



# PERFORMANCE OF INDIAN SME IPOs

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## Abstract:

*The SME platform has now established itself as the most cost-effective means for SMEs to obtain finance and get awareness. The current study aids us in comprehending how IPOs support SMEs. It is valuable in determining the relevance of SME exchanges and determining the impact of initial public offerings that were issued and listed on the BSE SME and NSE EMERGE platforms during Covid'19. According to the report, this platform is gaining traction as the number of issues listed on such platforms grows with time, which is about 6.33 crore, which is remarkable. The need of the hour is for industry players, government policymakers, and businesses to collaborate to allow SMEs that have been left behind to become digitally empowered.*

## Keywords:

*NSE EMERGE, BSE SME, Financial Literacy, Under pricing, IPOs, Prospectus.*

## 1. INTRODUCTION

An Initial Public Offering (IPO) is a mechanism for a company to raise capital publicly for the first time in exchange for equity shares in the company. For expansion a business requires capital for which there are two options; Bank Loans or raising funds from the general public. A firm may use an IPO while raising funds from general public that offers a portion of their ownership to potential investors. In order to become eligible for an IPO the company must register with SEBI and employ underwriters to help with the sale process. Following SEBI's approval, the IPO is made available to individual investors.

Furthermore, after the IPO issuance is completed, the business's shares are listed on the National Stock Exchange and the Bombay Stock Exchange, making it a publicly traded corporation. SME IPO is a separate method of acquiring cash for small businesses inside the IPO process.

Small and medium businesses, or SMEs, are businesses with low investment and turnover.

<b>Classification</b>	<b>Investment Amount</b>	<b>Turnover Amount</b>
<b>Small Enterprise</b>	1 crore - 10 crore	5 crore - 50 crore
<b>Medium Enterprise</b>	10 crore - 20 crore	50 crore - 100 crore

SME IPOs, like any other company's initial public offering (IPO), are intended to raise capital for a small or medium-sized business. Because SMEs are much smaller than larger corporations, the SME IPO has a smaller issue size than a typical corporation's IPO. SME enterprises are not listed on the Bombay Stock Exchange or the National Stock Exchange due to their small size.

SME's (Small and Medium Enterprises) are the backbone of India's rapidly growing economy. A SME exchange is a specific exchange or trading platform for Small and Medium Enterprises. The BSE Limited and the National Stock Exchange of India are examples of SME exchanges that operate within a recognized stock exchange or the major exchange in India.

SEBI originally published the framework for establishing SME exchanges in 2008. The report on Micro, Small and Medium Enterprises by the Prime Minister's Task Force in January 2010, which suggested the establishment of SME exchanges to stimulate the entry of equity capital into this sector, was a key step in this direction. In 2012, the BSE and NSE created the SME Exchange, a listing and trading platform for small and medium-sized businesses. SME listing benefits not just the companies, but also their existing and potential investors, such as offering an exit option for private equity investors and liquidity to ESOP holding workers. Good corporate governance is a prerequisite for listing, as it ensures the company's long-term viability and aids in the development of an impartial valuation. Customers, suppliers, investors, financial institutions, and the media all benefit from a company's public listing, which also offers stockholders with continuous liquidity. Since then, many businesses have taken advantage of the option to be listed (302 companies in first 5 years).

### **ELIGIBILITY CRITERIA FOR SME IPO**

The company must be incorporated as a public company under the Companies Act, 1956 or 2013, or the business must be converted into a public company for purposes of listing. In India, there are currently just two SME exchanges: the BSE SME platform (BSE) and the EMERGE Platform (NSE), both of which have their own eligibility criteria for SME listing in addition to the SEBI Guidelines.

#### IPO Listing Criteria for BSE

1. Post-issue Paid-up Capital: The post-issue paid up capital of the company shall be at least Rs. 3 crore.
2. Financials:
  - Net worth: As per the latest audited financial results, the company should have net worth (excluding revaluation reserves) of at least Rs.3 crore
  - Net Tangible Assets: At least Rs.3 crore
  - Track Record: For at least two years out of the previous three financial years, distributable earnings as defined by Section 123 of the Companies Act 2013 (each financial year has to be a period of at least 12 months). Extraordinary income will not be taken into account for determining distributable profits.

OR

The net worth of at least Rs.5 crore is required.

3. Other Requirements:

- The Company shall have a functional Website.
- There should be no change in the promoters of the company in the preceding one year from the date of filing the application to BSE for listing under the SME segment.
- The company shall facilitate trading in DMAT securities and enter into an agreement with both depositories.

