Deloitte.
Private

IPO and capital markets
Deloitte Private Newsletter

June 2022

Content

Foreword

In 2021, Indian companies raised approximately INR 1.19 trillion (INR 1.19 lakh crore) through IPOs—more than four times the amount raised in 2020 (INR 26,628 crore). Several factors have driven the IPO market in India, including new-age technology start-ups (such as Zomato, Nykaa, and Policybazaar), a low interest rate environment, strong participation from across investor categories, and the Indian growth story. This has pushed more companies to tap into the markets, reflecting not only the confidence in markets, but also in the corporate sector and prospects of the economy in the long run. With record-level IPO activity in 2021, this Deloitte Private newsletter edition provides a most timely focus on IPO and capital markets.

India's capital markets are witnessing important and emerging trends in terms of retail investor participation, OFS proportions in IPOs, alternative avenues for offshore listings, amongst others. On the back of strong retail participation, the number of Demat accounts has more than doubled to 7.7 crores from 3.6 crore between March 2019 and November 2021. Additionally, recent IPOs have witnessed a significant proportion of OFS. Around 50 percent of the total IPOs in 2021 provided exits to early-stage investors through OFS. However, the market regulator, the Securities and Exchange Board of India (SEBI) introduced certain reforms recently, including a cap on OFS by existing shareholders. SEBI has also introduced amendments to increase disclosures around pricing and purpose of the issue—empowering investors to make well-informed investment decisions.

In recent months there has been a slowdown in IPO activity due to geopolitical tensions, inflation, as well as global interest rate hikes, leading to market volatility and massive selling by foreign institutional investors. IPOs in India are likely to regain momentum subject to global and macro factors, possibly in the next 3–9 months. With more than 20 companies filing DRHPs and planning to raise funds, the pipeline looks strong and several companies have received SEBI approval for their IPOs (Go Airlines, MobiKwik, Emcure Pharmaceuticals, and PharmEasy, to name a few). Further, May 2022 also witnessed the listing of LIC, the largest IPO in the Indian capital markets.

In this signature edition of our newsletter, we have put together eclectic insights and perspectives from senior industry players who have recently undertaken IPOs. We are most fortunate to have an expansive and exclusive interview with Tuhin Kanta Pandey, Secretary DIPAM, on the role of capital markets in the government's overall disinvestment strategy, and an unpublished insider view into the marquee LIC IPO. We are also grateful to Vikas Sureka, CFO, MPL Gaming and Sumit Zaveri, CFO, Burger King for their views—they represent companies in exciting new categories for IPO investors. This edition of our newsletter also carries a wealth of material on the recent evolution of the IPO markets along with practical guidance for IPO readiness, serving as an aide memoire for those contemplating this journey.

We hope that you as a reader enjoy perusing this material, as much as we have enjoyed putting it together.

Best wishes

Uday Bhansali
President – Financial Advisory
Deloitte Touche Tohmatsu India LLP

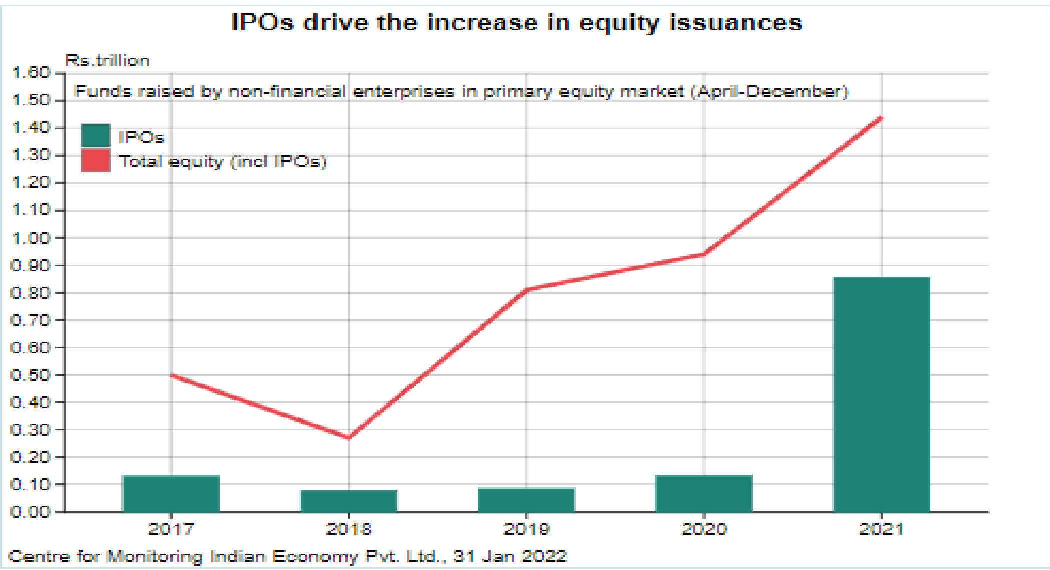
Update: The changing nature of the IPO market in India

Primary markets function through IPOs and play a critical role in any market-driven economy. They allow young companies to access finance from a broad category of investors. Companies that go public often see an improvement in their brand value and public image. Publicly listed companies have strong disclosure norms through the stringent 'Listing Agreement' and are more scrutinised than the unlisted firms. Listed companies offer High Net-worth Individuals (HNI) and retail investors great opportunities to become shareholders in promising businesses, along with the ease of entry and exit. Although listed shares can be obtained in secondary markets, IPOs allow investors to enter at lower prices and acquire listing gains if the shares list at a premium.

A bullish market attracts early-stage investors and entrepreneurs who issue (or transfer) equity to new investors in the hope of getting a reasonable valuation for their company's stake. Bull runs in the stock market often cause a surge in IPOs, as seen in 2020 and 2021, due to the excess global liquidity and low bond yields. This increase in the number of IPOs was observed across most global markets.

The IPO market in India is also riding on the buoyancy in the global equity markets. According to the 2022 Economic Survey, 75 companies garnered INR 89,066 crore through IPOs between April and November 2021. As Figure 1 confirms, this is much higher than any year in the past decade.

FIGURE 1



Key reasons for this boom have been an accommodative monetary policy followed by global central banks, which is leading to improvement in growth outlook. The Indian government's emphasis on reforms and infrastructure has also helped with the economic recovery. Additionally, a section of companies such as start-ups, have grown during the pandemic due to changing consumer preferences. These factors have contributed to the optimism in the primary markets, attracting many companies for fundraising through IPOs and listing on the stock exchanges. From investors' perspective, lower interest rates and limited avenues for investing have also contributed to the boom in IPOs. Interest rates on deposits have fallen while other asset classes have underperformed, thus pushing liquidity into equity markets.

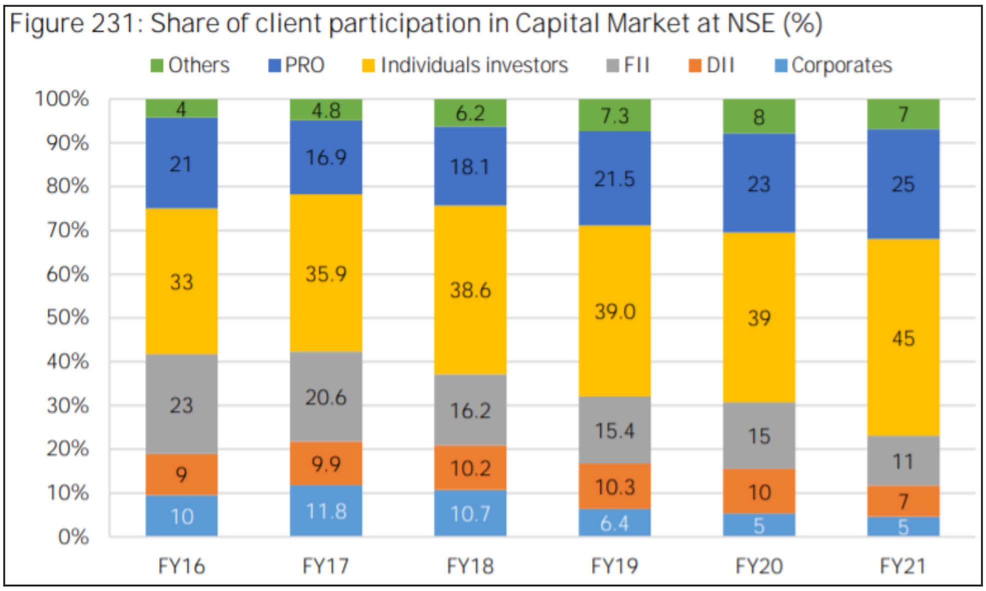
The structural changes in the economy due to demographic factors and new listing norms have also affected the Indian IPO market. This is visible in the nature of the issuances and variety of companies raising equity through IPOs. Other factors, such as rising middle-income class, access to the internet, increasing awareness about various asset classes, ease of participation, and stricter investor protection norms by SEBI have also contributed to the improved retail and HNI investor participation in Indian equity markets.

