Our Views

Direct Listing outside India of Indian Unicorns and Start-ups – Complex issues to solve for!

For a long time, listing of corporates outside India without being listed in India has been a much required ask of Indian Unicorns as well as Startups. And clearly there is merit in this demand – access to a deeper pool of capital abroad, diversification of investor base, significantly better valuation for some sectors and greater flexibility. As per our present legal framework, an Indian company should first be listed in India, before considering an overseas listing by way of ADRs or GDRs (DRs).

Action on allowing such overseas listing was promised by the Finance Minister as a part of the Atmanirbhar Bharat agenda and was quickly followed up by the Government by making an enabling provision in the Companies Act. The provision facilitates the formation of guidelines for such a listing transaction. Earlier, in June 2018, SEBI had also constituted an Expert Committee to examine the various legal, operational, and regulatory constraints in facilitating Indian companies to directly list their equity shares on foreign stock exchanges. The recommendations of the Committee were submitted in December 2018.

On a comprehensive analysis of this requirement, I believe there are quite a few matters to be ironed out before it becomes a reality. There are some very complex issues relating to FEMA, permitted countries for listing, anti-money laundering, KYC and taxation that need to be resolved. For example, under the present Indian tax laws, income earned from transfer of equity shares of an unlisted Indian company listed on a foreign stock exchange would be subject to capital gains tax in India, as these shares would be considered 'capital assets situated in India' because these are shares of a company incorporated in India. Foreign investors trading in DRs which represent shares of Indian companies do not have to pay capital gains tax in India on their profits as they are derivative instruments.

While I am sure that the above issues are being duly considered and evaluated by the various regulators, I see one potential solution to address these concerns. A hybrid model combining the current framework and a new set of guidelines could be an alternative to resolve several current technical challenges. As per the existing regulatory framework, an Indian listed company can do a DR program in the overseas markets. However, this does not enable a true price discovery in the international as the pricing of a DR is generally based on the price of the underlying listed and traded shares in India.

To facilitate an appropriate price discovery for the issuer, regulators should ideally consider a modification in the existing DR guideline whereby a DR offering can be done by way of an IPO of the unlisted shares. Post the IPO of DRs in the international markets, the underlying shares can then be offered to be listed on Indian stock exchanges – this can be termed as listing without any offering. Of course, to enable subsequent Indian listing, the regulators will have to revisit some of the existing regulations such as minimum public holding, promoter contribution and lock-in requirements. The usual process of listing in India can be followed for the same, including offer document filing, review by the regulators and due diligence. This mechanism will help resolve several technical issues.

A framework for issuance of DR already exists in the country and may not require too many changes to enable an IPO of DRs. As the company will get listed in India subsequently, it will enhance the Indian market cap and positively impact the market dynamics, the Indian investors could benefit through conversion of DRs, and the Indian regulators can continue to have an oversight of the company. And of course, the issuer will achieve its objective of appropriate value discovery in an international market with deeper pool of capital and a diverse set of investors.

Sometimes, it may be better to go with a simple solution for a problem which may otherwise be quite multifaceted and complex. Otherwise, creating a completely new set of framework for listing of shares directly outside India would surely take a long while as we get all ducks in a row across various regulations!

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