

CHANGING TIMES

# The Indian IPO wave throwing the rulebook out the window

From loss-making companies winning big to the gradual disappearance of promoters, India's new generation of listed companies aren't letting stock market dogma hold them back. Will the gains sustain, though?

Prajakta Patil, Anand Kalyanaram, Aishwarya Viswanathan, 18 Aug 2021

The IPO deluge underway since the last year is markedly different from listings in earlier years

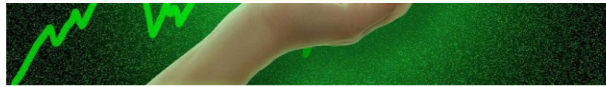
Companies driven by investors rather than promoters are making a beeline to list

So are loss-making startups aided by market regulator Sebi that is set to tweak rules

Massive oversubscriptions and big listing gains have fed into each other in a raging bull market. But caution is warranted



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**HIDE SUMMARY**

Indian IPOs have never been as common, yet they've never been so different from what we've come to expect from companies going public.

Close to 50 IPOs have hit the market over the past year—eight of them in just the past fortnight or so. And with a quarter of the year still to go, many will join their ranks before the year is out. As such, 2021 will be one of the most prolific years in the history of the Indian markets.

A closer analysis of these companies, however, reveals a marked difference from the usual IPO trends. The gradual disappearance of the company promoter in favour of public investors like VCs and PE firms, for instance. Or the spike in loss-making companies trying their luck on the bourses.

Ordinarily, both promoters and profits were key considerations for stock market investors. However, the lack of these two factors hasn't dulled enthusiasm for their IPOs. Foodtech leader Zumato, for instance, had close to no promoter shareholding, while also being loss-making. Its IPO was oversubscribed many times over, with its stock price shooting up on listing day.

In today's story, we parse these trends, showing how these big changes have big implications.

A bull run in the stock market brings with it the usual hangers-on. This time too, it's no different. A spate of initial public offers (IPOs) has flooded the Indian stock market since the middle of 2020 when the bulls, driven by liquidity, started charging at breakneck speed.

Close to 50 IPOs have hit the market over the past year—eight of them in just the past fortnight or so. Many more are coming, and the market can't seem to get enough. Most IPOs are being oversubscribed many times over and across investor categories. The eye-popping gains on listing day that result from this exuberance are feeding a virtuous cycle. Among high-networth individuals, the oversubscription, on average, has been close to 200X over the past year or so, according to markets data provider Prime Database.

Despite a quarter of the year still to come, 2021 has already cemented its place as one of the most prolific years in the history of the Indian markets —both in terms of number of listings and money raised. Next year may be even better, with Life Insurance Corporation of India (LIC)—the country's oldest and largest insurer— set to go public. The mother of all IPOs, LIC is expecting to raise upwards of Rs 1,00,000 crore (US\$13.5 billion) through its listing, which is expected early next year. Advance that by a few months, and 2021 will be hard to beat for a very long time.

But even as IPOs become more and more common, they've grown increasingly different from what we've come to expect in the past. We pored through the mainboard IPO data provided by Prime Database for companies that listed between 2016 and 12 August 2021 to identify how things are changing, why, and what this means going forward.

Among the new trends, many companies with little or even no 'promoter' shareholding are lining up to go public. That's a break from the past, when promoters usually held pride of place in the shareholding tables. Joining the IPO queue are loss-making companies, with more of these than ever before gearing up to test the appetite of public markets. Think, for example, startups like foodtech major Zomato, which upended traditional valuation metrics with its stellar listing.

These big changes have big implications.

### Of IPOs and red herrings

Fittingly for an analysis of IPOs, there are red herrings. For instance, IPOs often have a higher share of fundraising from offers-for-sale (OFS)—the sale of shares by existing shareholders—than from fresh issues of shares.

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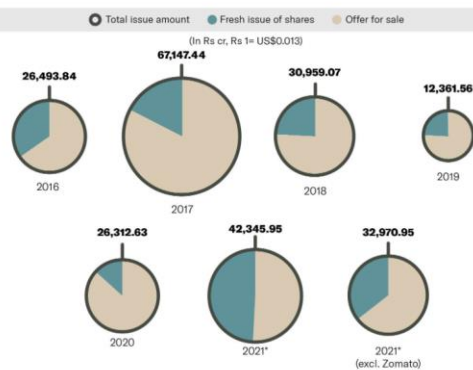


In an OFS, existing shareholders sell shares and keep the funds. In a fresh issue, the company issues additional shares and keeps the money. Bull market IPOs, in particular, see a higher proportion of OFS fundraising, with sellers seeking to make the most of a buoyant market and pricey valuations. In the bull runs of 2017 and 2020, OFS accounted for between 83-87% of the overall fundraising in those years.

Surprisingly, after nearly eight months of 2021, the OFS and fresh issue proceeds seem nearly evenly balanced, despite the raging bull market underway. An outlier, it turns out, is distorting the picture. Zomato, the largest IPO so far in 2021 (raising about Rs 9,400 crore (~US\$1.26 billion)) was almost entirely a fresh issue of shares. Its investors are still holding on to most of their shares, likely in pursuit of a bigger pot of gold. But for this, the scales again tilt in favour of OFS, with a 65% share of the overall IPO fundraising so far in 2021.