Rise of the young investor

The exuberance in the equity markets has led to a surge in the number of demat accounts. According to the SEBI chairman, the number of demat accounts has more than doubled to 7.7 crore from 3.6 crore between March 2019 and November 2021; 75 percent of these new accounts belong to investors aged under 30.[1] Evidently, the proportion of young investors seems to be on the rise in the retail and HNI categories.

The retail share of the total turnover at the National Stock Exchange (NSE) has risen to 45 percent in FY'21, up from 33 percent in FY'16[2] (see Fig 2). These numbers reinforce the increasing participation of retail investors in the market. The democratisation of equity markets and greater financialisation of savings are welcome news for the Indian economy, which is aspiring for greater formalisation.

Figure 2



[1] https://www.business-standard.com/article/markets/number-of-demat-accounts-have-more-than-doubled-since-march-2019-tyagi-122010501552_1.html

[2] NSE Market Pulse April 2021 | Vol. 3, Issue 4 Page 170: https://static.nseindia.com//s3fs-public/inline-files/Market_Pulse_April_2021.pdf

Increasing appetite for new-age technology companies

Due to access to information, young investors have greater awareness of new-age technology companies (also called start-ups) and are willing to invest in them. Several digital start-ups have registered significant growth during the pandemic and are listing in greater numbers as they received positive responses from investors.

The SEBI relaxed the norms related to holding period, delisting, and open offers to promote the listing of start-ups in India.[3] The changes were a welcome development as that allowed early-stage investors in start-ups to exit or dilute their holdings at market-determined prices. Listing on the bourses allows broad-based equity ownership into companies that private venture capital funds have nurtured. With age on their side and a higher risk appetite, young investors use these IPOs as an opportunity to invest in new-age companies founded by people like them.[4],[5]

Aggressive IPO bidding by HNIs

HNIs have been flocking to invest in start-ups through the alternative investment fund (AIF) route.[6],[7] However, this does not mean that their attraction for IPOs has waned. Of 63 IPOs in 2021, 25 were subscribed more than 100 times. Six of these registered listing gains of more than 100 percent. Six more closed with gains of over 50 percent on the listing day.[8]

Many HNIs have been investing aggressively in IPOs. They have even taken loans for this purpose. The HNI or NIIs have borrowed heavily for listing gains.[9] This is because the allocation of shares for HNIs is slightly different than that for retail investors. Retail investors get shares through a lottery system in case of oversubscription. However, the allocation of shares is proportional in the case of HNI investors. So, the more money they put in IPO bids, the higher the number of shares they can get allotted. This has led to heavy speculation and conflicts between IPO financiers and HNI investors. Lately, NBFCs have raised money via commercial papers to offer loans for financing IPO subscriptions.

The RBI wants to curb the speculative use of borrowed money to invest in IPOs for making listing gains. Therefore, it has capped the borrowing amount for investors to INR 1 crore per IPO. Market regulator SEBI has also modified allocation rules for HNIs. One-third of the HNI shares will be reserved for investors with application sizes ranging between INR 2 lakh and less than INR 10 lakh. The remaining two-thirds of the portion will be reserved for IPO applicants whose application size exceeds INR 10 lakh. This will allow even relatively smaller HNI investors to get equity allocation apart from discouraging over-speculation by large-ticket HNI investors.

Rising risks from recent IPO issues

Capital raised through IPOs has been primarily used to reduce debt or increase capital investment. This trend is gradually changing. Recent IPOs have had a higher proportion of Offer for Sale (OFS) issues. This means that companies did not entirely use the money raised via IPOs for investment and growth. Instead, the IPO proceeds allowed early-stage investors to exit. As a result, IPOs did not decrease debt or increase capex for several newly listed companies.[10] According to a report

---

[3] https://www.hindustantimes.com/business/sebi-eases-norms-for-startups-to-go-public-101616717558356.html

[4] https://economictimes.indiatimes.com/tech/startups/smells-like-teen-spirit-young-indians-keen-on-ipos-of-new-age-companies/articleshow/84390637.cms?from=mdr

[5] https://economictimes.indiatimes.com/markets/stocks/news/young-retail-investors-become-a-force-to-be-reckoned-with/articleshow/88512984.cms

[6] https://economictimes.indiatimes.com/markets/stocks/news/why-hni-investors-are-flocking-to-startups/articleshow/87696554.cms?from=mdr

[7] https://economictimes.indiatimes.com/tech/startups/hnis-to-invest-30-billion-in-indian-tech-startups-by-2025-report/articleshow/83607846.cms

[8] https://www.business-standard.com/article/markets/ipo-frenzy-drives-borrowing-through-commercial-papers-shows-data-122021000075_1.html#:~:text=IPO%20frenzy%20drives%20borrowing%20through%20commercial%20papers%2C%20shows%20data,-Ashley%20Coutinho%20%7C%20Mumbai&text=The%20rush%20for%20taking%20loans,2021%20stood%20at%20Rs%2021.

[9] https://www.business-standard.com/article/markets/ipo-frenzy-drives-borrowing-through-commercial-papers-shows-data-122021000075_1.html#:~:text=IPO%20frenzy%20drives%20borrowing%20through%20commercial%20papers%2C%20shows%20data,-Ashley%20Coutinho%20%7C%20Mumbai&text=The%20rush%20for%20taking%20loans,2021%20stood%20at%20Rs%2021.

[10] https://m.economictimes.com/markets/ipos/fpos/recent-ipos-only-filled-investors-coffers-did-little-to-dent-

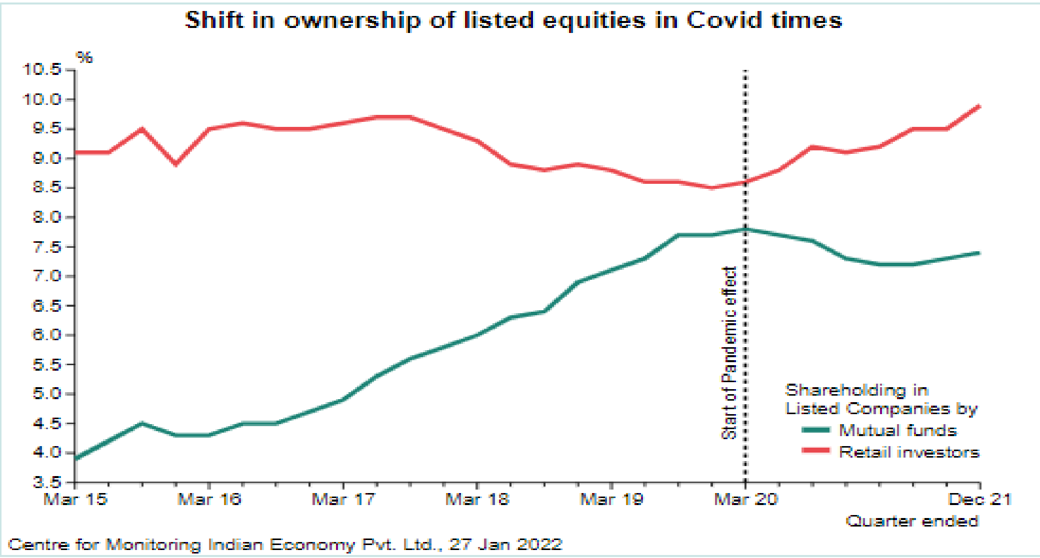
from the credit rating agency, India Ratings & Research, 19 percent companies raised funds for capital expenditure, 19 percent to repay existing loans, and 11 percent was an OFS.[11]

This prompted SEBI to put in place limits on the proportion of shares that can be sold under OFS through IPOs. Early-stage investors with more than 20 percent stake in the company before the IPO will be able to sell only half of their shares in the OFS. At the same time, investors with less than 20 percent holding in a company before the IPO will be allowed to sell only 10 percent of their shares through OFS.[12]

With exit of early-stage investors, the ownership of start-ups transferred from venture funds to retail and HNI investors. However, this also exposes inexperienced investors who lack financial literacy and professional guidance to more significant risks. Some of these start-ups are still quite young, with weak profitability prospects and cash guzzling business models. Retail investors often have low visibility of risks associated with such investments. With institutional investors liquidating their positions after IPOs, retail investors end up having increased stakes (see Fig 3). Investors coming later and entering equity markets at rich valuations and undertaking speculative trade are vulnerable to higher erosion in their wealth. Any subsequent valuation corrections could also lead to a popular backlash against markets, regulators, and the government.

