The Indian IPO Market in Early 2008

This case was written by Sachin Govind and Barnali Chakraborty, under the direction of S.S.George, IBS Center for Management Research. It was compiled from published sources, and is intended to be used as a basis for class discussion rather than to illustrate either effective or ineffective handling of a management situation.
The Indian IPO Market in Early 2008

“The IPO market is important from the economic perspective; it gives opportunity for companies to raise resources and acts a channel for investors to invest in such companies.”

- Devandra Nevgi, CEO and CIO of Quantum Asset Management Company Private Ltd, in February 2008

“Sentiment is a common thread between primary and secondary markets. Aggressively priced IPOs and those with massive oversubscription, without full financing, can signal that perhaps the market is getting too hot, as they did most recently.”

- Pankaj Vaish, MD and Head of Equities and Fixed Income Liquid Markets at Lehman Brothers in Mumbai, in February 2008

“The Indian corporate sector is strong and buoyant. The Indian market alone can give a 20-22% return on equity. Things are bound to improve, the question is: How soon?”

- Ramdev Agrawal, Director of Motilal Oswal, in January 2008

INTRODUCTION

In the first half of February 2008, Wockhardt Hospitals Ltd. (Wockhardt), Emaar MGF Land Ltd. (Emaar MGF), and SVEC Constructions (SVEC) withdrew their Initial Public Offerings (IPOs) owing to poor investor response. Some analysts were of the opinion that overpricing was the main reason for their withdrawal, while others felt that the turmoil in the global financial markets had played a larger role. Still others were of the view that the IPO of Reliance Power Ltd. (RPL), part of the Reliance Anil Dhirubhai Ambani Group (ADAG), which opened on January 15, 2008, was.

2 Quantum Asset Management Company is one of India’s first equity research companies. (Source: http://www.qasl.com)
4 Lehman Brothers, founded in 1850 and headquartered in New York, is a leading firm in equity and fixed income sales, trading and research, investment banking, private investment management, asset management, and private equity. (Source: http://www.lehman.com)
6 Motilal Oswal Securities is a leading research and advisory based stock broking house of India (Source: http://www.motilaloswal.com)
7 Wockhardt Hospitals is part of Wockhardt, a leading pharmaceutical and biotechnology company in India. As of early 2008, the company operated 12 hospitals at Mumbai, Hyderabad, Nagpur, Surat, Rajkot, Bengaluru, and Kolkata.
8 Emaar MGF Land Limited is a joint venture between Emaar Properties PJSC (Emaar) of Dubai and MGF Development Limited (MGF) of India. Emaar is one of the world’s leading real estate companies and MGF is one of the key players in retail real estate development in Northern India. The company started its operations in India in February 2005. (Source: www.emaarmgf.com)
9 SVEC Constructions, which was founded in 1985, is a leading construction company in India. (Source: http://www.svec.in/aboutus.htm)
10 The Reliance Anil Dhirubhai Ambani Group is a group of companies headed by Anil Ambani. The Group companies include Reliance Capital, Reliance Communications Limited, Reliance Energy Limited, Reliance Health, and Reliance Media and Entertainment. (Source: http://www.relianceadagroup.com)
responsible for the tepid response to these three IPOs, as the RPL IPO had sucked out liquidity from the market. The RPL IPO was oversubscribed by 73 times and collected a record Rs. 7,448 billion ($1190 billion) from the market. However, although the RPL IPO was oversubscribed, it listed below its offer price on the stock exchange, causing many analysts to believe that the Indian IPO market was losing steam. But when the IPO of the Rural Electrification Corporation Ltd. (REC) was fully subscribed, reportedly within 27 minutes of its opening, it appeared as though their views had been incorrect.

With choppy global markets, and the Indian stock market seesawing, analysts were of the opinion that the Indian IPO market too would be affected. However, others were not too worried about the global factors as they felt that the success of the IPO market was more a function of domestic growth. The proposal of the Finance Ministry of the Indian government to pass legislation to increase the minimum public holding in all listed companies to 25 percent from the existing 10 percent, was expected to lead to a large number of companies coming up with public offerings in the coming months, possibly bringing buoyancy back to the primary market.

BACKGROUND NOTE

The Indian primary market started picking up momentum in the 1980s, when a large number of companies came up with their IPOs (Refer Exhibit I for a note on IPOs). The modern securities market in India was the result of the capital market reform in 1991. In 1992, the Securities and Exchange Board of India (SEBI) was established. In the early 1990s, many companies came up with public issues, and met with good response from investors. However, the security scam of 1992 severely affected the primary market.