### IPO Listing Criteria for NSE

1. Post-issue Paid-up Capital: The post issue paid up capital of the company (face value) shall not be more than Rs. 25 crore.

2. Track Record:

- The company should have track record of at least 3 years.
- The company should have positive cash accruals (earnings before depreciation and tax) from operations for at least 2 financial years preceding the application and its net-worth should be positive.

3. Other Requirements:

- The Board for Industrial and Financial Reconstruction has not been directed to the applicant company (BIFR).
- No petition for winding up against the applicant Company has been accepted by a court of competent jurisdiction.
- No major regulatory or disciplinary action taken against the applicant firm by a stock exchange or regulatory authority in the previous three years.

### Objectives of the Study:

In light of current available research, the study seeks to explore certain qualitative elements of SMEs IPO in Indian Equity Market:

- To assess the importance of SMEs exchanges in India.
- To study the trends of SME IPO in Indian Equity market.
- To examine the impact of Covid-19 on Indian SMEs and their financial performance.

### Literature Review

(Rao, Kumar, Gaur, & Verma, 2017) The purpose of this exploratory study is to look at the funding challenges that Indian SME owners confront. It also divides the finance problems into four categories: demand, knowledge, supply, and benevolence. The study uses the convergent interviewing technique to highlight the primary challenges that SME owners encounter when it comes to funding. In the study, forty-four business owners from various industries and demographics were questioned. The findings indicate the difficulties that SME owners are now dealing with. SMEs were hampered on both the demand and supply sides. High credit costs, complicated lending procedures, information asymmetry, creditworthiness, and self-sufficiency in external financial resources are the most prevalent financing problems. The researchers have also observed issues related to a lack of information and awareness regarding financial products and services.

This study explores the financing preferences and practices of 309 small and medium-sized companies (SMEs) in India's northwest region using survey data. It also looks into the variances in financing preferences based on firm and owner/manager characteristics, as well as the factors that influence financing practices in India. Internal funds are preferred by respondents, who also prefer bank financing, primarily in the form of long-term loans and funds from government and financial institutions. SMEs prefer trade credit above funding from

family friends, relatives, and money lenders when it comes to informal sources. External equity is the least desired source of funding. By analyzing SMEs' funding choices and practices and revealing a financing gap, the study adds to the existing literature on SME finance. (Baker, Kumar, & Rao, 2017)

(Kumar & Rao, 2016) The goal is to present a complete picture of India's small and medium enterprise (SME) finance situation. It examines the financial ratios of SMEs and the components of debt from 2006 to 2013 using data from the financial statements of 1524 SMEs provided by the PROWESS database of the Centre for Monitoring the Indian Economy. The study examines disparities in SMEs' financing patterns across business variables such as size, age, ownership, sector, and area. The main findings revealed that SMEs are heavily reliant on short-term debt, with trade credit and bank loans being the most common sources of funding. Hierarchical regression analysis revealed that the major determinants of the capital structure of SMEs are age, profitability, tangibility, and liquidity. Overall, the report indicates that the funding situation of SMEs in India has to be improved, and recommends that new finance routes specifically tailored to address SME financing issues be explored.

One of the greatest barriers to SMEs' growth is a lack of access to capital market finance. SMEs have their own platforms, boards, and exchanges in around 30 economies. In 2012, India took a significant stride forward by supporting SME platforms on both the BSE and NSE stock exchanges. In terms of luring SMEs for both listing and trading, the BSE is currently the obvious market leader. Because 2,183 firms have been listed on the TSX Venture, the stock markets of developed economies such as Canada (TSX Venture) could be regarded the world's premier exchange for growth stage/SME enterprises. BSE Emerge is doing well and will shortly reach the milestone of 200 listings on its board (before the end of 2017). In this context, the current paper evaluates the state of SME platforms in India. (Madasu, 2017)

A new program to fund SMEs through initial public offerings (IPOs) was recently launched, and the response has been favorable and encouraging. The secondary market for SME IPOs has done exceptionally well. The entire process, however, is riskier for investors due to the low liquidity and turnover. This is why SEBI (India's stock exchange regulator) has given recommendations, yet this has resulted in a severe liquidity deficit. The effectiveness of SME financing through an initial public offering (IPO) is examined in this article, as well as the success of firms that have raised cash in this manner. Investigating how stock exchange engagement, where these firms are listed, may give long-term support to their managements. (Sharma & Gupta, 2018)

