IPO-bound cos may have to keep 25% with public

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MUMBAI: Companies planning to list may have to ensure that at least a quarter of their total equity lies with the public, as the government sets about its stated mission to ensure that investors get a wider selection of stocks to choose from.

A government official told ET that the notification amending the relevant clauses of the Securities Contracts (Regulation) Rules, 1957, is expected soon. The new norms would come into force soon after an okay from the law ministry, the official said requesting anonymity.

Under the current rules, companies have the option to go public with 10% or 25% equity dilution. If the company goes for 10% dilution, then the issue size has to be minimum Rs 100 crore, provided they issue 20 lakh securities. The government is scrapping the rules allowing companies to go for IPO with 10% dilution.

The government had made clear its intention to make a minimum 25% public float compulsory during the last Union Budget. The notification is intended to operationalise the budget annoucement.

Under the proposed plan, already listed companies will be required to divest at least 5% stake every year from 2010 to reach the prescribed threshold, according to a finance ministry official.

The move could affect the over 300 companies where promoters hold more than 75%, as they would now be forced to dilute their stakes in a phased manner to the public — an entity that includes the general public, portfolio investors and financial institutions.

The move could spark off a flurry of offerings from firms, mainly public sector undertakings which typically have low floating stock. The government estimates that there could be equity issuances worth nearly Rs 1.5 lakh crore if companies were to dilute their stakes to comply with the new stipulation.

According to investment bankers, the new move will temper valuations, as companies generally tend to raise maximum possible funds with minimum dilution.

Prithvi Haldea, MD of IPO-tracking firm Prime Database, said that the proposal could get quite challenging when big companies are involved, since large market capitalisation companies may not require such funds. “There may also not be enough market appetite for those kind of volumes,” he said.

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Mr Haldea’s arguments mirror the doubts expressed by many corporates and merchant bankers when the proposal was put up last year for public debate.

However, the thinking among regulators now is that this would give investors a wider choice of stocks, a former whole-time member of Sebi said.

Mr Haldea said the government should prescribe a 25% public holding or a minimum market float, which is more than 10%.

“We cannot have one law for all companies across the board. If the government insists upon this plan then it may discourage a lot of big firms to get listed,” Mr Haldea said.

Mehul Savla, director of Ripple Wave Equity, said the biggest challenge would be the enforcement of the new limit for existing listed companies.

“Any penal action against errant companies like delisting, suspension and financial penalties will ultimately hurt the small investors as well,” he said.

Mr Haldea argued that globally, many jurisdictions do not specify any percentage, but just insist on a minimum market float. In Singapore, a company must have a public holding anywhere between 12% and 25% for an IPO, depending on the market capitalisation. On the Nasdaq, one million publicly-held shares is mandatory for a listed firm, while in London, 25% public holding is essential in a listed company, he pointed out.