In 1995, Indian companies were able to mobilize around Rs 3 billion through the IPO route. In the late 1990s, the Indian business sector was in the middle of a transformation. While the returns on ‘old-economy’ company stocks were not very impressive, stocks of software companies did well.

In 1999-2000, approximately Rs 45 billion in the form of equity was raised in the primary market. During 1999-2000, the policies adopted by the SEBI helped further the development of the securities market in India. To encourage participation of companies in the Information Technology (IT) sector, the SEBI relaxed the ‘entry point norms.’ This allowed companies to “make public offer of 10 percent of post issue capital instead of 25 percent for other sectors,” subject to requirements of a minimum number of 2 million securities and a minimum net offer value of

11 ‘$’ refers to the US dollar in this case study.
13 Rural Electrification Corporation Ltd. (REC) was a wholly-owned Government Company under the Ministry of Power, Government of India till March 12, 2008, when the company listed on the Bombay Stock Exchange. The GoI’s share in the company came down to 81.82 percent post issue. (Source: http://recindia.nic.in)
15 The primary market is part of the financial market where enterprises issue their new shares and bonds. In primary markets, securities are bought by way of public issue directly from the company. In secondary market, shares are traded between two investors. (Source: www.sharemarketbasics.com)
16 The securities scam of 1992 involved the diversion of funds (especially the funds in the inter-bank market for government securities) to brokers for financing their operations in the stock markets. The scam was carried out by brokers with the help of top executives of some of the large nationalized banks, foreign banks, and other financial institutions. It resulted in misappropriation of funds of around Rs 35 billion and threw the money market as well as the stock market into disarray. (Source: Anuj Thakur, “Anatomy of Securities Scam,” iimcal.ac.in)
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Rs.300 million.\(^{18}\) The Credit Rating Agencies (CRAs) were brought under regulation. The SEBI also permitted the use of infrastructure of stock exchanges for marketing IPOs in an effort to “reduce issue and distribution costs for public issues, reduce delays, and speed up allotment.”\(^{19}\)

In 2000, the Indian IPO market mobilized over Rs. 21 billion. However, in 2001, it saw a steep decline in both the number of IPOs as well as the total amount of funds mobilized; only around 15 companies came out with their IPOs and the resources mobilized were only around Rs. 3 billion.

The primary market again gained momentum in 2003. The public issue of Maruti Udyog Ltd.’s stock was successful in attracting retail investor interest.

In 2004, the primary market in India saw several companies from industries like oil and gas, telecom, power, chemicals, banking, technology, finance, and infrastructure coming up with public issues.

In 2006-07, there were 77 IPOs, mobilizing around Rs. 285 billion. The average size of the public issues increased from Rs. 2.26 billion in 2005-06 to Rs. 3.51 billion in 2006-07.

In 2007, with the Indian IPO market raising Rs. 327 billion ($8.3 billion) from 90 issues, India ranked ninth\(^{20}\) in the size of its primary market (Refer Exhibit II for a list of the countries ranked according to capital raised from the primary market).

A SPATE OF WITHDRAWALS

In the first week of January 2008, RPL announced that it would offer 260 million equity shares (including the promoters’ share of 32 million shares) to the public. According to the company’s statement, the IPO was to be priced between Rs 405 and 450 and would raise between Rs 92.34 billion and Rs 102.6 billion.

After RPL’s IPO opened on January 15, 2008, there was a rush in the market to apply for the issue. “It has created an unprecedented euphoria in the market. The issue would be a good option for retail investors who are looking for short term gains,” said Rajesh Jain, Vice President of SMC Global\(^{21}\). The issue which was open for subscription from January 15, 2008, to January 18, 2008, was oversubscribed immediately after its opening. It was eventually oversubscribed by 73 times.

The issue received an extremely favorable response from High Net-worth Individuals\(^{23}\) (HNIs) and retail investors as it had an option of part payment\(^{24}\). Investors had to only pay 25 percent of the amount at the time of applying for the IPO, with the remaining amount to be paid on allotment. Institutional buyers were required to pay only 10 percent of the total amount. While institutional investors had this option\(^{25}\) in the case of all issues, only some companies offered the option of part payment to retail investors.

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\(^{18}\) “Policies and Programmes,” www.sebi.gov.in.

\(^{19}\) “Policies and Programmes,” www.sebi.gov.in.


\(^{21}\) SMC Global was founded in 1990. It is one of the largest investment solutions companies and provides a wide range of services to its customers. (Source: http://www.smcindiaonline.com)

\(^{22}\) “Reliance Power IPO Subscribed 10 times in 4 Hrs,” wwwwinhome.rediff.com, January 15, 2008.

