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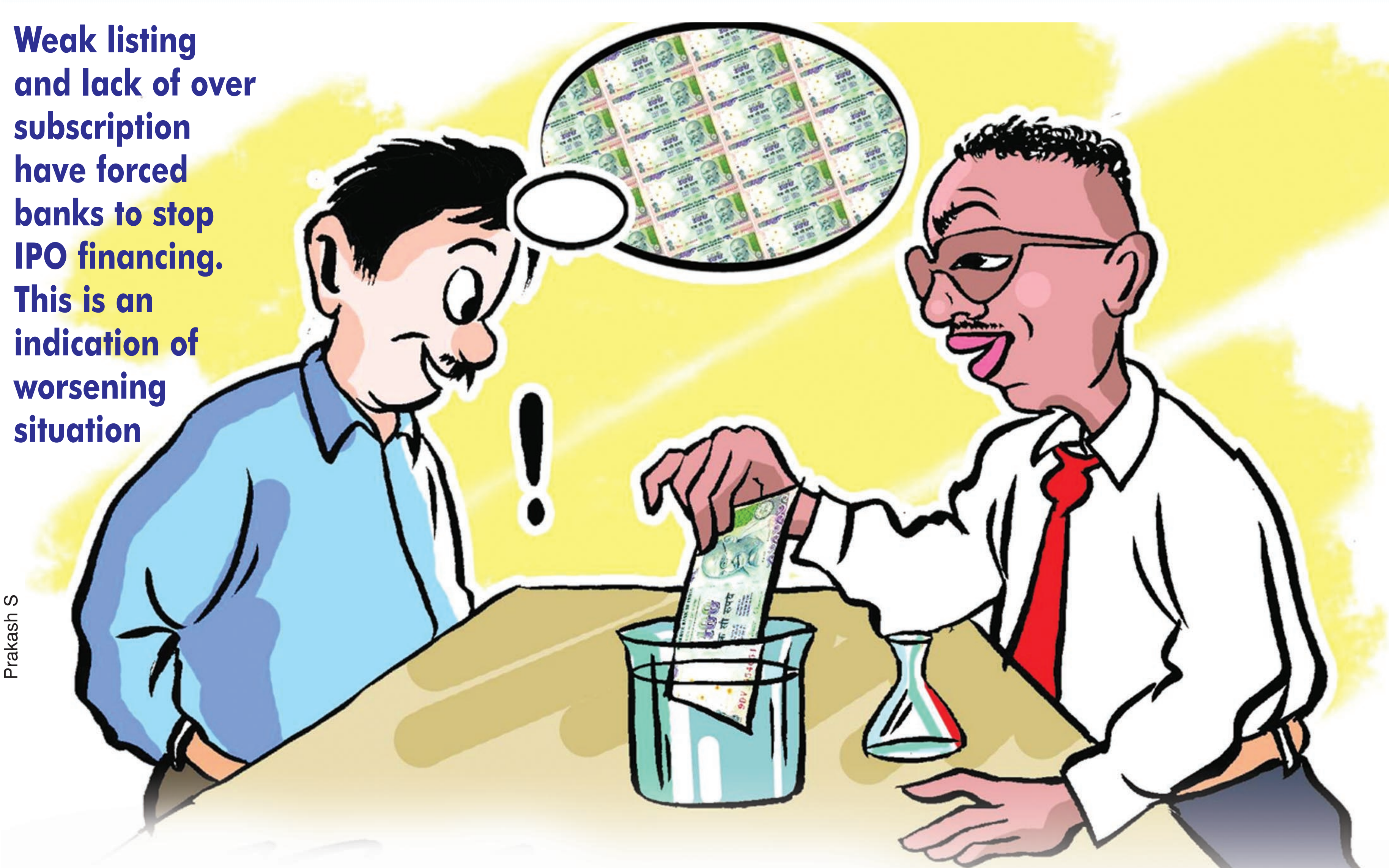
Weak listing and lack of over subscription have forced banks to stop IPO financing. This is an indication of worsening situation


Prakash S

IPOs at risk
Will it lead to realistic pricing?

ASHWIN PANCHAL

THE sad story of the IPO listings and new issue preparations continues. Recent fall in the stock market has shattered the hopes of the promoters who were planning to come out with mega IPOs to fund their expansion plans. There has been question mark on the timing of their issue and pressure on reducing the offer price. Even though market has recovered from low, now the investors are weighing the worth of the IPO prices.