As of the third week of February, a total of 54 companies raised INR 1.22 lakh crore thus far through IPOs in FY'22. Of these, shares of 32 companies (i.e., about 60 percent of newly listed companies) are trading below their listing day close prices.[13]

Figure 3



Some considerations for IPO investors

The IPO trend will likely continue in 2022 as several high-profile issues have been lined up, including the one from the largest public-sector insurer. However, rising interest rates in advanced countries, high inflation, surging oil prices, the prolonged COVID impact, and geopolitical tensions could dampen market sentiments. Investors should be mindful of these risks while allocating funds to IPOs over other asset classes.

corporate-debt-report/articleshow/88141193.cms?_oref=cook

11 https://economictimes.indiatimes.com/markets/ipos/fpos/recent-ipos-only-filled-investors-coffers-did-little-to-dent-corporate-debt-report/articleshow/88141193.cms?_oref=cook&from=mdr

12 https://economictimes.indiatimes.com/markets/ipos/fpos/sebi-approves-several-new-measures-to-reform-ipo-market-disclosures/articleshow/88544740.cms

13 https://www.business-standard.com/article/markets/over-half-the-stocks-that-debuted-in-fy22-trade-below-listing-day-close-122021700220_1.html

In conversation with Shri Tuhin Kanta Pandey, Secretary, Department of Investment and Public Asset Management (DIPAM)

Shri Tuhin Kanta Pandey,
Secretary, Department of Investment and Public Asset Management (DIPAM)

1. India's capital markets have transformed at a breathtaking pace over the recent years. Even the Government has raised significant capital through the divestment and minority sale of its equity. What has worked well and what could have worked better during these processes?

I think what has changed in India is that the capital market has become the first port of call and a diversification strategy for many. The width and depth of the Indian capital market has also increased considerably, owing not only to India's economic growth, but also the burgeoning middle class and millennials who are looking at their portfolios with a fresh perspective. In addition to the new companies that have entered the equity market, including start-ups, there are also listings of PSUs by the

Government which has essentially brought in an equity culture and created depth in the market by providing variety of sectors to choose from.

In our own experience, I think we have done quite a lot in our two roles—the minority stake sale and divestment on the market, and strategic disinvestment where control is passed on. In the last six years, we raised about INR four lakh crore (4 trillion rupees) in terms of disinvestment, which includes divestment and also strategic disinvestment to the order of ~INR 70,000 crore. While these particular strategic disinvestments have been from one listed company to another, in some cases unlisted as well, capital market support was necessary. This is also true for the "brownfield expansions" of NTPC or ONGC in buying other government companies. But we have moved away from that now. Handing over of management control is a key reform that has been undertaken for pure play privatisation.

In the privatisation space, capital markets are looking forward to this strategy and if we succeed it may have a larger domino effect. As an example, in Air India's case, we were successful and it had a larger impact on both public sector stocks, as well as private sector stocks. Government shedding control almost adds a little boost to the market and adds impetus for economic reforms. Every successful transaction, in that sense, adds value to the overall, public-sector portfolio.

Although we did dilute in the market, in some cases, listing is quite welcomed in bringing new stocks to the market. During COVID-19, we had IPOs of RailTel, IRFC, and Mazgaon Docks and now there is LIC. While we are planning for IPO of IREDA, and another company in renewables that will also be brought to the market soon, so these have helped. In some other disinvestments, we have had to review our strategy and pause, particularly in equity ETF, namely, CPSE ETF and Bharat 22 ETF. While for the private sector companies that SUUTI (Specified Undertaking of Unit Trust of India) has, namely L&T, Axis, and ITC - we have exited L&T and substantially reduced Axis. We still have our stake in ITC but, nevertheless, this was also in a bundle in a basket. Creating a price overhang has not gone down well with the markets, which is why, we heard the market from the point of view of minority shareholders. We have not been using equity ETF and neither do we intend to use it in the future. Rather, I think we will take up a more nuanced strategy and look at it on a company-to-company basis.

We have also shunned repeated OFSs (Offers for Sale) in the market so that there could be better play. Some companies are not performing well, so to that extent we have issues around a certain fixed strategy and would rather make it dynamic. Overall, PSU stocks as an index have started performing relatively well as compared with what it was earlier. In the last one year, both NIFTY CPSE as well as BSE CPSE have improved. There has been significant improvement over the years, and some of the divergences between the BSE and the NIFTY in general and the CPSE-specific indices are getting bridged.

The markets have given us an opportunity to raise funds and have also encouraged us to rethink our strategy in terms of our minority stake sale disinvestment to make it more nuanced. This is an overall experience, where, we have seen other markets adopting a similar strategy. We have also been very cognizant of the fact that markets do indicate the underlying performance of a company to some extent. In that context, we have brought in performance-based incentive schemes of the CPSEs with elements that reflect the market—return on equity, return on assets, market cap, asset turnover ratio – to emphasize to the CPSEs that their performance is also to be judged on their engagement with the market and how the market is viewing them.

We are also watching consistent dividend policies, where we have been quite successful. Government-owned companies have consistently been paying good dividend. Those are some of our corporate governance benchmarks. One of our strategies is to have CAPEX continued but at the same time we have also said that these CAPEX plans must yield tangible improvements in both top line and bottom line. We are now increasingly seeing share buybacks to provide return to the shareholders, including the minority shareholders, in instances where surplus cash available and which is not deployed elsewhere. Also, bonus shares, splitting of shares much like in the case of IRCTC, would increase liquidity of their stocks.

I think we are increasingly getting attuned to capital markets. DIPAM has been guiding the various administrative ministries to pause and ponder and perhaps consult DIPAM on policy steps that can affect the markets in a big way.

2. **LIC has been the most recent and unprecedented success as an IPO. What was the strategic rationale of taking LIC public, maybe from the perspective of the government, industry, and the corporation?**

An important policy of the Government has been to bring in most of our commercial enterprises, as possible, into the listing space subject to a certain size and their operations, which will ultimately impact and attract the markets.

LIC was one financial institution that had remained under Government control for far too long. In line with the Government's strategy, it was certain that this institution should have a wider listing and wider public ownership. This was for multiple reasons. First, the listing itself would offer tremendous confidence to the management to face the market and competition in a square way. Comparison with peers, both in India and abroad, adds to the competitive strength and paves the way for changes in the economic management of a corporation, especially to reorient both its product mix and distribution channel mix to create better shareholder value. Second, an independent board would bring in perspectives from the market and add value to the ESG practice of the company. Third, it provides resources to the Government in a significant way. There was no point for the Government to continue to maintain 100 percent ownership of LIC. If the dividends had to come to the Government, they could equally go to minority shareholders as well. The growth opportunities could also be used by the investors. At the time of its listing, LIC was trying to bring in ~INR 5.5 trillion as market cap to the Indian capital market. As we go forward, and as the float and liquidity increases over time, a large public institution in insurance will add further heft to the Indian capital markets. That was the rationale.

3. **It must have involved great complexities and its own set of challenges. What were some things that went right? Given its magnitude, can you share some of your thoughts on how the journey has been, the challenges, and how you overcame those?**

When we brought in LIC initially, there was a lot of disbelief from across sections. The foremost question was whether the Government could do it. As a brand, LIC has been deeply intertwined with every nook and corner of the Country. But the nuances of its value, its shareholders' perspectives, its policy holders' perspectives, were all quite a mystery to most, including large part within the Government. A lot had to be discovered, which essentially needed a deep dive into this legacy institution. That was the level of complexity.

While it made sense from economic, transparency and growth perspective, there was also a socialistic sort of loyalty amongst a large section of the population. Policy holders were skeptical about bringing in external shareholders. The process by itself was another challenge—it was a statutory organization without proper capitalization and fund bifurcation. While in principle the decision was already made, there were many unanswered questions on how we would discover the embedded value and if Corporation's own internal IT structures could handle this process.

This is when DIPAM deployed Deloitte and SBI caps as pre-IPO partners for LIC's IPO journey. This was again entirely new because the standard approach had always been to rely on merchant bankers to market and sell the issue. Deloitte prepared a strong implementation plan in terms of project management, down to a very granular level of detail, along with round-the-clock monitoring and weekly meetings of the stakeholders. Everything had to be crystallized, from the kind of drafting changes to comply with SEBI regulations, ensuring an independent board necessary for a listed company, to consolidating accounts for several subsidiaries, for example, a bank under LIC. These roadmaps were created and the handholding by Deloitte and SBI Caps went well into preparing RFP to get merchant bankers.