\(^{23}\) HNI (or HNWIs) are individuals with a high net worth. Typically, in India, these are individuals with assets (excluding their primary residence and consumables) in excess of US$ 1 million. As of 2006, there were an estimated 100,000 HNIs in India.

\(^{24}\) Part payment option allows investors to apply for a higher number of shares than their existing cash balance will permit them to. Another advantage is that as the total amount is not required to be paid upfront, only a fraction of the investment is blocked before the allotment of shares. And if the issue is oversubscribed and the investor is allotted fewer shares than he/she applied for, then he/she may not have to pay the remaining amount.

\(^{25}\) Institutional investors get this leeway due to the quantum of funds that they commit. Besides, the chances of their not meeting their commitments are slim.
The IPO of RPL turned out to be India's largest. Commenting on the investor response, P Chidambaram (Chidambaram), Finance Minister of India, said, “...Investors seem to be confident in the future of [the] Indian economy.”

On January 21, 2008, now known as Black Monday, the Indian stock markets, including the Bombay Stock Exchange and the National Stock Exchange, plunged, leaving thousands of investors jittery (Refer Exhibit III for the BSE Sensex between May 2007 and May 2008). The volatility in world markets was seen as the main reason for the crash.

On January 31, 2008, the Wockhardt Hospitals IPO opened, followed by Emaar MGF on February 01, 2008, and SVEC on February 04, 2008. However, poor investor response forced the companies to first lower the price bands of their offerings and to extend the last dates for subscription. With these measures failing to improve the situation, the companies decided to call off the IPOs (Refer Exhibit IV to know more about these IPOs).

On February 7, 2008, Wockhardt Hospitals withdrew its IPO. At the time of withdrawal, the Wockhardt IPO was subscribed by only 0.20 times and it became the first IPO since July 2006 to fail. According to a company statement, “The decision not to proceed with the IPO was made in light of continued global and domestic market volatility and poor market sentiments and the resultant effect on the subscription levels in the IPO.”

The next day, Emaar MGF also withdrew its IPO. According to a company statement, “The decision has been taken due to prevailing adverse market condition...although the QIB and HNI portions of the IPO were fully subscribed and the overall book was closed to 90 percent. Given the prevailing sentiments in the capital markets, it was unclear how well the stock would trade post-listing. It has been considered wiser to revisit the market only when the demand and sentiment are stable...” Afterwards, Shrvan Gupta, Executive Vice Chairman and Managing Director of Emaar MGF Land, said, “Negative sentiment for IPO market is a major cause for this withdrawal. We may consider listing after three-six months once markets stabilize.

While the RPL IPO was oversubscribed many times over, the stock found few takers when it was listed on February 11, 2008. Although the RPL shares opened at a higher price than the offer price of Rs 450, by the time the stock market closed for the day, the price of the share had dropped to Rs 389. “The listing has come as a big surprise. Nobody expected a listing below the issue price at least [sic]. People were looking to sell at listing gains, and because of the overall sentiment, there are very few buyers now,” said Deven Choksey, managing director at K.R. Securities (Refer Exhibit V for the listed IPOs in early 2008).

WHAT WENT WRONG?

Several explanations were offered as to why the three IPOs failed in quick succession. A survey conducted by ASSOCHAM in early 2008 concluded that overpricing of the issues and investor’s

26 “Reliance Power IPO Subscribed 10 times in 4 Hrs,” wwwwinhome.rediff.com, January 15, 2008
28 In India, Qualified Institutional Buyers (QIBs) include public financial institutions, scheduled commercial banks, mutual funds, FIs registered with SEBI, venture capital funds, foreign venture capital investors, state industrial development corporations, insurance companies, provident funds, and pension funds. These entities are regarded as QIBs and are not required to specifically register with SEBI as QIBs.
33 The Associated Chambers of Commerce and Industry of India (ASSOCHAM) was established in 1920 by promoter chambers representing all regions of India. It has a membership of over 100,000 companies and professionals across the country. (Source: www.assocham.org)
risk averseness due to weak global cues were the main reasons for the failure of the IPOs. The report said, “While Indian stock markets have become structurally strong and well-regulated, bad pricing of issues and weak market sentiment have played spoilsport.”

Many analysts agreed with the survey’s findings. According to Stuart Smythe, Executive Director and Head of Equities, Macquarie Securities India, “Realization is dawning on many investors that IPO valuations may be on the high side. They are becoming rational now and their risk appetite has been moved by recent global market weakness.”

Analysts felt that companies coming out with IPOs in the future would do well to price their offerings appropriately. According to V.N. Dhoot (Dhoot), President of ASSOCHAM, “While prevailing liquidity conditions in bourses play an important role in the successful listing of a company’s stock, valuations should not stretch into long future as it dampens investors’ appetite.”