'It looks like it will be difficult to convince investors at this point to pay higher values," said merchant banking source. Now a `wait and watch' policy would be best applicable to IPO issuing companies, who are facing an uphill task. The market has fallen 29 pc since its peak on May 11, when the Sensex touched a high of 12,671 points.

Small investors as well as HNIs, who burned their fingers are unlikely to return to the market in the immediate future. Besides, weak listing and lack of over subscription have forced banks to stop IPO financing and that has led the situation to the worst.

In the current market scenario, although certain issues have been caught in the meltdown and had troubled time for their oversubscription, others saw sharp erosion in share prices as compared to their offer prices. The companies like Deccan Aviation Ltd, Prime Focus, Gangotri Textiles and Rathi Udyog were clearly struggling, however managed to sail through. Since the time SEBI has imposed margins on qualified institutional buyers (QIBs), most bids now come only on the last day.

Prime Database analysis shows that apart from Reliance Petroleum and Union Bank of India, which sold 7.5 times and 1.87 times respectively, not a single issue was oversubscribed on the first day. Issues of Jagaran, R Systems, Plethico, Opto Circuits, Visa Steel and JK Cement of above Rs 100 cr garnered only 0.0 to 0.1 pc of amount on the first day. Unity Infraprojects, which is a big player in infrastructure sector and had priced its issue quite aggressively at Rs 651-732 range with 34 lakh shares on the block, however, has got good response from foreign funds.

The issue has scraped through and subscribed 1.28 times. But the response from retail investors was poor. In fact, investor's who have made handsome profits through IPO investment have saw sharp erosion in their investment following the steep fall in the indices.

As many as 150 stocks, including the likes of Jet Airways, ING Vysya Bank, Biocon, Reliance Communication Ventures, Karnataka Bank and Oriental Bank, have hit new lows as stocks fell like nine pins. The declines have also not spared some of the recent high profile IPOs such as Reliance Petroleum, Gitanjali Gems, Emkay Stocks, Plethico Pharmaceuticals, Sun TV, Punj Lloyd, INOX Leisure and PVR Ltd - all these stocks traded below their issue price.

Taking advantage of the bullish market, companies have priced IPOs as high as 24 times their forward earnings, leading to a steeper fall in their shares than the overall market, an analyst said. If the bearish trend persists for long, than mega issues of DLF, GMR Infrastructure, Lanco, Parsvanath Developers, Khanna Papers and SBI associate Banks may have to postpone their plans.

At least 20 more IPOs are mooted in the next few months. The government may also find it difficult to its 10-15 pc divestment of stake in Air India, and Indian Airlines, through an IPO by 2006.

The Aviation Ministry is looking at the possibility of raising the (financial) resources and improving (the airlines') financials by going for an IPO at a suitable time. A 10 pc stake in each of the airlines is likely to be offered to the public, to raise funds for their expansion. The IPOs by Indian companies, which have got increasingly expensive in the last few quarters, may have to be more reasonably priced in the coming months if they are going to attract takers, merchant bankers say.

According to analysts, the sharp fall in stock market would help bring more sanity into issue pricing. There have been instances of some issuers becoming aggressive with their IPO pricing. Said Prithwi Haldea, Chief of Prime Database: "We may now see more realistic pricing and that is good news for the investors. The issue pricing will now be more logical as there is a fall in the market. On a fundamental level, we should understand that an issuer can no longer price his IPO at his own will, because unlike the 90s, SEBI's new guidelines require that at least half the IPO should be subscribed by the QIB." Clearly, everybody loves a booming primary market. Large corporate houses cash in by raising large and sometimes unnecessary chunks of money.

In the early 1990s they pumped the money raised in the primary market into real estate and finance companies, creating an unsustainable bubble. Eventually, both these markets collapsed and hundreds of finance companies vanished.

India needs a healthy IPO market for a sustained 8 pc growth of the economy. However, the market regulator must develop the system to avoid any kind of IPO-scam in the future.

KEY DRIVERS AS PER GRANT THORNTON INDIA

A. Stock market valuations: This is obviously linked to the optimism in the economy and the corporate profits. These two created confidence in corporates to aggressively go after M& A as a key part of their growth strategy.

B. Availability: In a number of sectors, there were several small and niche players who had key skills but were struggling due to lack of capital or skill sets to manage the businesses profitably.

C. Consolidation: This factor is globally regarded as a key driver for M&A. Even today there are over 2,000 software companies of all sizes and focuses, over 500 paper mills, over 5,000 pharmaceutical units and over 1,000 packaging companies in India. There is a clear scope for consolidation of some of these establishments.