(Dhamija & Arora, 2017) used multivariate analysis to discover that the kind of offer, issue size, promoter ownership, level of oversubscription, lead management status, and stock exchange of listing are all important drivers of SME IPO under pricing. These first public offerings have consistently outperformed the benchmark index since their initial public offerings. Other research on the main board exchange has indicated that IPOs underperform the markets on average for a long time after they are listed. This might be because particular equities are traded infrequently, resulting in lesser liquidity. Stock exchange regulators, issuers, and investors will all be affected by the results. The goal of this research is to evaluate and compare the price discovery efficiency of SME IPOs to that of Main Board IPOs using underpricing methodology. Between 2000 and 2019, a total of 1110 initial public offerings (IPOs) were listed on the BSE, NSE, and their SME Platform, including 526 SME IPOs and 584 Main Board IPOs. According to the findings of this study, SME IPOs are more efficient in terms of underpricing. Furthermore, despite the high chance of listing day profits, SMEIPO demand is lower than that of their bigger counterparts. (Wazal & Sharma, 2020)

The purpose of this study is to look at the impact of underwriter reputation on under pricing and long-term returns of small and medium-sized enterprise (SME) initial public offerings (IPOs) over a 12-month period in an emerging country like India, using a sample of 403 IPOs that were issued between 2012 and 2018 and later listed on the BSE SME platform and NSE EMERGE. However, due to the move of 27 SME IPO businesses to

the main platform, the sample size for analyzing long-term performance has been reduced to 376 IPOs. To analyze the relevant link, the current study used the ordinary least square regression technique. The findings' robustness was further assured by utilizing two-stage least square regression to check for endogeneity bias (2SLS). The findings show that while underwriter reputation has a good impact on SME IPO under pricing it has no substantial impact on their long-term performance. This study could provide useful information to politicians tasked with reforming the Indian stock market. The data may provide some insight into the necessity of employing reputable underwriters in the IPO process for SME issuers. The findings could help investors improve their equity valuation and make more educated investment decisions. (Arora & Singh, 2020)

(Ghalke, Kumar, & Rao, 2022) Access to affordable funding at the right time is crucial for the growth and survival of small and medium-sized businesses (SMEs). The goal of this research is to look into the effectiveness of newly established SME exchanges in helping Indian SMEs expand. The impact of obtaining public equity capital on a company's growth prospects, capital structure, and credit profile is examined in this study. The cost and speed of obtaining capital on specialist SME markets against the main board are also examined. To evaluate the impact of growing public equity capital, this study uses a difference-in-difference (DID) regression approach. SMEs that raised funding on the SME market between 2013 and 2018 make up the treatment sample. According to this study, when a firm gets listed, its overall debt lowers. SME financing costs do not change as a result of the IPO, according to this study. Finally, our analysis reveals evidence of a sales growth slowdown following the IPO, indicating that firms are utilizing the IPO cash to rebalance their accounts after a period of significant investment rather than for growth financing.

## 2. MATERIALS AND METHODS

An explanatory research has been done on the subject of Indian SMEs IPO. The analysis was derived from data of MSMEs' Annual Reports, the BSE SME and BSE website, the NSE EMERGE platform and 4th MSME Census, the National Sample Survey Organization 73rd round, various journals and other sources. To arrive at the conclusions, secondary data from numerous papers and previous work on the subject was reviewed. Because data for different factors was available for different years, the study was conducted from 2018 to 2022. The data will be used to carry out a case study analysis.

### Hypothesis Statements

- BSE SME IPO performance in relation to BSE IPO
- There is impact of Covid-19 on Indian SMEs IPO.
- There are advances in IPOs of Indian SMEs.

## 3. RESULTS AND DISCUSSIONS

SEBI has conducted extensive consultations with all stakeholders. In compared to the main board, the SME platform should be more cost-effective and have less compliance requirements. As a result, the SME Board's regulations have loosened guidelines and compliance requirements so that SMEs may easily comply with the low-cost burden. The submission of half-yearly results and shareholding pattern is required on the SME platform. They are also exempt from publishing their statements in the newspaper. When it comes to migration to the main board, the company's face value capital must be greater than Rs 10 crore, and the market cap must be greater than Rs 25 crore. Aside from that, the firm must get two-thirds non-promoter approval.