According to some analysts, the main reason for the poor investor response in the Indian IPO market in early 2008 was that Foreign Institutional Investors (FIIs), a significant and growing influence in the Indian stock market, were not showing much interest (In fact, they were busy selling off their holdings in the Indian market so as to make up for the subprime losses incurred in the US.). The number of IPO withdrawals grew in other markets, too. According to Thomson Financial, in January 2008, 21 global IPOs were withdrawn compared to 16 in December 2007.

However, according to the finance minister, the financial turmoil in the US should not affect investor sentiment in India. Chidambaram said, “There is no reason to allow the worries of the western world to overwhelm us. Our economy is very different from the economies of some developed countries which are facing some stress. Our economy is a strong economy, our corporate sector is very strong. If the economy will grow this year at 8.9% and is expected to grow at 8.5% next year, the market sentiment should be a very positive sentiment.”

Some analysts felt that a few IPO failures did not amount to much. “There are enough number of large IPOs lined up that can change the dynamics of the Indian market. Economic percentage growth decides the number of IPOs to hit the capital market, and in our case, all augurs well,” said Prashanth Prabhakaran, Senior Vice-President of Kotak Securities.

The spate of withdrawals, however, threw up some important questions on the IPO issue process and the responsibilities of the market participants. For example, market experts questioned the role and responsibilities of investment bankers, saying that they had not been thorough in their analysis

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35 Macquarie Securities Group is a major financial services company with presence in 25 countries. In India, the company provides specialist investment, advisory and financial services. It has memberships of the National Stock Exchange and Bombay Stock Exchange.
39 Thomson Financial’s one of the world’s leading information companies. (Source: www.thomson.com)
41 Kotak Securities, a subsidiary of Kotak Mahindra Bank, is the stock-brokering and distribution arm of the Kotak Mahindra Group. (Source: http://institutional.kotaksecurities.com)
and assessment of companies. “Merchant bankers should be penalised if an IPO is withdrawn, as they are responsible for the valuation,” said Vinod K Sharma, Director and Head of Research at Anagram Securities.  

Analysts were also concerned that investors were giving more importance to the gray market price of an IPO (Refer Exhibit VI for more information on the gray market for IPOs in India) than to the fundamentals of the company in question, its future prospects, or the issue size, while deciding whether or not to subscribe to the IPO. If the gray market had a premium on the IPO, the investors generally believed that the company’s shares would list at a higher price than its offer price. “The IPO gray market is becoming more and more influential with respect to decision making for the smaller investors who look at the premium prevailing in such markets before taking a final call to participate in the official book building process,” said a broker.  

Some experts were of the opinion that SEBI should exercise more control over the pricing of primary market issues. They felt that as the capital market regulator, it was its responsibility to check the overpricing of primary market issues and to ensure that gray market activity did not affect the price of an IPO.  

LOOKING AHEAD  

In early February 2008, the Indian Finance Ministry proposed to increase the minimum public holding in all listed companies to 25 percent from the existing 10 percent, in order to reduce the scope for price manipulation and to introduce more public participation in the stock market. According to an ASSOCHAM Eco Pulse study, only two companies -- Bajaj Auto and Larsen and Toubro (L&T) -- satisfied the proposed criteria of minimum “public” shareholding and this was expected to result in a large number of IPOs in the coming months. “Implementation of the proposed changes in the Act will lead to a huge flow of IPOs and follow-on offers by a large number of companies into the primary markets,” said Dhoot (Refer Exhibit VII for the top ten listed companies in the private and public sectors in India with 25 percent or less public shareholding).

Although some analysts welcomed this proposal, they were concerned that the term ‘public,’ as proposed by the Finance Ministry, included FIIs, who were seen as being responsible for the recent fall in stock prices. “The move is welcome. It will introduce more shares for trading in the open market. Moreover, if the word ‘public’ is [better] defined, it will reduce the scope for monopolizing of shares by FIIs,” said Pavan Duggal, Supreme Court lawyer.