I would say it has been an extremely complex project because even the top management at LIC was unsure of how to go about it. Early on, we had onboarded Milliman Advisors because of the sheer complexity of deriving the embedded value. We had 10 merchant bankers, five from outside of India and five Indian banks. All of them came together, brought in their own perspectives. Online systems also had to be developed because this was happening at the time of COVID-19. Additionally, we had court challenges in Madras High Court and Bombay High Court, which were successfully handled. Even right on the date of allotment, we had a Supreme Court hearing. Then, of course, we also had the unprecedented Ukraine crisis. While this may have been full of challenges, it also demonstrated the true capacity of the Indian capital markets despite much muted response from FIIs.

The Indian insurance market is under penetrated and has great opportunities to grow further. I am confident that LIC 3.0, as Mr. M R Kumar (Chairman, LIC) calls it, will start delivering on different fronts including the product mix. Deloitte has been instrumental in highlighting some of these opportunities and challenges early on.

It has been, to some extent, a leap of faith for us in the Indian system to carry this through and today it has given us a great deal of confidence. The capital markets have matured significantly, much more than what we had possibly imagined.

4. **There has been a spurt in IPOs in India over the years. In your view, can the Indian market support this growing number and scale? If the frequency of large government IPOs were to increase, would the Indian markets be conducive and have the depth to absorb them?**

Yes, I think what is very significant in the Indian capital market is retail investors participating directly in the IPOs. In many markets, like in the US, they don't. In that sense, this is more sophisticated because we bring all investor categories to the IPO straight away. We do not restrict retail investors to the secondary market only. But at the same time, we need to bring in a fair amount of QIB and anchor investors, who can lend support to retail investors, so they are not guided purely by emotions. They can take conscious calls with the support of these institutions through their research and analysis. Also, markets being what they are, waver, and are also largely contingent on central banks around the world. Black swan events, such as the pandemic, have their own impact on the stock markets because sometimes extra liquidity also pushes valuation and prices. These will also correct over time. I think the evidence points towards the capital markets being capable of offering reasonable returns, and often acting as a hedge for inflation.

In several cases, even bank and interest rates drop to negatives but capital markets allow you to choose between debt instruments and bonds, as well as fixed income and equity, so you can build a diverse portfolio. In the case of IPOs, LIC has been very significant, even though we had continuous FII exits month on month. However, an almost equal amount came in through domestic sources, so I think an important factor in the capital markets is to have faith that they will deliver. Additionally, domestic savings are still being routed into the markets as a way to fundamentally diversify the savings pool. For the upcoming generation of investors, the stock market is a significant aspect of their savings. Which is also why mutual funds haven't faced redemption pressures, in fact, there has been a continued ingress into SIPs. Sometimes, when the markets are down, it’s a good time to buy. Even after the Ukraine crisis, multiple IPOs have come in. LIC, too, was a leap of faith for us because we were able to sense the latent demand, where we thought we could follow the momentum. In that sense, DIPAM has also used this opportunity in the listing of PPL (Paradeep Phosphates Limited), where we had divested 74 percent in 2002 and had about 19.5 percent left. In light of the food security issues, the fertilizer policy, and the supply chains, it was crucial that fertilizers, such as phosphates and non-urea, be manufactured domestically. PPL was successfully listed, and we have exited through that listing. The other important factor in this context is the reasonability of valuation for IPOs. As more IPOs enter, valuation is something that will need to be reasonable.

5. Is valuation an art or science? How does one manage the expectation gap on the pricing of an IPO? What are some guiding principles for companies who are planning to list their companies?

At DIPAM, we have tried to be in sync with the professional advice. We listen to the professionals, but also challenge them to do intensive analysis to work out valuations through different methodologies. We don't really leave them merely to multiples and finding the median of such multiples while that is one of the approaches. We always ask them to conduct a triangulation, even a fundamental valuation, sometimes to understand if Discounted Cash Flow (DCF) is applicable. For example, in the case of LIC, or any other company, while there may be peers, they could be quite different—you cannot have apples to oranges comparison. It has to be properly thought through, so we don’t get into a situation where we're trying to upfront the value. That does not help. The goal should always be the reasonableness of valuation, and sometimes, the market may not understand this. Even with a reasonable valuation, the listing may start with a discount, but that is more of a short-term reaction. Fundamentally, after looking at the numbers and digesting the Draft Red Herring Prospectus (DRHP), you will have a clear idea of the situation three or six months down the line.

Also, listing pop gains are not something that I would say is the right way for investors. After all, when you're investing, you don't come in for a day or two and exit on listing day. I think we are leaving those kinds of investors aside. You want investors that stay for some time, but also provide them liquidity to exit in the event when they need money. Investors should also give a little bit of a play to the new corporation for a few quarters of results and see how it performs.

A reasonable valuation will definitely lead to better investor satisfaction, and in the long term, to give a total value of the shares is also good for the issuer. In the case of LIC, if we are doing a 3.5 percent dilution, 96.5 percent is still ours. We have to look at how the 96.5 percent will perform, because to upfront the value of the 3.5 percent would be a short sightedness. When the stock goes down, our value would also go down, and we will have difficulty in bringing out subsequent issues.

I would say, valuation is both an art and a science—science because of the quantitative methods, but, in the quantitative methods there are certain assumptions, and those can be an art.

6. With the success of all the IPOs and divestment by the government in the recent years, what are some key messages that you would give to private corporates on building trust with investors and especially retail investors?

Eventually, I think, we should have a plan. We should think of it as a corporation, where we have to perform. Then I think having a median view really helps because having an aggressive view of your performance going forward, and then trying to work around it, affects the valuation and growth rates. Optimism is good but an aggressive approach, just to sell and raise money, is not sustainable in the long term.

Research analysts and others play a key role in this regard because they follow a largely objective approach and are probably not carried away by sentiments of who is coming into the market and who is going out. At the end of the day, the corporation does not change fundamentally but the market changes four times a day. There is an influx of instantaneous information available today, which is why volatility is far higher. There is a constant need to build an upside or a downside for every small piece of news, but fundamentally, things don't change that way. What is needed is for people to fundamentally look at things with depth and maturity, so they are then able to guide investors. Investors, too, should look at the broader analysis and not limit themselves to their "gut feelings" and get carried away in the heat of the moment.

Interview with Vikash Sureka, CFO, MPL Gaming

Vikash Sureka, CFO, MPL Gaming

1. **What would be some key features/differences that you would consider highlighting as attractiveness of the two capital markets – India and the US?**
   One of the key questions one must answer is which market they want to list- the US or India? A few years ago, with growth of technology companies, there was discussion on how investors only look at performance metrics and not growth. However, it has changed significantly in past 3 to 4 years. In my view, no major difference exists in the mindset of investors in the US or India.

   For me, the fundamental characteristic to choose a market is availability of the peer group that helps investors compare and benchmark you. The depth of the market is a critical factor. US markets have depth; investors understand your story well and you also know what the metrics are that you should be focused on. Companies and peers are one of the important factors. Moreover, based on my experience, the patience level of investors in the US market is higher than that in the Indian market. They provide time for management to invest and story to play out for the next two-three years.

These two are the fundamental driving factors to identify the right market.

2. **Considering the recent Unicorn IPOs and the relatively larger number of US$1 billion plus IPOs in the past, how compelling has Indian IPO become compared with a US IPO? Is Indian capital market becoming more mature for such IPOs?**

If you are looking at mid-cap and small-cap IPOs, quality of investors, availability of capital, and the ability to deploy large amounts of funds, to get a fair share of allocation during the book building process are not challenges in India. If we look at the recent IPOs before COVID-19, there is no dearth of quality investors or capital in the Indian market.

The challenge is patience in investors after listing. The questions are raised on profitability while new-age companies went to market with growth as a story and not profitability.

3. **Are market features a key factor for choosing the market? For example, is confidential filing a key feature for consideration?**

Confidential filing is not the key decision-making factor for a company to apply for IPO, but it is one of the greatest tools one can have. IPO is a long process that includes preparing the management, company, and people for the post listing requirements. The confidential filing allows the company to buy time. One can start the process and prepare the company. After this, if the market is still not conducive or the business is not ready, the organisation can decide to list later on the basis of the readiness of the management and business team. The amount of flexibility it provides to the CFO and the management is unprecedented.

If the regulator agrees to get this tool, would it further reduce the difference between India and the US markets?

In my view, confidential filing probably won't make a material difference in defining whether organisation will go for IPO. However, the feature will enable companies to be better prepared and provide optionality. When the company goes for confidentiality filing , it becomes eminent that the company is looking for capital raise, thus enables it to look at optionality from investors' perspective such as M&A, access private capital with enough time on hand. If the company doesn't have an option, it is only the IPO path that the company has to take to explore the market.

