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NEW-AGE IPOS, HERE COMES THE REGULATOR

Relevant for: Indian Economy | Topic: Issues relating to Growth & Development - Capital Market & SEBI

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What are the key changes proposed?

Companies must state if they plan to use the money for acquisitions. They do not need to name the target but must reveal the intent, portion of IPO proceeds likely to be used, nature of business of the target, and the timeline of the acquisition. Currently, firms can set up to 25% of the fresh issue size under general corporate purpose (GCP)—a portion for which no specific objective is stated. Sebi plans a cap of up to 35% of the fresh issue for acquisitions and GCP combined, if the acquisition is unidentified in the objects of the offer. Sebi may also tighten the conditions for offer for sale, and increase lock-in period for anchor investors.

Why is there a need for the new rules?

The current fiscal year has witnessed a rush of public share sales, mostly by startups which are loss-making and engaged in unconventional technology-driven businesses, making it difficult for common public investors to understand how the companies use the money to generate revenues. Even though most of these IPOs by such new-age firms got vastly oversubscribed, public investors may be inadvertently taking too much risk by putting in their money merely on the basis of their popularity. Sebi's latest proposals, once they are implemented, will reduce such risks.

What does it mean for common investors?

Investors will know how their money will be used. This is critical, especially in case of startup listings, because new-age businesses are based on modern, uniquely structured concepts, making it tough for a majority of investors to fathom the risks. That's why Sebi wants firms to elaborate on the object of the issue if the primary object of the IPO is to make future acquisitions.

Will it bring more accountability?

Yes. Existing investors and promoters are currently allowed to monetize their stakes through offer for sale. However, at least 20% of the promoters' stake is locked in for 18 months post-listing to enhance investor confidence. Sebi now wants to cap the amount of stake sale by significant shareholders (those holding more than 20%) at 50%. The balance 50% will be locked in for six months. Further, at least 50% of the anchor book will be allotted for investors who agree to a 90-day lock-in after listing.

What will it mean for those planning IPOs?

Startups will need to be more transparent and make investors better-informed about the nature of their business and future plans. Currently, companies do not need to reveal explicitly how 25% of IPO proceeds will be used, and hence, they are free to use this amount by putting it under GCP, which is not monitored. Some of the recent IPOs are so large that the GCP amount becomes substantial. Sebi now wants even the GCP to be monitored. The use of GCP amount may need to be disclosed in a quarterly report.

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