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43 Anagram Securities Ltd. is the stock broking arm of Lalbhai Group.
44 Sanat Vallikappen, “DLF’s PE is 74. Emaar was priced at 165,” www.dnaindia.com, February 9, 2008.
46 Bajaj Auto, the flagship company of the Bajaj Group, is one of the largest two- and three-wheeler manufacturers in the world. It has a public shareholding of 27.7 percent. (Source: http://www.bajajauto.com)
47 Larsen & Toubro Limited (L&T) is India’s largest engineering and construction company. The company is also involved in electricals, electronics, and IT services. It has a public shareholding of 35.5 percent. (Source: http://www.lntecc.com)
48 According to the Finance Ministry, ‘public’ could mean ‘non-promoters’ including financial institutions, foreign institutional investors, mutual funds, employees, NRIs/OCBs, private corporate bodies, etc. As there were several views on what the word public should include, the Ministry suggested that there be a discussion on it (Source: “Ministry Proposes 25% Public Holding Floor,” http://business-standard.com, February 2, 2008).
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In the wake of the controversy relating to pricing of IPOs, the government also directed the Institute of Chartered Accountants of India (ICAI)\(^{51}\) to conduct a study on the subject. “The government has asked the ICAI to study the issue of IPO valuation and system of stock movements. The ICAI will submit a report on the valuation of IPO in due course. The ICAI study would take into account the practice followed in other countries as well as India and suggest ways for dealing with it,” said Prem Chand Gupta, Corporate Affairs\(^{52}\) Minister.\(^{53}\)

In mid-2007, the SEBI had appointed a committee, the Group on Review of Issue Process (GRIP), to study the IPO process and come up with recommendations to make it more efficient. The report recommended that the SEBI require companies to use an ‘indicative price’ for price discovery rather than the price band and to increase the percentage of the deposited bid amount from 10 percent to 100 percent for qualified institutional buyers (QIBs). Analysts were of the opinion that if QIBs were required to deposit the full bid amount, then they would be more diligent in assessing the value of an issue and also limit the number of shares that they applied for. They would also subscribe to fewer companies than before, which would reduce speculation. Another recommendation was to reduce the period between the close of an issue and its listing to 7 days from 21 days, so as to curtail gray market activity.\(^{54}\)

The committee also recommended that companies be allowed to file their draft offer with the SEBI even before they were given the authority to issue capital. Another recommendation was that retail investors be allowed to apply for shares worth a maximum of Rs 200,000, opposed to a maximum of Rs 100,000 now.

As of March 2008, the Indian stock markets remained in the doldrums, with investors staying away. Therefore, some companies decided to postpone their IPO plans. “We are dropping plans of an IPO for Infotech\(^{55}\) in 2008 because the markets are volatile. If we go now for an IPO, we won’t get better valuation,” said A M Naik, Chairman and MD of L&T.\(^{56}\)

However, other companies were not so pessimistic. Despite RPL shares listing below offer price, ADAG announced that it would proceed with its plan of IPO for its telecom towers unit, Reliance Infratel of Reliance Communication.\(^{57}\) The company expected to raise Rs. 40-60 billion ($ 1-1.5 billion) from the IPO. To compensate RPL investors for their loss due to the shares listing below the price they had paid, on February 25, 2008, RPL announced that it would issue three bonus shares for every five shares held. According to newspaper reports, Anil Dhirubhai Ambani (Ambani), Chairman of Reliance ADAG, diluted his personal holding in Reliance Power by 5%, to 40% with the issue of the bonus shares. “We’ve seen very turbulent conditions in the global and Indian capital markets. The Reliance Power IPO closed at a time when the market was close to an all-time high. But clearly, since then there has been turbulence in the markets. After considering

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\(^{51}\) The Institute of Chartered Accountants of India (ICAI) is a statutory body established under the Chartered Accountants Act, 1949, for the regulation of the profession of Chartered Accountants in India. (Source: http://www.icai.org)

\(^{52}\) The Corporate Affairs Ministry is concerned with the administration of the Companies Act, 1956, the Partnership Act, 1932, and the Competition Act, 2002. It also supervises the functioning of professional bodies namely, the Institute of Chartered Accountants of India, the Institute of Cost and Works Accountants of India, and the Institute of Company Secretaries of India.


\(^{55}\) L&T Infotech, a subsidiary of L&T Ltd, is a global IT services and solutions provider. (Source: http://www.lintinfotech.com)


\(^{57}\) Reliance Communications, a telecommunications company, is the flagship company of the Anil Dhirubhai Ambani Group (ADAG) of companies.
these adverse changes, we have decided on a bonus issue to protect the interests of long-term investors,” said Ambani.  

Air India was also expected to go ahead with its IPO in the second half of 2008. The Indian government was expected to sell up to a 15 percent stake in Air India. Praful Patel, the Civil Aviation Minister said, “The government was keen to list Air India and raise funds for expansion of the company, so we may consider issuing an IPO in the second half of this year.” The government was expected to raise between Rs 2.5 billion and Rs 4.0 billion from the issue. Future Ventures, a Future Group Company, also planned to raise around Rs. 37.3 billion.