D. Emotional attachment: As India globalised and liberalised, employees lost their loyalty to the company and life long employment became history. This commenced over a decade ago. In the past three-four years, business owners have also opened up their horizons to consider acquisitions as well as divestitures, and are increasingly open to treating their business units as investments as opposed to family heirlooms.

E. Private equity: The entry of private equity has enabled companies to look at M&A more aggressively. In addition, the private equity players started to look for complete acquisitions with management support as we have seen in Punjab Tractors and Nutrine.

ANALYSIS OF TRANS-NATIONAL DEALS IN 2005

- There were more outbound deals (Indian business acquiring international companies) than inbound deals both in value and volume terms
- While Indian companies have acquired several businesses overseas to get an international footprint, most of these outbound deals have been lower value deals showing that Indian businesses are treading carefully and minimising their risks through value buys
- Inbound deals are fewer in numbers and much higher in value. The largest proportion of outbound acquisitions have been in Europe (50 pc of deal value), followed by North America (24 pc of deal value). USA and UK are the two countries that garnered the maximum outbound deal share, at 35 of deal value

Note: *Grant Thornton India is the Indian firm of Grant Thornton International, the fifth largest accountancy firm network in the world, with over 600 offices in over 110 countries and employing more than 22,000 people. The firm is one of the leading accountancy, taxation and corporate finance advisory firm advising business owners and entrepreneurs with international ambitions.*

Indian companies on the prowl

AMAN DHALL

INVESTMENT banking professionals need to tighten their seat belts as the Indian M & A (Mergers and Acquisitions) market is taking off its flight on a globetrotting visit. India Inc has already acquired 29 foreign companies (US $ 2.1 bn) in the first four months of this year in comparison to the 42 acquisitions (US $ 2.3 bn) made last year.

Industry Analysts believe the liberalisation of the Indian Economy back in early 1990s had paved the way for the current Indian onslaught overseas.

"The volume of international acquisitions by Indian companies is expected to grow exponentially in the coming years. The figure for 2006 is expected to cross the US $ 4 bn mark," says Anil Kumar, Managing Partner, Virtus Global Partners (New York based investment bank).

At present, investment bankers are flooded with M & A deals pertaining to Indian companies driven by huge currency availability in the domestic market. Private equity players and banks craving to fund such overseas acquisitions have led to the cross-border deals scaling new-fangled heights in the vibrant world market.

In the early 1990s, the perception about the Indian companies was not that good and raising money in the domestic market was not so easy. Now things are different as Indian IT Sector started to make waves in the world market through impressive growth coupled with smart professionals ready to hit the road with their innovative ideas and relationship building skills.

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Experts describe the two decades (90s and 00s) as 'confidence building' and 'consolidating' ones for the Indian financial system, which they evaluate, would rise exponentially in the next decade (10s) and reach its peak in the decade following (20s).

IT, Pharma, Auto Component, Manufacturing, Biotechnology companies are seeing a substantial interest from the global companies, who reckon them as the best bet for investing in the Indian Industry. "These sectors have fared exceptionally well in the Indian market. While Indian companies in the recent past have accumulated a lot of wealth and wish to deploy it cautiously, American firms are also keenly watching India's growth story and want to be a part of it," highlights Harry Minj, The Managing Partner in Virtus Global Partners. Currently, this firm is engaged in providing M & A advisory to several mid and large size clients with revenues in the range of $ 40 mn to $ 150 mn for acquiring companies in US and India as well as private placements to the tune of $ 15 mn to $ 60 mn.

"What happens in the M & A market is if an Indian company goes for acquisition abroad? It will typically like to buy 100 pc stake. When a foreign company picks up a stake in domestic company, it would like to test the waters first by buying majority stake and then goes for a complete takeover at a later stage," according to Kumar, an analyst.

Virtus Global is in talks with six technology firms, two pharmaceutical firms, one candy manufacturer and one automobile company in the US to go for such cross-border transactions in India. They are also in touch with five Indian companies for their deal in the US.

With more product-based companies in industry, exit became much easier for the firms in recent times. "Sectors like automobiles and pharmaceuticals are governed by 'smart managements' and have a great scope in both the US and India. Today, the buying companies always keep an exit strategy in its mind while going for a purchase," says Minj, graduate of IIM-Bangalore.

Acquisitions made in the US represent about 24 pc of the total Indian pie. This number may go up to 35 pc as per analysts.

SECTOWISE BREAKUP-ALL DEALS BY VALUE