## Offers-for-sale (OFS) dominate

More IPO money is raised through existing stake sales than through fresh issue of shares



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Graphic by Prajakta Patil

Source: primedatabase.com, 12 Aug.'21

## No promoter? No problem

Other changes, however, indicate a significant deviation from tradition.

On 6 August, the board of market regulator [Sebi] took the first step towards a change that has been a long time coming. It approved a shift from the concept of 'promoter' to 'person in control' or 'controlling shareholders'. Sebi will now work with other regulators and prepare draft amendments to securities market regulations to pave the way for this transition.

This far-reaching change is in keeping with the changing shareholding contours in many Indian companies. Earlier, promoters held the majority of shares in most companies and ruled the roost. Now, diversified public shareholders hold a chunk of shares in a new crop of companies that are largely board-controlled and professionally run.

This is especially true for many tech startups, which reach the IPO threshold being majorly-owned by professional investors such as venture capital (VC) and private equity (PE) firms. These investors are categorised as public shareholders. By the time Zomato was eyeing a debut on the bourses, its public shareholding was 100% and its promoter shareholding, over many rounds of fundraising and dilution, was practically non-existent.

Zomato is hardly alone. The likes of gaming firm Nazara Technologies and auto classifieds platform CarTrade, which also have low promoter shareholding, have already IPOed. These companies are already part of the new normal that the Sebi board has envisaged. The shift is reflected in the higher average public shareholding (non-promoter shareholding) in the IPOs of 2021 and 2020, compared with those of 2019 and 2018.

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## New phase

Back in 2016-17, banks and financial services companies dominated the list of low/no-promoter entities due to their regulatory requirements. Now, tech companies and startups are leading the charge.



This trend is only expected to speed up going forward, with the likes of payments decacorn Paytm\* set to go public in the next few months. Alibaba's Ant Group, SoftBank's Vision Fund, and SAIF Partners own nearly 68% of the company. At 14.67%, the stake of Paytm founder and chief executive Vijay Shekar Sharma pales in comparison.

## Public on the rise

Led by tech startups, average non-promoter (public) shareholding in IPO-bound companies is climbing over the past 2 years

Pre-IPO shareholding



Top 10 companies with highest Public shareholding pre-IPO

Company name	Sector	Listing date	Public
Equitas Holdings	Financial services/investments	21 Apr,'16	100%
Ujjivan Financial Services	Financial services/investments	10 May,'16	100%
RBL Bank	Banking/term lending	31 Aug,'16	100%
BSE	Financial services/investments	03 Feb,'17	100%
Tejas Networks	Telecommunications	27 Jun,'17	100%
Indian Energy Exchange	Financial services/investments	23 Oct,'17	100%
Uti Asset Management	Financial services/investments	12 Oct,'20	100%
Zomato	Food technology	23 Jul,'21	100%
Nazara Technologies	Information technology-software	30 Mar,'21	79.3%
Central Depository Services	Financial services/investments	30 Jun,'17	76%

THE KEN Graphic by Prajakta Patil Source: primedatabase.com, The Ken research, 12 Aug,'21

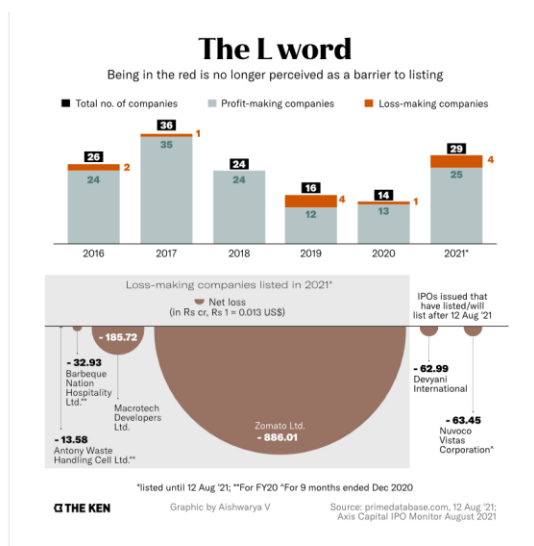
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Long used to the concept of 'promoters', who were perceived as the driving force and with whom the buck stopped, shareholders, founders, and corporate India must adjust to this new reality. One where professional investors could be more mercenary-like than traditional promoters in their approach to capital allocation, long-term view of the business, and restructurings (including exits). Founders may also pitch harder for superior voting rights that give them a higher say than their shareholding allows. Sebi is reviewing the framework for such shares and issued a discussion paper to this end in July.

### Losers also win

It's a brave new world in the IPO market in India. Losses don't dissuade companies from public listings, nor do they drive away eager investors keen on a slice of such companies. As many as six companies out of the 37 that have IPOed so far in 2021 (including 8 that would list after 12 August) were loss-making. Since 2016, never have so many loss-making companies gone public. And investors have lapped these IPOs up.