The REC IPO, with a price band of Rs. 90 to Rs. 105 per share, opened on February 19, 2008, and closed on February 22, 2008. The issue was oversubscribed 27.30 times. “At a time when secondary markets globally are witnessing a sharp correction and there is an acute liquidity crunch, companies are over-pricing their public issues. People are wondering if this is the right time to hit the primary markets. However, if an issue is rationally priced, any time is a good time. We have seen good issues doing well during this time. Rural Electrification Corporation's public offer is a case in point,” said Sanjeev Khandelwal, Director of Prime Database. On March 12, 2008, the REC share closed the day at Rs.121.20, gaining 15.5 percent on the issue price.

According to newspaper reports in May 2008, India was the second worst-hit market in the world on the basis of deferment or shelving of IPOs. IPOs amounting to around 240 billion ($ 5.98 billion) were deferred or withdrawn in the first five months of 2008. However, there were some big issues such as those of Reliance Infratel, Jaiprakash Power Venture Ltd, JSW Energy, OIL India, and National Hydroelectric Power Corporation planned in the latter half of 2008.

Most analysts also believed that the slowdown in the IPO market was temporary. According to Atul Mehra, MD & Co-CEO of JM Financial Consultants, “We believe 2008 will continue to be the year of mega IPOs. The primary market is not just alive, but there is much steam left. 2008 may go on to become the biggest primary market year.”

59 Air India is the only state-owned airline in India.
60 Gaurav Mehra, “Air India IPO to Hit the Market in Second Half of This Year: Praful Patel,” www.topnews.in, January 14, 2008.
63 Prime Database was started by Prithvi Haldea in 1989. It is a database of comprehensive information on the primary capital market. (Source: http://www.primedatabase.com)
65 JM Financial Consultants is a wholly owned subsidiary of JM Financial Ltd., a listed company. JMFC provides private wealth management, portfolio management, and investment advisory services to its clients.
Exhibit I
A Brief Note on IPOs in India

An Initial Public Offer (IPO) is the sale of stock of a company to the public in the primary market. A company comes out with an IPO to collect capital for its future expansion. Before an IPO, a company generally takes the help of underwriting firms (investment banks), which help it to determine the number of shares to be offered, the offer price, and the timing of the issue. Underwriting firms are responsible for selling the shares of the company to the public and usually get a commission based on the value of shares sold. Currently, underwriting is optional with most bankers preferring soft underwriting, meaning the underwriter agrees to buy shares at later stages of the IPO i.e. after the pricing.

The underwriters apply to the governing body of the financial market and in a registration statement, known as ‘red herring prospectus,’ provide information about the offering (barring the offer price and offer date) as well as on the company such as financial statements, the background of the management, etc. The red herring prospectus also mentions the grading of the IPO. An IPO’s grade is assigned by a Credit Rating Agency (CRA) registered with the governing body of the financial market. The CRA assigns grades to IPOs on a five-point scale, with a higher score indicating stronger fundamentals. Obtaining IPO grading is mandatory and the company is required to bear the expenses associated with grading. A company cannot reject the grading of its IPO and the grade has to be disclosed in the red herring prospectus. In India, IPO grading is provided by rating agencies approved by the Security and Exchange Board of India (SEBI) such as CRISIL, CARE, ICRA, and FITCH.

After the governing body investigates and gives its approval, the offer date and the ‘price band’ of the IPO are announced. The lower price limit in the price band is referred to as the ‘floor’, and the upper price limit is referred to as the ‘cap.’ Each investor specifies the number of shares he/she wants and the price (within the price band) he/she will pay for those shares.

After the closing of an IPO, the bids are allotted to different categories and the rate of subscription in each category is determined. The ‘cut off price,’ the equilibrium price at which the company can sell all the shares on offer, is then determined on the basis of the bids. This process of price discovery is known as book building process.

After the ‘cut off price’ is determined, bidders who bid at or over the ‘cut off price’ are allotted shares, based on the extent to which the IPO has been subscribed. For example, if an investor bids for 200 shares of an issue at the price Rs. 50, then he gets 200 shares at Rs. 10,000 (200 x Rs 50), if the ‘cut off price’ is Rs 50. Now if the cut off price is Rs 40, then the cost for the shareholder is Rs. 8,000 (200 x Rs 40). Then, Rs. 2,000 (Rs. 10,000 - Rs. 8,000) will be refunded to the investor*. If the issue is over-subscribed four times and the cut off price is Rs. 40, then he/she gets 50 shares at Rs 40 which costs Rs. 2,000 (50 x Rs 40). Then Rs. 8,000 (Rs. 10,000- Rs. 2,000) will be refunded to the investor. However, if the rate of oversubscription is very high, then some investors may not get any shares. In some cases, allotments are decided on the basis of a lottery.

Companies are allowed to sell shares at different prices to different class of investors, provided the offer made to the public is lower than what is offered to other investor classes.