4. **What would be some key readiness steps, the top 5-7 areas that companies should priortise and monitor as they prepare for an IPO?**

- First and foremost is the **business readiness to operate in the public environment.** The readiness of the business to go through the scrutiny where every action of the company can be questioned. There is a story that the organisation will present to investors – readiness means if your business is ready to support that story.

- **Preparedness of the management and organisation to be a public company.** The organisation has to ensure that governance systems, risk governance metrics, and independent committee, are in place to provide confidence to investors.

- **Coverage by analysts:** You have a group of research analysts who understand your business model, are able to forecast business, and give out a reasonable view to their investor base that help create interest in the company.

- **Marketing plans:** Roadshows and the ability to create interest with the good quality investors who believe in the story of the company and the management. Meet the investors who are willing to look at the investments with 4 to 5 years horizon with the organisation.

- **Structuring efficiency:** Is the organisation prepared with structuring and if investors have been made aware of the same as this also affects investors' interest?

If these five things are done right, the organisation is well prepared for its journey to IPO.

5. SOX is one consideration that comes in many discussions. What has been your experience?

While early 2000s, regulation was one of the important considerations. I don't believe a well-run company would worry about regulations. Organisations use various technologies and tools that help a great deal to manage regulations. Despite being one of the factors, regulations are not the top five factors considered for taking a decision on IPO.

Has the nature of ownership changed from early 2000 until now in companies from the IPO perspective?

When most companies access the public market, they have done close to 5-6 rounds of funding. The quality of investors one attracts, decides whether you are ready to go public or not. Investors put a rigor on reporting that makes organisation understand the importance of governance and regulatory requirements that comes with it. That's the biggest fundamental shift in my view.

Does it also help break the myth that if you have a strong investor, it will slow you down?

If you talk to any investor or founder, the goal is always to make the organisation successful. The only difference of opinion is time horizon. The founder is invested for the long-term vs the investors who are there for the short term. In my experience, having a strong investor, is beneficial for the organisation. They are objective and driven to get outcomes through incentivising management. This the helps organisation to move fast. In cases where founders/promoters are risk averse, the investors can accelerate the company's journey by making the decisions quickly to realise the potential and growth much faster.

6. How do you explain the "Equity Story" and what is the CFO's role in that?

Equity story is always teamwork – no one person will be able to make it work.

1. It comes down to simplicity. If you see the story from inside, it is complex. However, you should be able to tell the entire story in 15 minutes.
2. The story has to be inspirational and objective. When backed by numbers, it helps investors to look forward to the outcome.
3. The story should have promises that you can meet.

It is a combined effort of CEO, CFO, and the investor relations team where the IR team plays an important role. Investors tend to believe in story by CEO.

"Selling of the story by CEO and delivering of the story by CFO"

From a story communication perspective, the SEBI has levied several restrictions in India. What are those communication differences between the Indian and US markets?

If you see it as a point in time, it is difficult. Let us look at the overall time for the IPO process that spreads across almost one and a half to two years. During this time if you are able to have 4-5 rounds of interactions with analysts and investors to present your story and get feedback, the outcome won't be different.

The US market is more perceptive for the "Time to Work (TTW)" environment where people are willing to spend time and effort to talk to management. In India, we don't have such formal process. In some cases, we have an informal process. This training is far more relevant.

7. **Coming back to India, recently SEBI has issued a consultation paper seeking more disclosures about KPIs, including its audit. What are your thoughts or suggestions? How do these compare with your experience while working on US IPO?**

When you are accessing public markets, you have to establish a level of trust with your investors, including retail investors. The SEC rules are elaborate and evolved through regulations and the disclosure done by companies is elaborate, helping build investors' confidence. Anything done by SEBI to help the company build trust is the right move. However, there is a difference in the maturity level of each organisation. If information helps investors identify the value addition in the future, it is relevant and matters. However, if there is isolated information that is in the past and does not affect the future, it should be fine not to disclose it.

The thesis for new-aged companies changes frequently in response to the market dynamics. Thus, the information/metrics that were given earlier may not be relevant. Rather it should be current to build investors' confidence about the current price, prospects.

There needs to be a direction to make regulations more transparent, stick to the roadmap, and should not be based on one-two cases of IPOs.

8. **What are some of the aspects to be considered by CFO and planned to explain the equity story (issue price)? How should companies explain value? Any specific nuance?**

Other than giving guidance and forecast, management always talks about the future. The business story is about future like what is your market, competition, your relative position in the market, growth of the market, and your share of the market. These are enough and more to give confidence to investors and make them understand if the organisation is at the forefront of the industry. If the organisation is able to present the industry overview and show progress on the basis of the business growth drivers is enough for investors to take a decision.

The management's ability to go back and explain how we have evolved as a company, how has the market evolved, and how we are better positioned to take advantage of the market currently is important. That gives a good premise for the company about why it should be valued at a given price.

What are some of the considerations in determining the IPO price?

Various conversations that an organisation had through several rounds of funding give you the base. The price discovery happens in the private funding rounds as private investors would have done due diligence on the organisation, business model, and management. The public market's value will be different from that of the private market; but a private round of investment gives a good benchmark.

The second is the peer group – it is a good way to discover price. Sometimes, the direct peer group is unavailable. The metric that you want to focus on involves growth, EBITDA, and net cash flow. You can use the quality of metrics that is similar to a peer group you create. The peer group benchmark is relevant.

Between the private round of funding and the peer group, you will get a fair view. After that the book building process can help decide the price.

9. **OFS – is it seen with cynicism or as just another way of raising money?**

I see pureplay OFS with scepticism. I would expect investors to look at the companies raising only secondary money more prudently than companies that are raising primary money.

Does this question often asked by investors in meetings/roadshows?

Yes, it is always asked how much a company is looking to raise through primary. If there is no primary, it gives a view that either the company is mature enough to not be able to show growth (in this case, your business doesn't need more capital) or you will have to demonstrate that capital is required to make it a bigger company.

10. What are some of the suggestions you would have to make access to capital easier for Indian businesses? For example, Overseas Direct Listing? How can that become a real option?

There is tremendous interest around the world to invest in the Indian consumption story. If you are India domiciled holding company, there are several tax challenges. If you are a mature organisation, it is impossible to do that. I certainly feel that Indian companies will soon have a direct access to US markets. We need to open up the Indian market for the world. In my view, that will also help retain intellectual property (IP) in India. As a country we would benefit from making direct listing possible.

Suggestions for government

Taxation is not the issue. It is just the mindset that needs to be changed. We need to create a roadmap on where we want the country to go in the next five years, and what are various things we are doing to attract investments and make it easy to do business in India. If all the things are put together and regulated in a structured and consolidated manner, there will be visibility and transparency on how it works.

11. What in your experience are the top five learnings from planning an IPO to being a successfully listed company?

I worry the least about the process – getting the organisation and system, financial, and DHRP ready. For developing the metrics, one will have enough help and will happen and it is just a matter of time and resources. It is not a risk factor in my mind.

One is always underprepared for what happens after listing – what will you do after you go public and what will be quarter on quarter performance?

People are worried about the event. If you have not thought through about the first 2-3 quarters, you are doomed. Therefore, it comes down to your story that you are going to sell which you will have to live after you go public. Both your story and your quarterly results would define whether you will be successful or failure. Many times, management teams don't know. Sometimes IPO give more than 100 percent value in the next couple of months. Is it because you undersold your story or otherwise? If stock tanked that means they oversold.

I am generally happy when what is told as a story converts into consistent and reasonable performance return over the next 2-4 quarters.

IPO readiness: Are you ready to take the centre-stage?

IPO can be an exhilarating and transformational experience in the lifetime of a company. It is a validation of the dream that has turned into a successful enterprise and is a step towards discovering their true value. The capital market is the barometer. It is the capital market that determines the success or failure including the right valuation of an enterprise. However, the process of going public can be complex, expensive, and time-consuming. It will present the management with new challenges, expectations, and stakeholders that are analysts, investors, activists, regulators, and media.

Capital supply is limited. IPO windows are unpredictable. Being ready is the key. Managing a successful IPO listing and being a successfully listed company is an art. It requires early and clear planning and meticulous execution. A few learnings from the recent listing experience are mentioned below.

1. What's your alpha? Given investors' many alternatives to invest their capital, it is vital to have a clear and sound investment thesis. What is the investment opportunity and potential future value your company offers? How will you create long-term value for investors you seek and differentiate it from what competitors offer? How will IPO funds be deployed? Remember, value is an interpretation that investors make of the facts they have at their disposal about *future expectations,* not historical performance. Beware: complexity is the enemy of valuation. Investors seek certainty or at least clarity.

