017. The total offer was subscribed more than 130 times; the QIB category (which includes mutual funds, insurance companies, banks and foreign institutional investors (FIIs)) saw oversubscription of 54 times. Consequently, the company, which is predominantly into residential construction, saw a listing-day gain of 37 per cent, despite weakening sentiments hovering around the real-estate space in mid-2017. However, the Qualified Institutional Buyer category almost halved its stake in the company in less than a quarter's time —

from 26.9 per cent in September 2017 to 13.2 per cent in December 2017. The stock fell more than 30 per cent within the next year, and now trades at ₹219 a piece — 13 per cent below its offer price in the IPO.

Similarly, when the Centre attempted to partially sell its stake in HUDCO, institutional investors made a beeline — the QIB category was oversubscribed more than 50 times. Within the 10.2 per cent publicly held stake in the company, institutions were allotted just above 5 per cent (as of May 2017).

However, with the stock rallying by 20 per cent on the listing day, institutional investors soon booked their profits. Institutional holding in the stock declined to 3.7 per cent in June 2017 and to 2.7 per cent in December 2017. The retail investors who continue to hold on the stock are however left in the lurch, with a capital erosion of more than 20 per cent from the offer price in the IPO.

The IPO of Burger King India launched in early December 2020 saw its QIB and HNI categories get oversubscribed 35 and 355 times, respectively. The retail category of the issue was subscribed 60 times.

In less than a month (by end-December 2020), high networth individuals reduced their shareholding to 2 per cent from the 4.1 per cent allotted to the category. Some institutions, too, booked profits (the stock doubled on the listing), reducing their holding to 23 per cent from 26 per cent.

Lesson #2 Fundamentals, valuation matter

The IPO market has seen high-valuation bets wither out in the long run. For instance, the IPO of Prataap Snacks, which came out in the thick of the 2017 bull market, valued the company more than 200 times its FY17 earnings. After posting a listing-day gain of 25 per cent, the stock's one-year returns were a negative 12.6 per cent. Today, the stock trades 28.8 per cent below its offer price.

Parag Milk Foods is yet another IPO (May 2016) that demanded steep valuation — 44 times its FY16 earnings — due to its presence in the value-added dairy segment. The stock also gave its IPO investors 15.3 per cent gains on the listing day.

However, the price crashed the next year following an 80 per cent (y-o-y) drop in the company's net profits to ₹10 crore in FY17. Those who bet on the stock in its IPO have seen a wealth erosion of 50.6 per cent till date.

RBL Bank, yet another darling IPO bet of investors, shrunk investor confidence, after the management (in its quarterly results of June 2019) indicated a plausible deterioration in asset quality in its corporate book. The frayed nerves of investors were further piqued by the pandemic in 2020.

Scoreboard

Year	No. of IPOs	Amount raised (₹ crore)	No. of stocks trading below listing price
2015	21	13,614	10
2016	26	26,494	9
2017	36	67,147	19
2018	24	30,959	11
2019	16	12,362	4
2020	15	26,613	1
2021	4	7,369	1

The bank's collection efficiency was hampered by the lockdown, and it was hit by the change in the MFI (Microfinance Institutions) regulations in Assam. The stock is now down 15 per cent from its listing-day price.

IPO investors need to hence watch out for such adverse signals in the financials and be prepared to bail out when the business metrics exhibit a drop.

Lesson #3 Tread carefully on stocks with regulatory issues

Many IPOs have also been victims of diktat from governing agencies. Classic examples are banks that had to bear the brunt of corrective measures and restraining orders from the RBI.

In 2015, when the RBI distributed small finance bank licences to 10 NBFCs, it also mandated that the banks go public within three years of reaching a net worth of ₹500 crore.

This has resulted in the equity market seeing many small finance bank (SFB) debutants in the last five years, including AU Small Finance Bank, Ujjivan Financial Services and Equitas Holdings. AU Small Finance bank has more than tripled its investor money since its listing in 2017.

However, as the other two NBFCs listed the holding companies instead of the banking subsidiary, their stock prices took a heavy beating when the RBI refused to neither tweak the norm nor grant any material extension of the deadline for listing their respective SFB subsidiaries.