* Not applicable to institutional investors as they are not required to deposit the entire amount

Exhibit II

Top IPO Markets in the World

<table>
<thead>
<tr>
<th>S.No</th>
<th>Origin country of companies raising capital</th>
<th>Capital Raised (Q2 2007) in bn $</th>
</tr>
</thead>
<tbody>
<tr>
<td>1</td>
<td>USA</td>
<td>15.7</td>
</tr>
<tr>
<td>2</td>
<td>China</td>
<td>15.5</td>
</tr>
<tr>
<td>3</td>
<td>Russia</td>
<td>11.7</td>
</tr>
<tr>
<td>4</td>
<td>Brazil</td>
<td>5.4</td>
</tr>
<tr>
<td>5</td>
<td>Germany</td>
<td>4.1</td>
</tr>
<tr>
<td>6</td>
<td>UK</td>
<td>3.6</td>
</tr>
<tr>
<td>7</td>
<td>Italy</td>
<td>2.9</td>
</tr>
<tr>
<td>8</td>
<td>Spain</td>
<td>2.5</td>
</tr>
<tr>
<td>9</td>
<td>Saudi Arabia</td>
<td>2.5</td>
</tr>
<tr>
<td>10</td>
<td>India</td>
<td>2.4</td>
</tr>
</tbody>
</table>


Exhibit III

BSE Sensex between May 2007 and May 2008

Source: http://finance.yahoo.com/
### Exhibit IV

#### IPOs Withdrawn in February 2008

<table>
<thead>
<tr>
<th>Company</th>
<th>Issue size</th>
<th>Issue price</th>
<th>Rate of subscription</th>
<th>Other information</th>
</tr>
</thead>
<tbody>
<tr>
<td>Wockhardt Hospitals</td>
<td>Rs 656 crore ($164 million)</td>
<td>Rs 280 – Rs 310 per share. Then reduced to Rs 225 - Rs 260 per share.</td>
<td>6 percent in FII and domestic institutional investor quota, 51 percent in retail investor segment and 5 percent in non retail-non institutional investor segment.</td>
<td>The issue opened on January 31, 2008, and was scheduled to close on February 5, 2008. The company extended the offer period by two days. Then the IPO was withdrawn on the closing date.</td>
</tr>
<tr>
<td>Emaar MGF Land</td>
<td>Rs 6,400 crore ($1.6 billion)</td>
<td>Rs 610-690 per share. Then reduced the price band twice. The last offer price was Rs 530-630.</td>
<td>29 percent in FII and domestic institutional investor category, 47 percent in retail investor category and 78 percent in non retail-non institutional investor category respectively.</td>
<td>The issue opened on February 1, 2008, and was scheduled to close on February 6, 2008. The company extended the offer period to February 11, 2008. The company withdrew its IPO on February 8, 2008.</td>
</tr>
<tr>
<td>SVEC Constructions</td>
<td>Rs 34-38 crore ($8.5-9.5 million)</td>
<td>Rs 85- Rs 95 per share. Then reduced to Rs 80-90.</td>
<td>Subscribed 0.25 times.</td>
<td>The issue opened on February 4, 2008, and was scheduled to close on February 8, 2008. The company extended the offer period to February 13, 2008. Then the IPO was withdrawn on the closing day.</td>
</tr>
</tbody>
</table>

### Exhibit V

**Some IPOs Listed between January 01, 2008 and February 15, 2008**

<table>
<thead>
<tr>
<th>Company</th>
<th>Issue Size (Rs million)</th>
<th>Issue Price (Rs)</th>
<th>Listing Date</th>
<th>Listing Day’s Price (Rs)</th>
<th>Price on February 12, 2008</th>
</tr>
</thead>
<tbody>
<tr>
<td>J. Kumar Infraprojects</td>
<td>720</td>
<td>110</td>
<td>February 12, 2008</td>
<td>100.1</td>
<td>100.1</td>
</tr>
<tr>
<td>Reliance Power</td>
<td>101,230</td>
<td>450</td>
<td>February 11, 2008</td>
<td>416.8</td>
<td>356.1</td>
</tr>
<tr>
<td>Future Capital Holdings</td>
<td>4,900</td>
<td>765</td>
<td>February 1, 2008</td>
<td>882.0</td>
<td>873.8</td>
</tr>
<tr>
<td>Precision Pipes</td>
<td>750</td>
<td>150</td>
<td>January 11, 2008</td>
<td>142.8</td>
<td>80.6</td>
</tr>
<tr>
<td>Manaksia</td>
<td>2,480</td>
<td>160</td>
<td>January 8, 2008</td>
<td>178.9</td>
<td>83.3</td>
</tr>
<tr>
<td>BGR Energy Systems</td>
<td>4,380</td>
<td>480</td>
<td>January 3, 2008</td>
<td>898.8</td>
<td>576.8</td>
</tr>
</tbody>
</table>

The IPO gray market is an unofficial market where the shares and applications of forthcoming IPOs are traded. Two important terms related to the IPO gray market are *kostak* and premium.

