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Level playing field in IPO market

Mark to Market | Ravi Ananthanarayanan, Mobis Philipose and Vatsala Kamat

The Securities and Exchange Board of India (Sebi) has done well to introduce parity between institutional and retail investors in the initial public offering (IPO) book-building process. Institutional investors now pay 100% of the bid amount upfront while bidding in an IPO, a far cry from the days when they didn't have to put up any margin money and allotment to them would be on a discretionary basis by merchant bankers. Some years ago, Sebi applied a 10% margin and moved the system to one of proportional allotments. The current move brings complete parity.

Mehul Savla, who runs a transactions advisory firm, **RippleWave Equity Pvt. Ltd**, says that the move will reduce distortions in the book-building process. Under proportional allotment, there is a snowball effect as the book-building comes to a close. When the bidder sees that the book is already, say, five times the size of the shares on offer, his/her bid tends to be five times the amount of shares that were originally intended to be acquired. Savla explains that this is because of the foreknowledge that the allotment will be not more than one-fifth of the bid amount. With institutional investors now having to put up 100% of the bid amount upfront, this snowball effect will be considerably lower.

One of the reservations of getting institutional investors to lock up large sums of money was that there is an opportunity cost of giving up interest income. But when the Asba (application supported by blocked amounts) facility is extended to institutional investors, this opportunity cost will be removed, as they will continue to earn interest on the margin money. In this sense, they will be better off because they don't earn any interest on the 10% margin money they put up under current guidelines. Also, the regulator plans to reduce time taken to list the shares, which will also address this concern of funds being locked up.

Mint reported that Sebi is also considering asking exchanges to stop making the subscription number public while an issue is open, to discourage inflation of demand. All of these measures will considerably improve the efficiency of the primary markets.

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