Our Views

Primary markets can become as efficient as secondary markets

Our regulators, effectively leveraging technology, are constantly moving towards higher efficiency and improved processes in our secondary trading markets. Now, we have reached to a level of T+0 settlement and are also envisioning instantaneous settlement.

There has been marked improvement in the efficiency of our primary markets as well. SEBI's efforts to explore Artificial Intelligence (AI) for processing offer documents more efficiently in a time bound manner, if successful, will be a considerable step in that direction. Public issuance timelines and post issue activities have already been cut significantly. IPO timelines are down from almost 2 to 3 months post SEBI clearance to just about 10 to 12 days. Can this be further improved?

One area which can make a big difference in our IPO timeline is participation of the retail investors directly into IPO subscription. Retail and High Networth Individual (HNI) are important constituents of the markets. Their subscription to an issuance is critical and they remain a significant element of the issue subscriber base as there is a requirement of mandatory allocation of 50% of an issue directly to retail and HNI investors.

There was a time, 2-3 decades back, when there was fixed and regulated pricing mechanism and IPOs were a very lucrative investment opportunity for public. The concept of retail participation was therefore protected at that time to ensure that the wealth being created is shared with the wider society.

However, over a period, with several developments in the market one may need to relook at this situation. Now the pricing decision is left to the issuer and the IPO listing gain has become uncertain. With the book building method of transactions, IPO pricing has become very competitive and more realistic. The pricing is mainly driven by the institutional investors who are more informed and have the relevant skillsets to assess valuation. Most retail and HNI investors opt for the easier route of cutoff price option. It means they let other investors decide the price and they are happy to simply invest at such price levels. So, retail and HNI category are practically not involved in the pricing decision.

Secondly, a recent study by the department of economic and policy analysis wing of SEBI indicates that a significant number of the retail and HNI investors sell shares allocated to them on listing. This artificially puts pressure on the stock on listing. Some of this selling is undertaken to offset the leverage taken by such investors for the IPO application.

Therefore, overall, a 50% mandatory allocation directly to retail and HNI may not be very relevant under the current circumstances. I totally understand that in a fixed price and regulated regime this could have been a different situation.

This issue has been debated time to time including in the context of improving the timeline for the IPO allotment. I think we need to review this situation again as several factors have changed - a listing price gain has become uncertain, Domestic institutional investors (DIIs) have become prominent in the market and have got a better handle to contribute to the IPO price discovery.

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As an alternative, we could encourage IPO dedicated schemes by Mutual Funds where a retail investor can participate and while leaving the investment decision to professionals. Since the institutions will be in a better position to negotiate the IPO price, overall, everyone is likely to get a better deal.

Other alternative sometimes proposed for a more guided retail investment is retail investors making an application through brokers. This was being suggested to improve the process time. However, given that our processes are today a lot more efficient, this option may not be required.

A non-mandatory retail participation will ensure less pressure of sale at the time of listing, and a lower impact on post listing trading price. If this is done, like in international markets, our IPOs can also be listed and traded in a very short time frame of 3 to 4 days from the building of the book. Am encouraged to raise this issue again as SEBI in recent times has made some very decisive decisions for better efficiency in the secondary markets like T+0 settlement system and a big decision of reintroducing the fixed price method in delisting offer. In the same vein, I suggest that this long outstanding issue of direct participation of retail investors in the primary markets can be relooked at. All this cumulatively will make our markets as one of the very best in the world.

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