*Kostak* is the premium amount in rupees at which unlisted shares of a company are traded in the gray market. For example, unlisted shares worth Rs. 100,000 (calculated on the basis of the cap of the price band) of a company may command a *kostak* of between Rs 2500 and Rs 2700. *Kostak* is settled on the day of allotment of shares and the seller will get the premium irrespective of whether he/she is allotted any shares or not. In this way, an IPO investor can avoid the risk of shares not being allotted. The buyer (if he/she is a speculator) expects the share to list above its offer price and to make a profit by selling the shares on the listing day. The difference between the selling price of the total allocated shares and *kostak* is the profit of the buyer.

While the gray market premium is also the premium amount in rupees at which IPO shares are traded in the gray market, it is different from *kostak* on one count -- the risk of under allotment of shares lies with the investor (the person who applies for shares in an IPO). The gray market premium indicates the level of interest in a particular issue. The premium of an IPO share can be positive or negative. For example, if the issue price of an IPO is Rs. 450 and the gray market premium is Rs. 400, then the buyers are ready to buy the shares at Rs 850 (Rs 450+400). In this example, the gray market premium is positive.

As the gray market premium is determined by the forces of supply and demand, like the prices of listed shares, it keeps changing. The demand and supply in the IPO gray market are mainly influenced by the subscription rates and conditions in the secondary market. When secondary markets are buoyant, most shares command a premium in the IPO gray market. Even when the offer price of a company’s shares is perceived to be low, the share quotes at a positive premium in the gray market.

Trades in the gray market are settled on the day of listing. After the investor is allotted the shares, he/she has to give the shares to the gray market buyer at the agreed price (issue price plus premium). The investors of an issue generally do not get all the shares they have bid for. If the investor (seller) gets fewer than the anticipated number of shares, he/she has to buy the remaining shares from the market and deliver the agreed number of shares to the buyer.

Lead managers of IPOs usually consider the gray market premium rate as an indicator of the price band while fixing the price band. Many investors consider the gray market premium before applying for an IPO. However, gray market premiums may change between the time an investor applies for an IPO and the time the issue gets listed.

In India, the most active centers for the IPO gray market are Ahmedabad, Kolkata, and Rajkot.

Exhibit VII

Listed Companies* Having 25% or Less Public Shareholding

<table>
<thead>
<tr>
<th>Private Sector Companies</th>
<th>Public Share Holding (%)</th>
</tr>
</thead>
<tbody>
<tr>
<td>DLF</td>
<td>12</td>
</tr>
<tr>
<td>Mundra Port</td>
<td>19</td>
</tr>
<tr>
<td>Wipro</td>
<td>20</td>
</tr>
<tr>
<td>TCS</td>
<td>22</td>
</tr>
<tr>
<td>Sun TV Network</td>
<td>23</td>
</tr>
<tr>
<td>VSNL</td>
<td>24</td>
</tr>
<tr>
<td>Adani Enterprises</td>
<td>25</td>
</tr>
<tr>
<td>Reliance Petroleum</td>
<td>25</td>
</tr>
<tr>
<td>Unitech</td>
<td>25</td>
</tr>
<tr>
<td>Lanco Infratech</td>
<td>25</td>
</tr>
</tbody>
</table>

<table>
<thead>
<tr>
<th>Public Sector Companies</th>
<th>Public Share Holding (%)</th>
</tr>
</thead>
<tbody>
<tr>
<td>Hindustan Copper</td>
<td>0</td>
</tr>
<tr>
<td>MMTC</td>
<td>1</td>
</tr>
<tr>
<td>NMDC</td>
<td>2</td>
</tr>
<tr>
<td>Neyveli Lignite</td>
<td>6</td>
</tr>
<tr>
<td>NTPC</td>
<td>10</td>
</tr>
<tr>
<td>Power Finance Corporation</td>
<td>10</td>
</tr>
<tr>
<td>National Aluminum</td>
<td>13</td>
</tr>
<tr>
<td>Power Grid Corporation</td>
<td>14</td>
</tr>
<tr>
<td>SAIL</td>
<td>14</td>
</tr>
<tr>
<td>IOC</td>
<td>20</td>
</tr>
</tbody>
</table>

* the list is not exhaustive

The Indian IPO Market in Early 2008

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The Indian IPO Market in Early 2008


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