Prominent names here include Zomato, real estate giant Macrotech Developers (popularly known as the Lodha Group), restaurant chain Barbeque Nation, and Devyani International, which operates food and beverage chains such as Pizza Hut, KFC, and Costa Coffee in India. Another six loss-making companies are already on the 2021 IPO horizon, including insurance aggregator PolicyBazaar, Paytm, and budget airline GoAir.



Now, there's nothing stopping loss-making companies from making a beeline to list. Sebi allows for this, though with some guardrails to protect retail investors. While profitable companies can offer 35% of the IPO shares to retail investors, loss-making companies can only offer them 10%. Still, investors would do well to look before they leap into such IPOs. Among other factors, it's good to assess whether there is a path to profitability, if losses are reducing, and if the company is a market leader with a good competitive moat.

Loss-making IPO companies have also upended traditional valuation metrics such as  $P/E$  (Price-to-earnings), and  $EV/Ebitda$  (Enterprise Value-to-operating profits). Instead, metrics such as  $P/S$  (Price-to-sales),  $EV/Sales$  (Enterprise Value-to-sales), etc., are in vogue for such companies.

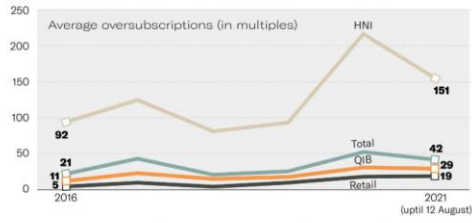
### Oversubscription overfloweth

Despite the high valuations and novel metrics, investors are rushing in to try and get a slice of these IPOs. On average, the overall oversubscription in the public issues we've seen in 2020 and 2021 (about 45X) is higher than in the previous IPO bull run in 2017 (43X).

This heightened interest is seen across investor categories—be it qualified institutional buyers (QIBs), high net worth individuals (HNIs), or retail investors. HNIs, in particular, have rushed in—with oversubscription in 2020 and 2021 close to 200X.

## Mad rush

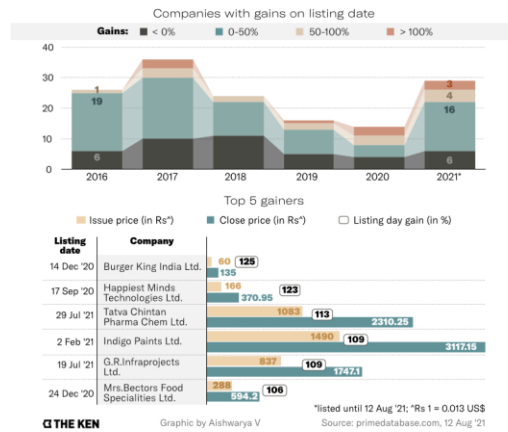
IPO oversubscription across investor categories has shot up in 2020 and 2021



Such heavy oversubscriptions have played a big part in the healthy listing gains being seen in most of today's IPOs. This, in turn, prompts oversubscriptions in new IPOs. Since the beginning of 2020, six IPOs—including that of IT services firm Happiest Minds and QSR chain Burger King India—saw their share prices soar to more than double the issue price by the close of listing day. Overall, the outperformance of IPOs in 2020 and 2021 is better than during the 2017 bull run.

## Outsized gains

Many IPOs in 2020 and 2021 have doubled or more on listing day



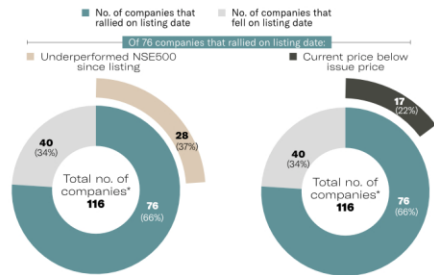
## Does the pop sustain?

Oversubscriptions and listing day gains are all well and good. At least if you are lucky to get an allotment of shares and play the IPO flip game by selling on listing day. For those that want to hold the shares for longer, though, there's more uncertainty. Listing day gains do not necessarily guarantee the company will outperform the broader market in the short to medium term.

Of the 116 stocks that IPOed between 2016 and 2020, about 65% (76 stocks) rallied on listing day. Of these, about four in 10 IPO stocks from 2016 till 2020 have underperformed the broader [Nifty 500 index](#) till date. Worse, one in five have fallen below the issue price since. Besides, some recent IPOs, such as Glenmark Life Sciences, Krsnaa Diagnostics, and Windlas Biotech, have seen rapid listings with single-digit gains or even losses. The lesson: weigh what you buy and hold carefully. Fads are temporary, fundamentals are permanent.

## It's a marathon...

Despite initial gains, many companies see their share prices dip over time



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Graphic by Aishwarya V

\*Companies listed between 2016 and 2020  
Source: primedatabase.com, 12 Aug '21

\*Paytm founder Vijay Shekhar Sharma is an investor in The Ken

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BSE CarTrade Devyani International IPO LIC Nazara Tech NSE Paytm

Stock market Zomato Zomato IPO

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