INDIA BUSINESS
LAW JOURNAL

Running with the bulls

With funds raised from ipos in india at an all-time high, it is the enthusiasm of retail investors that is fuelling the charge. Georgy Thomas reports.

It was a record year – a stampeding bull market in 2021 that ran in a record INR1.1 trillion (USD15.9 billion) worth of fundraising from IPOs, with corporate lawyers quick to tell *India Business Law Journal* much of it was due to increased retail investor participation.
Numbers shared by the government in its Economic Survey 2021-22 seem to back this up. The survey notes that the share of individual investors in the NSE equity cash segment increased from 38.8% of total turnover in 2019-20 to 45% in 2020-21, and 44.7% so far (April to October 2021) in 2021-22. From April to November 2021, nearly 22.1 million individual demat accounts were added for online trading, the survey says. For the record, the IPO market in calendar year 2021 saw 63 companies racing to a record mop-up. The sum raised was nearly double the previous record of INR688.27 billion by 36 companies in 2017.

In 2020, 15 companies garnered INR266.13 billion from the public market. So, last year's INR1.1 trillion fundraising was more than four times the 2020 figure.

Siddhartha Sivaramakrishnan, a Singapore-based partner at McDermott, tells *India Business Law Journal* that trading volumes would be huge if something like the "tremendous" IPO activity in China, a lot of which is driven by retail investors, were to happen in India. "Companies could be doing IPOs every day of the year for the next several years and still not meet the demand from that segment of the population," he says.

MARKERS OF A DEEP MARKET

Is India on its way to the long-cherished goal of deepening its equity capital markets? To answer this, we need to know what makes a deep equity capital market. According to Siddhartha: "The way that you deepen it is by widening the range of investors who participate, bringing in not just the hedge funds, but making sure the mutual funds, the domestic saving schemes, etc., are investing." In his view, retail investors consider participation in sophisticated financial market products as a means to grow.

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Juhi Singh
Partner
S&R Law

Juhi Singh, a New Delhi-based capital markets partner at S&R Associates, considers a deep market one where large players and retail investors co-exist. She lists a few factors that made the surge in retail participation possible, the first being the introduction of a unified payments interface (UPI).

"It has become easier for retail investors to invest in IPOs through the UPI mechanism," she says. "This is a development that has happened over the past couple of years." Second, she notes internet penetration has made it possible for retail investors to trade through smartphones using the apps created by brokers. Third is the effect of increased participation from both tier-2 and tier-3 cities, as well as the addition of millennials to the pool of investors.

The role of retail investors in last year's record IPO fundraising was acknowledged by others as well. Prashant Gupta, a New Delhi-based partner and national practice head in capital markets at Shardul Amarchand Mangaldas & Co, notes: "Retail and HNWI [high net-worth individual] investors have been participating in IPOs at record levels, further driving the IPO market."

Bobby Majumder, a Dallas-based member at Frost Brown Todd, observes that a spike in domestic retail investor participation contributed to the bumper year in India's capital markets.

HEDGE AGAINST UPCOMING VOLATILITY?

Will retail investors be able to fuel another record year for the market this year? The question acquires urgency since the anticipated rate hikes by the US Federal Reserve to tame inflation is expected to send ripples through equity markets everywhere.

The rate hikes will strengthen the dollar, which will erode returns for international holders of emerging market (EM) stocks and bonds, hence the fear that they will dump EM assets in case of larger than expected hikes.

As per the projections published in December 2021, the Fed is expected to raise rates three times this year, followed by three more next year and another two in 2024. The first of these hikes is expected at the Fed meeting in March.

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Bobby Majumder
Member
Frost Brown Todd

Majumder believes planned Fed rate increases are likely to be a dampener. “These rate increases are likely to cause FIIs [foreign institutional investors] to shift assets from riskier markets such as India in favour of higher yields at home,” he says, adding there is “the risk that the less than stellar performance of some of the unicorn IPOs such as Paytm will dampen the appetite of India retail investors to participate in new issues”.

Gupta also reckons the planned Fed rate hike “will definitely have an impact on the liquidity for the equity markets and, therefore, valuations”. He believes that although volumes may be slightly tempered in 2022, “quality issuers accessing equity markets at rational valuations will continue to do well”.

This sets the context for two themes that could draw retail investor interest this year: (1) the unicorn space – unlisted companies valued above USD1 billion; and (2) Life Insurance Corporation (LIC), the behemoth public sector insurer.

Analysts who spoke to *India Business Law Journal* believe unicorns have come of age, and in India have acquired oodles of mindshare among millennials on account of their sky-high valuations. No doubt this mindshare played a role in Paytm raising USD2.5 billion last year, which was an all-time high for an Indian IPO. Its stock, though, plunged 27% on listing day, and retail investors who parted with INR2,150 per share are still under water. But other unicorns that listed successfully last year – like Zomato (up 65.8%), Nykaa (up 89%) and Policybazaar (up 23%) – ensure the theme remains in play.

As of February 2022, there are 59 India-based unicorns in the database maintained by market intelligence company CB Insights, with the highest valued being online education firm BYJU’S, at USD21 billion.