Anticipating investors' expectations and articulating a clear equity story is key to gain their confidence.

2. What information does the street need to value your stock? The market's need for information is insatiable. CFOs and IR must determine what information is needed and when, who will produce it, and how to glean insights to guide the market to their view of the stock. How might investors and analysts value the company, and what models might they use? How are you producing information needed to convey the company's strategy, progress, and story? Is the KPI data book and the controls over its generation consistent and auditable? How is your performance relative to your peers and identify developments that could boost better understanding of your story? The more systematised the process, the more time is needed to analyse data for insights, trends, and KPIs.

3. Are you willing to let go? Launching IPO doesn't mean losing flexibility but it's about accountability. After listing, the governance requirements are enhanced. Some key committees of the board, such as audit committee, nomination and remuneration committee, and risk management committee will comprise a majority of independent/non-executive directors. There would be an expanded separation of management from ownership. Independent director will also have to be appointed on the board of material subsidiary. Have you decided the board composition? Do you have the right-sized board? Do you have the right profile of independent directors? Have you planned the familiarisation event to help members understand operations? Do you understand your own increased responsibilities?

4. What type of investor do you want? When planning your IPO, think about which type of investors best align with your company's investment thesis, risk profile, and capital needs. You also need to consider whether your investment thesis supports these objectives. Do you seek investors with a long-term orientation who desire consistent, steady returns? Or are investors who are willing to forgo short-term returns for long-term growth a better fit? A mismatch of expectations can create volatility in your stock. This needs to be carefully considered in the lead-up to the IPO and roadshow. It needs to be actively managed in the aftermarket. Beware of other investor types that can impact the stock.

5. How clear is your organisation structure and is it aligned with the growth strategy? As you separate ownership from management, a more formal organisation structure will evolve. Newer roles such as investor relationship and stakeholder management will gain prominence. The governance and compliance function will be strengthened. Infrastructure for management reporting and accuracy, including early and timely closure of financial statements and its audit will gain prominence. Do you have an experienced team? Are roles and responsibilities aligned to the new reporting structures? Are their compensation and performance parameters aligned with the growth strategy? Do you need to undertake or plan for any ERP or business information/intelligence upgrade initiative?

6. Have you assessed the capital structure? Many companies would have structured financial instruments, such as convertible debentures/preference shares. Certain privileged rights in the Articles of Association for a few investors/founders. Many of these need to be altered ahead of the IPO. Are sufficient free float shares available? Is the per share value attractive to investors especially retail investors? Have you ensured special/permitted rights to certain investors are compliant? How much dilution is proposed for ESOPs for your employees?

7. Is the group structure efficient? IPO is a time of value discovery. Promoters/founders do consider restructuring of their personal shareholding to facilitate future succession and wealth distribution amongst family members that include facilitating philanthropic objectives. Moreover, if the group structure is complicated, there

could be potential tax leakages. Have you assessed the need for any promoter level restructuring? Is there any business to be carved out – is it tax efficient? What's your effective tax rate? Can it be improved? Are there any ongoing tax litigations? Is there any exposure to shareholders? What are tax obligations on investors?

8. **Are you ready to comply with the financial statement requirement, including audit?** There is general understanding that nothing much is required if Ind AS financial statements are ready. However, it is important to understand that specific reporting requirements need to be included in an offer document - the restated financial statements, the proforma financial statements, use of proceeds-driven financial information, many historical results, and related party transactions. In addition, the comfort letter process which includes a private arrangement between the company, underwriters/merchant bankers and auditors can be complex and time consuming. The comfort letter process demands auditable MIS and non-financial information as close as possible to the IPO date. It is far more than what is included in the offer document. Have you engaged with auditors early? Is there any change in auditors – are all aligned? Are there any independence concerns? Is there sufficient time for review?

9. **How do you address the societal expectations?** There is growing awareness to share the actions taken by companies towards environmental, societal and governance obligations, beyond the mandated requirements. Many investors and funds prefer companies with clear plans and actioned ESG conscience. Are you aware that there are many rating agencies that may rate your ESG readiness? If you don't provide information, there could be assumptions. What are your key investors expecting you to do on ESG? Are you conscientious – how do you propose to explain it?

10. **Is your data room adequately ready before the kick-off?** IPO documents – DRHP, RHP, and prospectus – are legal documents. In India, once a DRHP is filed, it becomes a public document, and any individual can comment about it. There are many examples of delayed or even derailed IPOs, based on the quality in terms of disclosures. Moreover, investor interactions can be based only on the information included in offer documents. There is always a challenge between what all to provide and how reliable is the source and quality of data. Invariably, companies end up providing less information. An early planning and anticipation would enable flexibility. A more ready data room to enable a quicker legal and merchant banker due diligence will also effectively save time and lead to potentially fewer comments during the review process. Simple principle, any information included in the offer document must be fully supported. Have you anticipated what's relevant information? Are you organised the data room to avoid repeat requests or information sought in different forms/format? Is it complete?

11. **Are you ready for the project management challenge?** An IPO involves multiple important stakeholders. The regulator, multiple merchant bankers, legal counsel, international counsels, auditors, topical experts, new board members, investors, research analysts, printers, data room providers, etc. The management bandwidth would be seriously stretched. There is only limited time. Do you have experienced team members who can focus only on the project management and ensure co-ordination? Are they sufficiently empowered? Is there an early sensitisation of the information required from multiple departments? Are the external dependencies clearly identified, responsibilities assigned, and progress tracked?

12. **Are you ready for dual track?** Not each DRHP filed result in a final launching of an IPO. There are many instances in which companies have decided to remain private after the filing. There are many instances of a buy-out from a secondary/strategic investor. A public filing enhances your disclosure and provides additional confidence to a potential investor.

Business scenarios can change from the time of decision to go public. Are you open to explore the flexibility? Can IPO wait for that little extra time that will make it more attractive? Are you feeling compelled? Like many business decisions you need to have an open mind to be flexible.

13. **Are you ready to sign off on Internal Financial Controls (IFC)?** One of the often confused area is IFC. In India, an auditor is mandated to report on the internal control over financial reporting – that is limited largely to the financial reporting controls and its effectiveness *as-at the reporting date.* It is also thought that an internal audit is sufficient compliance of the obligation. However, IFC also covers operational controls and security of assets, including data, cyber security, and enterprise-wide risk, including strategic risk faced in areas such as marketing and operations, fraud risk, information security risk, compliance with laws and regulation across the group. The CEO and CFO are required to provide sign-off on its design and operating *effectiveness throughout the year.* Does your functional team understand this increased responsibility? Are there processes in place to provide the necessary comfort to the audit committee?

14. **What message will you send to the street post IPO?** One of the key benefits of an IPO is the flexibility to raise further equity at a shorter notice by way of private placement with qualified institutions. Thus, the pressure to manage investor perceptions may increase in the aftermarket. After the IPO, the CFO and other leaders must continually monitor investors' sentiment towards the company and sustain its story in the marketplace, routinely providing information and leveraging analysts and media to help create demand for the stock – especially in the event of a crisis. With the transparency of information and social media, investors can easily punish the stock of a company that takes too long to address a negative event. Do you know how your decisions, culture, and behaviour support the value proposition to investors? What data and insights help demonstrate to investors that their stock is a solid investment? How frequently are you planning to interact and are the questions being addressed? Who will execute this strategy to build shareholder value?

15. **Do you have a strong investor relations team?** Does the team have clarity on the compelling investment thesis – defining the desired investor base that aligns with your thesis and risk profile, assembling relevant and timely information and insights to guide investors towards the management's view of the stock's value, telling a compelling and credible story to the street, and managing investor perceptions in the aftermarket. How well that's done can significantly impact the stock's valuation during the IPO and overtime. As a company's business strategy evolves, its investment thesis may change. However, it should remain the cornerstone of how CFOs and other executives communicate with the street. Periodically, consider re-evaluating what makes the company an attractive investment with facts to support your views.

The Indian capital market is coming of age. The recent tech-based/new-generation businesses IPOs have shattered the myth that Indian stories must be told in the overseas capital market. We are at the cusp of a potential change with the untested equity stories and their unconventional valuations successfully entering the Indian capital market. The excitement can be sensed by the quantum of over-subscription. Beware, per se it may not indicate the true depth of available liquidity. These may be short-term flows, moving from one opportunity to another. Liquidity doesn't mean cheap money.