Equitas Holdings posted a listing-day gain of 23 per cent over its offer price, when it debuted in 2016. The stock rallied by another 27 per cent in the one year since listing. However, the exuberance fizzled out in the subsequent years. After the listing of its banking subsidiary in October 2020, the stock now trades at 23 per cent lower than its ask price in its IPO, factoring in the dilution for existing shareholders of Equitas Holdings and the pricing discount for the holding company.

Bandhan Bank is another example. Despite an ask price of over 4.8 times its then book value, the stock demonstrated listing gains of over 27 per cent when it hit the market in March 2018.

However, within the end of the year, the stock began witnessing the pressure of impending promoter dilution. The bank was required to bring

down its promoter holding to less than 40 per cent in less than a year since listing. Apart from rejecting the bank's repeated pleas for extension of the timeline, the RBI also penalised it by imposing a pause on its expansion plans. The enactment of the Microfinance Regulation Act 2020, in Assam was a dampener, too. The bank now trades at ₹348 apiece, a discount of 7 per cent to its offer price in 2018.

Besides banks, the stock prices of PSUs may also be prone to changes due to policies and regulations.

Lesson #4 Flavours may go off season

Another thing to avoid in the IPO market is placing blind bets on trending themes.

While the tailwinds in the industry can sure help boost profits for a company, the fundamental business model plays a more crucial role.

The initial term of the Modi government saw a lot of activity in the infrastructure and construction space — Bharatmala Pariyojana and Pradhan Mantri Awas Yojana (PMAY) were announced. With this, the equity markets, too, went gung-ho about stocks in the segment. During 2015-2017, eight infrastructure companies went public, riding heavily on the PM's flagship programmes. Most of them were into construction of residential buildings or roads.

Investors, too, made a beeline to the issues — the overall subscription crossed over 100 times in the case of Capacit'e Infracore and Salasar Techno Engineering.

While quality bets in the space, such as PNC Infracore (2015) and Dilip Buildcon (2016) more than doubled investors' wealth, half the thematic issues (four) burnt investors' money.

The IPOs of Capacit'e Infracore, Sadbhav Infrastructure Projects, Bharat Road Network and Power Mech Projects now trade at a discount of 13-84 per cent to their offer prices.

In 2020, following the industry tailwinds from the anti-China sentiments, investors were all fired up about stocks in the speciality chemicals space. Chemcon Speciality Chemicals and Rossari Biotech saw roaring subscriptions and listings. It needs to be seen how long they hog the limelight. The IPO of SH Kelkar, a speciality chemical player that went public in 2015, has eroded 32 per cent of investor wealth, to date.

Listing-day gains don't hold up

Top 5 IPO stocks that now lag offer price after rallying on listing day (%)

Company	Offer date	Listing-day gains	1-year return	3-year return	Fall from offer price to date *
Inox Wind	18-03-2015	34.8	-44.1	-73.4	-78.8
Apollo Micro Systems	10-01-2018	65.1	-73.1	-70.2	-59.4
Parag Milk Foods	04-05-2016	15.3	-2.4	0.7	-50.6
PNB Housing Finance	25-10-2016	14.9	57.3	-34.8	-44.2
SH Kelkar & Co	28-10-2015	15.2	35.3	-7.2	-32.4

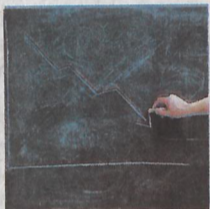
Stocks that have shined

Top 5 gainers (%)

Company	Offer date	Listing-day gains	1-year return	3-year return	Gains from offer price to date *
Dixon Technologies	06-09-2017	63.8	-5.5	236.8	986.7
Avenue Supermarts	08-03-2017	114.3	109.1	199.0	967.0
IndiaMART InterMESH	24-06-2019	33.9	61.2		779.5
Affle India	29-07-2019	17.5	110.5		620.9
Route Mobile	09-09-2020	86.0			449.2

Source: primedatabase.com

*until February 17, 2021



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Of the 142 stocks that launched their IPOs since 2015, about 55 now trade below their IPO ask price; only 59% currently trade above their IPO prices



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