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Amit Singh
Partner and Head of South and Southeast Asia Capital Markets
Linklaters

Amit Singh, a Singapore-based partner and head of South and Southeast Asia capital markets at Linklaters, is bullish on unicorns. "There are a large number of tech companies coming of age in India that likely will have valuations attractive to international investors," he says. "As a result, we expect the tech sector is likely to lead in IPOs, particularly for unicorn issuers. Singh notes that unicorns like Delhivery and PharmEasy have already filed with the Securities and Exchange Board of India (SEBI) for IPOs.

Sivaramakrishnan has a more nuanced view, hinting unicorns are more of an institutional than retail play. In his view, institutional investors fund unicorn IPOs since they understand the risks. "The cost of adding customers in digital is nil, or minimal," he says, "so the scalability is potentially very large with relatively low costs." This explains why investors fund loss-making businesses in digital, he reasons – institutions make multiple digital bets because they only need one or two to pay off. Much is riding on market expectations that LIC's mega listing, anticipated this financial year, will smash all Indian IPO records.

LIC has 66% market share in new business premiums, with 283 million policies and 1.35 million agents as of 31 March 2021. As per the draft red herring prospectus (DRHP) filed with the SEBI, the government proposes to sell 5% of its LIC equity through an offer for sale (OFS). With the DRHP estimating the value of LIC at INR5.39 trillion, the market could value it at INR15 trillion. Although the DRHP has not mentioned the issue size, it's estimated that a 5% equity sale could fetch the government up to INR750 billion.

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Siddhartha Sivaramakrishnan
Partner
McDermott

But there is more to the LIC listing theme than just valuation. S&R's Juhi Singh says a successful LIC listing could have a bearing on deepening the equity market. "Not only will the LIC listing boost the size of the overall market, it will also increase the depth of the investor base," she says. "The proposed reservation for policyholders, coupled with the surge in the number of demat account holders, will increase retail participation and interest. This will, in turn, instil confidence in issuers wanting to tap public money."

The DRHP has proposed that up to 10% of the issue size may be set aside for LIC's policyholders. "You may have noticed that, ahead of the proposed IPO, LIC has initiated an awareness campaign for retail investors and policyholders to ensure their participation in large numbers," says Juhi Singh. "Both LIC and the government are taking this very seriously."

The LIC newspaper ads bear the title: "It's best in life to be prepared". A public notice issued by the company has asked policyholders to update their PAN (permanent account number) in LIC records to "participate in any such public offering".

SEBI TO BAT FOR RETAILERS

The SEBI's recent tightening of IPO norms has been welcomed by corporate lawyers as a sign of the maturing of the domestic market. No doubt the SEBI considered retail investor concerns after thousands burned their hands at the Paytm counter.

According to Amit Singh: "The tightening of the IPO rules was inevitable for a growing and maturing market like India, and examples like Paytm emerge in any country that undergoes a boom like this." He expects market participants to quickly adapt to the changing regulatory landscape, and believes the "changes in rules will not be an obstacle to a continued boom in IPOs".

The new rules for offer of sales (OFS) put curbs on complete exits, post-IPO, by large shareholders. The SEBI has also extended the lock-in period for anchor investors and clamped brakes on the use of IPO proceeds for acquisitions. In another move, it prescribed a minimum price band of 5% between the floor price and the upper price band.

Welcoming the changes, Majumder says they should cool some of the more speculative issues coming to market. "The OFS rule revisions and the price band revisions in particular will dissuade some companies from coming public early, and ensure that IPOs are priced more realistically."

Gupta notes that "the new rules primarily impact technology/internet companies, which are loss-making at the IPO stage".

ESG push expands investor agenda

Environmental, social and governance investors are shaping debt markets, including for Indian issuers

Last year also saw a record USD22 billion being raised from overseas bonds by Indian corporates, easily beating the previous best of USD18.5 billion in 2019. Easy liquidity and low interest rates are factors powering the new record.

It is tempting to look at this year's bond market prospects purely from the perspective of issuers, but Ranajoy Basu, a London-based partner at McDermott, notes the tectonic shifts taking place in the cross-border debt market to address investor concerns.

Basu says environmental, social and governance (ESG) and impact investing are redrawing the debt market landscape using non-financial frameworks.

In his view, the key message being delivered by shareholders and stakeholders to CEOs is that they want to see ESG forming a part of a company's corporate strategy. "There are clear measures and milestones being put in place for companies to come out with programmes to become ESG-compliant," says Basu, and this applies to India as well.

"We have actually seen instances where, without a mid-term strategy, share prices start getting impacted. So it's a unique time that we are operating in, where companies must look at ESG in a very serious way."

Basu says the trend is to either completely change the way the business is being run, or to alternatively identify parts of the company that are most easily transitioned. ESG-compliant pieces of a company are then strategically divested.

"There is a unique community of impact investors, or ESG investors who want to invest in parts of companies that are considered fully ESG-compliant," he explains, noting it is difficult to do so if the parent company is run in a certain way over decades. Hence the divestment.

According to Basu, the investor push on ESG is such that even an oil supermajor like Shell has announced measures to turn net-zero positive in the next 10 years. "At the moment, we're doing a really big project with the fashion industry," he says.

"There is a huge movement in the fashion industry to turn their businesses into ethical fashion."

Regardless of whether they are cut from retail or institutional cloth, investors look determined to set trends this year.