More the IPO stories, larger the capital market, and larger and deeper it gets. It in turn will support many more dreams and enterprises. India is blessed with talent and being ready is the only thing in the hands of the company. Nothing gives more confidence than a clear plan and an eventual successful IPO.

India progressively opened up for foreign investment in various sectors from 1991. The trend over the period demonstrates that Indian entities that had foreign investment, had either exited in a private deal (to a strategic partner or a private equity player) or had a public issue to raise further capital and give an exit to investors. Moreover, this trend is not uncommon for purely Indian-held companies.

Historically, the Indian Public Issue (IPO) was the only option for an Indian company to raise funds from the public. For an IPO, multiple compliances and conditions need to be satisfied; critical amongst them being profit track record. Further, 100 percent of the pre-IPO work must be done before launching an IPO. These compliances and conditions make the entire process onerous, expensive, and time-consuming with no certainty of outcome.

However, fundraising through IPO touched a record high in 2021, raising more than US$157 billion. This number itself justifies the efforts that need to be undertaken for an IPO.

Due to an onerous process, many foreign investors explored options to list an Indian company overseas. What could not be done directly in the absence of regulations, was done indirectly. At present, Indian regulations do not permit an Indian company to directly list overseas, though there was some discussion on that in the past. Further, a dual listing of an Indian company’s share is not permitted under current regulations.

Interview with Sumit Zaveri, CFO, Burger King, India

1. **You recently concluded successful IPO (Initial Public Offering) and then QIP (Qualified Institutional Placement) rounds of funding. In your words, what are the few things that you did right?**

I will start with the background of our company to answer your question. We are a Private Equity (PE) funded organisation. In some time, PE investors would look at exiting from investments for the value. Existing investors expecting value delivery is one of the primary reasons for most organisations. It was one of the reasons for us as well.

As for our company, we opened our first store in 2014 in India. We knew that if we want to establish ourselves as a brand we need to grow rapidly. Using the initial capital by promoters, we grew and became one of the fastest-growing Quick Service Restaurants (QSR) in the country. We opened 200 stores in the first five years. Our journey until 2019 has been fierce. As an organisation, we believed that if we want to raise capital in the market, we need to show our growth story but at the same time grow sensibly and demonstrate it to the market by being profitable.

Our aspiration was to grow to 700 stores by December 2026. Besides providing exit to our investors, when we started the IPO process, our purpose was to raise capital to fund our growth. We sized our IPO accordingly. When we went to IPO, we were at 250 stores and had to do another 450 stores to reach our target. With an average investment of INR 2.5-2.6 crore per store, we would have needed INR 1100-1200 crore. We raised INR 600 crore through IPO and incrementally we needed

INR 500-700 crore to fund our growth. Our objective was boosting growth through IPO. Growth we will achieve with new investment should then further support us achieve our target through internal business cash injections.

Thus, we created a balance by funding growth through a combination of IPO and cash/profits generated from new stores that helped us create trust with investors and worked in our favour.

2. **During COVID-19, you did QIP that was twice the price of your IPO. What would you attribute the success of QIP to?**

During both the processes, IPO and QIP, we learnt that investors are effectively looking at investing in the people who run the business. Both the times we approached the fund raise driven by the management. The management talking about business works really well and builds investors' confidence.

Second, we focused on providing visibility to business growth and explained our approach to growth to investors. We changed the way information was shared by other QSRs. We also provided comfort to investors that we will improve the transparency with which we would share our information. We shared Quarter-on-Quarter (QoQ) performance, including parameters such as average daily sales and dining vs. delivery share of revenue to help investors understand our business.

Third, we were amongst the first ones in the QSR industry to give guidance that was relatable. We provided our guidance on three premises – sales, growth, and gross profit improvements. Even for our first quarter results after the listing, we gave a clear guidance on what our growth would look like, gross margin improvements, average daily spends, and our café opening plan.

So, since the beginning, our focus was on sharing the past performance in a transparent way, providing guidance on future, and then meeting our guidance. These three things worked in our favour to build confidence and trust with investors.

3. **What were some of your learnings from the IPO process? What would you do differently on the basis of your experience?**

If I have to look at it from the Indian market perspective, investors look at business performance in a restricted view where profitability is given significant importance. Our regulators, SEBI is also trying to make amendments to it. Indian investors especially after listing give high weightage to profitability. There needs to be more maturity in the market to look at growth business concepts in a little different light.

On the regulatory side, there are limitations in providing forward-looking statements for the organisation. It is difficult to tell your story using past performance instead of looking at the future growth. How does one explain growth on the basis of the past performance? How would one raise growth capital by providing investors with the explanation of the past performance?

In my view with our two different capital raising experiences, the organisation should approach investors with humility and transparency. Irrespective of the size of the investments an investor makes, meeting investors is an opportunity for the company to present itself, talk to investors, and explain the organisation's story and business.

One of the major factors in the decision of investment is the confidence on the management and these interactions with investors help build that trust and confidence.

4. **Some of the common challenges for IPO companies are audit readiness, quarterly audited, monitoring of KPIs, ESOP, segment reporting, internal controls, etc. In your opinion, what are some of the important issues?**

I would like to put the issues/factors in two main segments – finance and regulatory.

- Finance theme
    - The rigour of structured closing before one decides to go for IPO - Closing as a process

- **Expectations from finance as a team -** Get the team ready who can ensure the requirements are met
- **Managing expectations -** Make people understand what is expected out to them; we started working on getting the expectations right a year and half before our IPO process
- Detailed discussions and **deep dive in numbers** much before the IPO
- **Identifying and bridging the gap in the skillsets** by adding team members so that we can deliver per the expectations - compliance and risk management

- **Regulatory theme**
  - Several regulations become applicable after listing - **Rewrite/create some of the policies, such as ESOP and materiality clause**
  - Creating a culture **that identifies the importance of confidentiality,** including relevance and understanding of price-sensitive information and insider trading regulations
  - Training and getting the team ready for various regulations that apply to the organisation for listing and ensuring that **systems and policies comply with the regulatory framework**
  - Preparing and **sensitising the entire organisation for the implications of post listing requirements**

5. What percentage of your time was spent on preparing financials vs. analyst interactions?

When we were preparing an organisation, the substantial part of my time was spent on preparing the document. Simultaneously, we also worked towards preparing the organisation for the IPO. After filing the document, a substantial time was spent on meeting investors and analysts to talk about our story.

In my view, the time spent on preparation and analyst interactions was sequential rather than running both in parallel.

6. How much of your time was spent on getting the next six to eight quarters right? How much of forward-looking readiness should a company be prepared for?

In my view, two aspects are important – growth and business performance metrics, such as profitability.

For growth as one of the levers, it should be about medium-to-long-term view so that expectations are well understood. Growth story would depend on the organisation’s overall aspirations. Organisation must show how effective they are on their foresight for the next two–three years. Most analysts look at two–three years to build their own models and stock markets look at 12-24 months forward multiple to value companies. Therefore, in my view, providing a business perspective for a longer time, such as two–three years, is critical.

On business performance metrics, it should be on a QoQ basis so that you are able to show improvement.

The visibility on business performance at a short interval is important but a longer horizon would be the key to understand the business.

Does the focus change after IPO?

When we have to announce results on a QoQ basis, one must ensure there is no variability. Also, it should not be made up performance. Therefore, an organisation must tell its investors the key performance metrics/parameters that it wants investors to evaluate itself on. In parallel, providing visibility about the long -term growth path is important. For example, QoQ profitability is one of the metrics. As an organisation, we used improvement in gross margin vs. store EBITDA as one of the key performance metrics. We created the metrics that was more relevant to the organisation vs. having the metrics for which we have to worry on.

At present, how much of your time spent is on maintaining the investor and analyst connect?

At present, 20-30 percent of the time is spent on meeting investors and building the connect. This time allocation also depends on the organisational structure. We also have an investor relations representative as part of our structured business effort. It is an organisation's decision on how much and how effectively they need to connect with analysts and investors. If you have an investor relations team, it must understand business. Although organisations have the investor relations team, they should ensure transparency so that the team is able to understand and get the information about the business. In my view, for CFO/ Head of Finance to spend enough time on business finance, a separate investors' relations function is very important. But it is team effort. In our case, CFO, CEO, and the investor relations team together met analysts and investors.

7. Based on your experience, what is the key role of CFO in explaining the equity story and define the issue price? How should companies explain the value?

In our case, it was slightly easier because our promoters were PE investors. When we went for IPO, the management decided on a book building process and let the market decide the price of the issue. Moreover, promoters continue to hold more than 40 percent of the capital in the company. If you list your share at the fair price and subsequently able to support your business story through growth, it is a good sign for the market. It gives a clear understanding that IPO is priced fairly and based on the right valuation from bankers and investors and is not a full exit. If the organisation can demonstrate that the business will generate capital appreciation for investors as a larger community, eventually the company will be able to derive the fair price from investors.

