

Woo the masses

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Instead of rating merchant bankers and grading issues under the garb of investor protection, SEBI should try to get back retail investors



Time and again, the Securities & Exchange Board of India has demonstrated its uncanny ability to close the stable door after the horses have bolted. In the interest of investor protection, for several years regulators the world over have been seeking to improve the functioning of equity markets by introducing independent views and research into capital markets. However, independent research that is structured as an investment recommendation has struggled for business viability since brokers and investment bankers provide free research, in common parlance known as 'placement driven' research.

Against this backdrop, in January 2006 SEBI, in its wisdom, introduced a grading system for Indian equities to encourage independent research into the capital market. Since rating agencies are independent of the issue-selling process and their so-called proficiency in analysis, the watchdog thought it fit that rating agencies such as Crisil, Care, ICRA and Fitch, give investors their expert opinion. In February 2007, this grading was made mandatory for all capital market issues. The grading mechanism was based on a relative assessment of parameters such as management capabilities, business prospects, corporate governance, financial performance, capital history, compliance and litigations, among other peripheral issues.

A post-mortem showed that the idea did not yield the desired results; grading failed to make a major impact either on the investment rationale of retail investors or the wealth created by the underlying companies post-listing. In fact, nowhere in the world are public offerings graded. In any case, post the sub-prime crisis, when rating agencies gave AAA ratings to sub-prime bundled debt which proved worthless, their credibility took a huge knock.

In fact, during the boom years of 2007 and 2008, companies such as Reliance Power (oversubscribed 72 times), Edelweiss Capital (oversubscribed 110 times), Gammon Infrastructure (oversubscribed 3.5 times), to name some, got a four out of five grading, that is, above average fundamentals. While Edelweiss jumped handsomely, RPower and Gammon ended the first day of listing below the offer price. An important ingredient in grading

is to look at the offer price or price band to ascertain whether the pricing of the issue is fair, justified or not.

Come 2012, SEBI chairman U.K. Sinha sent a circular that merchant bankers handling public offerings should disclose their track record in managing IPOs/FPOs. SEBI has banned some merchant bankers who managed recent IPOs. (Thank God that the markets are down and issuers are feeling jittery of tapping the public purses.) The barred entities are Hem Securities, Atherstone Capital, Chartered Capital and PNB Investment Services, etc. In this lot is Hem Securities, which has been hauled up time and again for manipulating stock prices.

There are several such examples of other errant merchant bankers who have gone scot-free or have been fined measly sums, at the cost of gullible investors. Indian capital markets are fraught with investors being taken for a ride, particularly when the Indian markets are in a secular bull run. After a bout of greed, it is fear that has gripped the retail/ small investor and even the issuer.

Now, the latest SEBI circular has asked merchant bankers managing IPOs/FPOs/debt instruments to disclose how the issuers have performed over the last three years in terms of performance, utilisation of issue proceeds and the extent of deviation of funds if any, schedule of project implementation and peer group comparison "so as to enable investors to take well informed investment decisions". Haven't we heard that 'past performance is no guarantee for future performance'?

With the offer document containing other regulatory and statutory disclosures, the net result will be the offer document would carry a similar disclaimer from merchant bankers based on the documents furnished by the issuing company which could be outright fictitious. In such a scenario, the bulge bracket would rule the roast and the small fries and newcomers would keep on shrinking.

Given current market conditions, the retail investor has been steadily decimated. These gimmicks of whether rating of issues or merchant bankers is unlikely to revive confidence. There are a series of issues why retail investors are being steadily marginalised. SEBI would do well to consider steps to bring them back. «