Qualified Institutional Placement (QIP) is driven by a formula. However, we offered a relevant discount to ensure that pricing is reasonable to investors. Subsequently, we were able to add value to investors. We believed that the price needs to be closer to investors' expectations. But we also need to ensure that we are not underplaying the growth story.

We followed two principles that include showing consistent growth to investors after the capital raise and setting a reasonable price for investors.

8. Recently SEBI has issued a consultation paper seeking more disclosures about KPIs, including its audit. What are your thoughts or suggestions? How should companies price their IPO?

I feel that there is a need to relook at regulations. As a country we have done good work and made changes in the past couple of years. A few things I believe would be relevant are:

- There should be a distinction for growth capital. There is a change in regulations required when capital required is for the growth phase. For example, I feel that new-age businesses, such as Policy Bazaar, Zomato, and Paytm, do not have the right mechanism to value them. We need to relook at the regulations differently as more such companies would come to market for capital generation.
- How do you share information to help investors take informed decision because forward-looking statements are not allowed? There is no mechanism to share forward-looking statements. For example, in our business we can share the number of stores we will open but how much revenue it will generate for the business is not something that is shared. That will help investors to ascribe value to businesses.
- Third, putting loss-making companies in the same category is not right. There could be companies such as new age vs. long gestation companies, including infra companies. Putting the business together is not necessarily the right way to look at it. We have to find a balance somewhere.

Which are the three improvements to the IPO process that you would recommend?

- How do you enable growth businesses to tell their stories when they approach investors?
- Clear directive for valuation based on the type of capital raise (growth vs exit): if it is substantial OFS, valuation principle should work on historical statements. If the capital raise is for growth, valuation principle should work on the forward-looking statement.

9. Your IPO was a combination of primary and OFS. OFS is seen with a lot of scepticism. What are your views on it?

OFS is seen with scepticism but in my view if the organisation can demonstrate value appreciation plan post listing, it creates confidence with the incoming investors.

OFS must be there or not there – that isn't the question. The question is if you exit your investment, how you demonstrate the faith in the business that will be important for incoming investors? In our case, promoters continue to hold more than 40 percent, indicating confidence in the business. The management needs to demonstrate that they are not dumping the business and continue to be part of the business and believe in the growth story.

"No one is better than the management team that can demonstrate/create faith in the minds of investors, and it is critical."

10. How soon a company should start the IPO process and prepare itself?

I feel that a company needs to start at least 9–12 months earlier. This would require preparing the business and aligning the entire company for being a listed entity.

Second, prepare your organisation's story with which you will approach investors.

Third, getting the right set of people on the job such as lawyers and bankers (at least six months before filing) and taking the effort that they understand on what you stand for is critical. That is where the maximum amount of time should be spent. For the selection of people, it would take minimum six months as getting the right bankers who understand the organisation's perspective, is important. Getting the right people to manage the process efficiently would be another important aspect.

Listing on an overseas stock exchange

It was observed that it was easier to list an Indian company indirectly on an overseas stock exchange due to foreign investment regulations. The said regulations permitted investment in an Indian entity under:

1. Foreign Direct Investment ("FDI") route
2. Foreign Venture Capital Investment ("FVCI") regime, for investments made by SEBI-registered FVCI
3. Foreign Portfolio Investor ("FPI") regime, for investments made by SEBI-registered FPI
4. Non-Resident Indian ("NRI") regime, for investments made by NRIs and persons of Indian origin

Most overseas investors preferred to have a special purpose vehicle (SPV) set up in an overseas jurisdiction that invested in an Indian company. Further, if the promoter of the Indian company were non-resident, the promoter held his/her investment outside India. In this situation, it was easier to list overseas the SPV directly in an overseas stock exchange that was effectively valued based on the underlying Indian operation. However, if promoters were Indian residents, their shareholding was directly held in India. They were not able to capitalise from an overseas listing.

There are many examples of an overseas SPV listing on NYSE, NASDAQ, London Stock Exchange, etc. In such cases, compliances and the process were run for the overseas SPV, coupled with its underlying Indian operating subsidiary. To overcome the pressure of processes and uncertainties, as well as incentivise another listing option, SPAC was introduced a few years ago that has suddenly perked the interest of eligible suitors.

A Special Purpose Acquisition Company ("SPAC"), commonly referred to as a "blank cheque company", serves as an alternative way for private companies to enter public markets and give the public access to more early-stage growth companies and private equity-like investment managers. The process is divided into two parts, raising the blind pool of funding by completing 40-50 percent of the compliance requirements. The remaining compliances are done after raising funds and before utilising money, in a method known as D-SPACing. The funds raised are kept in an escrow account until the completion of compliances and processes. It is not a shortcut to listing but is an alternative that has found fancy with new-age businesses that are unable to comply with conditions such as profit track record, etc.

SPAC provides flexibility for promoters to go down the offshore listing route, without actually listing an Indian company. In the US, SPAC outpaced the traditional listing. In 2019, there were 59 SPAC listings that went up to 613 SPAC listings in 2021, raising more than US$ 162 billion. SPACs now account for roughly 70 percent of all US IPOs above US$50 million. The number of SPAC mergers has also increased significantly. There were 28 mergers in 2019; the number rose to 199 mergers in 2021. In terms of value, it increased from US$25 billion in 2019 to nearly US$470 billion in 2021. High-tech companies have been the prime target for SPACs followed by healthcare. SPACs that were traditionally more US-focused are now increasingly looking at targets outside the US, including in Asia and Europe. Only one SPAC has been liquidated (wound up) in 2021, compared with two in 2020 and five in 2019. This signals a strong trend that shows that SPACs have been able to close their initial business combination instead of liquidation.

In case of SPAC, the time to market is less compared with a traditional IPO, which is a major benefit. The route to traditional IPO is a long one and companies start preparing for it 12–18 months in advance. Traditional IPOs are also subject to market fluctuations. Numerous IPOs have either been deferred or squashed in the past, on account of adverse market conditions. A SPAC transaction can be completed in months, thereby avoiding exposure to market fluctuations.

Overseas markets are more mature for new-age technology start-ups and e-commerce companies; such companies command good valuation that otherwise could be difficult to get in India. The ecosystem in India for such new-age companies has not yet evolved from a retail investor's expectations and applicable regulations' perspectives. The recent listing of some new-age businesses shows that there is still some time before they too catch wind of Indian retail and institutional investors.

There are various nuances/aspects that one will have to look closely, in the whole process, especially from the Indian tax and regulatory perspectives, regarding Indian promoters holding shares/units of a foreign entity that, in turn, holds an Indian company. Round tripping of investments, restrictions for sending funds to hold sponsor shares, and capital gains tax on swap of Indian company shares for listed SPAC shares, along with Place of Effective Management (POEM) consequences for Indian residents managing the SPAC structure, are some of the regulatory and tax challenges that behold the SPAC structure to show its full potential for an Indian promoter-driven company.

Depending on the facts of each case, a regulatory compliant and tax-efficient structure could be explored for each SPAC, and more importantly at the time of De-spac where transfer takes place.

It is important to give a reference to the Security Token Offerings (STO). STOs combine the technology of blockchain with the requirements of regulated securities markets to support liquidity of assets and wider availability of finance. STOs are typically the issuance of digital tokens in a blockchain environment in the form of regulated securities. They are essentially the digital representation of ownership of assets (e.g., gold and real estate) or economic rights (e.g., a share of profits or revenue). It is an upcoming method to initially raise a few million dollars for early-stage businesses planning to grow in the financial or technology sector wanting. Until now only a few countries, such as the US, Germany, and Singapore, have activities happening around STO and regulations around it. India is yet to come out with regulations on STOs.

Multiple avenues have traditionally been explored by Indian promoters and companies in the past for raising funds. Overseas listing, SPAC route, and STOs are upcoming avenues that offer existing opportunities to tap a larger pool of investors globally and in turn, command attractive valuation.

Connect with us

Uday Bhansali
President – Financial Advisory
Deloitte Touche Tohmatsu India LLP
udaybhansali@deloitte.com

K. R. Sekar
Partner, Deloitte Private Leader
Deloitte Touche Tohmatsu India LLP
krsekar@deloitte.com

Acknowledgements

Sunder Iyer, Vikas Bagaria, Hemal Mehta, Sandeep Negi, Rishabh Jain, Rumki Majumdar, Gagan Sharma, Rinki Goel, Megha Agarwal

Deloitte.
Private