In addition to the SME platform, BSE has created a barometer index called BSE SME IPO to measure the performance of SME IPOs in the secondary market. The index was introduced on December 14, 2012, and began trading on January 18, 2013. The BSE SME index had a massive increase of nearly 10,500 % from the start of trade till March 2022, which is much greater than gains in other Indian stock indexes. Fig. 1 shows the performance of the BSE SME Index in contrast to the main index, the BSE Sensex:



Figure 1 BSE SME IPO Performance

Source: BSE Website

MSMEs are encouraged to sell their products on e-commerce sites, particularly the Government owned e-Marketplace (GeM) where Ministries and PSUs (public sector undertakings) get their procurement. The GeM portal had completed 8.16 million orders worth 159,483 crore (US\$ 21.38 billion) for 55,929 buyer groups from 3.1 million registered sellers and service providers as of November 26, 2021. To provide enough liquidity in corporate operations, domestic company requires a large financial stimulus, including concessional working capital loans from the government and banking institutions. MSMEs (Micro, Small and Medium Enterprises) in India are quickly choosing digital payments over cash, with 72 percent of payments made via digital against 28 percent via cash. The rise in digital usage offers opportunities.

After a slowdown in 2020 due to the pandemic, offers from public share sales of small and medium companies (SMEs) enjoyed a recovery in 2021. In 2021, SMEs raised Rs 787 crore from 59 offers, which is 4.7 times the amount raised in 2020 from 27 offerings. This is still significantly less than the all-time high of Rs 2,409 crore in 2018 and Rs 1,738 crore in 2017. According to analysts, the number of issuances fell in 2020 as investors chose larger companies that were seen as more robust during the epidemic to risking their money on smaller enterprises. According to IBEF, the BSE SME (small and medium enterprises) platform is projected to see more than 60 SMEs enter the market in one year (2021-22) to raise equity financing for their business needs. In 2020, 27 SMEs went public through the initial public offering (IPO) route, raising Rs. 168 crore (US\$ 22 million).

Year	Number of IPOs	Amount Raised (Rs Cr)	Successful IPOs	IPOs
2012	14	127	14	0
2013	34	362	34	0
2014	40	289	40	0
2015	43	275	43	0
2016	67	555	67	0
2017	135	1,738	133	2
2018	144	2,409	141	3
2019	54	657	51	3
2020	27	168	27	0
2021	59	787	59	0
2022 *	18	289	18	0
<b>Total</b>	<b>635</b>	<b>7656</b>	<b>627</b>	<b>8</b>

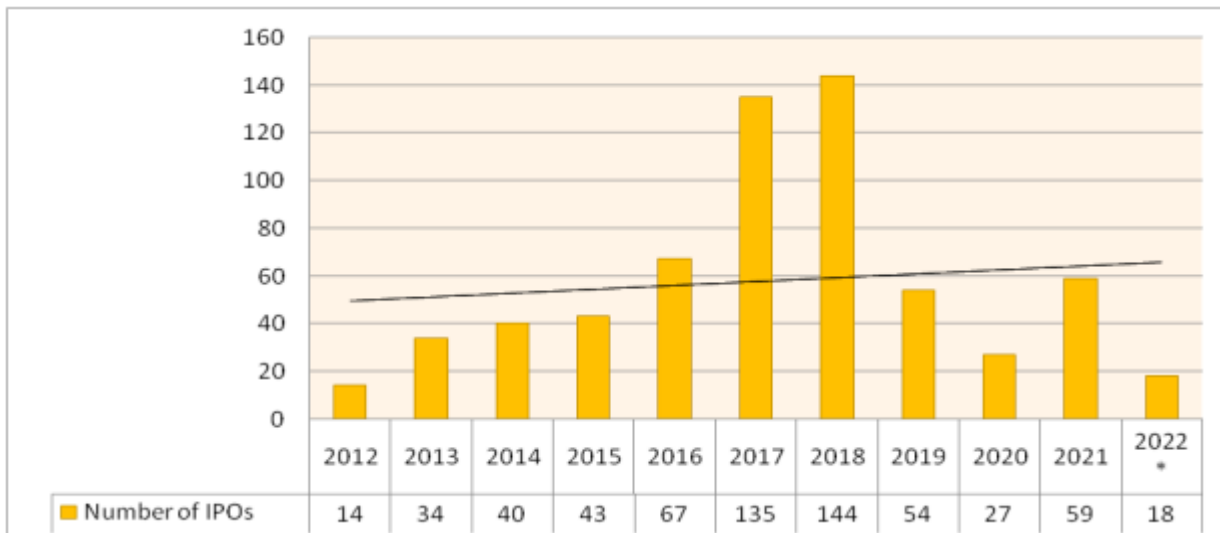


Figure 2 Number of IPOs raised in Indian Equity Markets

It has been actively serving its objective since its inception in 2012. During all the 10 years, the two platforms (NSE EMERGE and BSE SME) raised a total of 7656 crores. Fig. 1 show how the number of initial public offerings (IPOs) has increased over time, broadening the market's base.

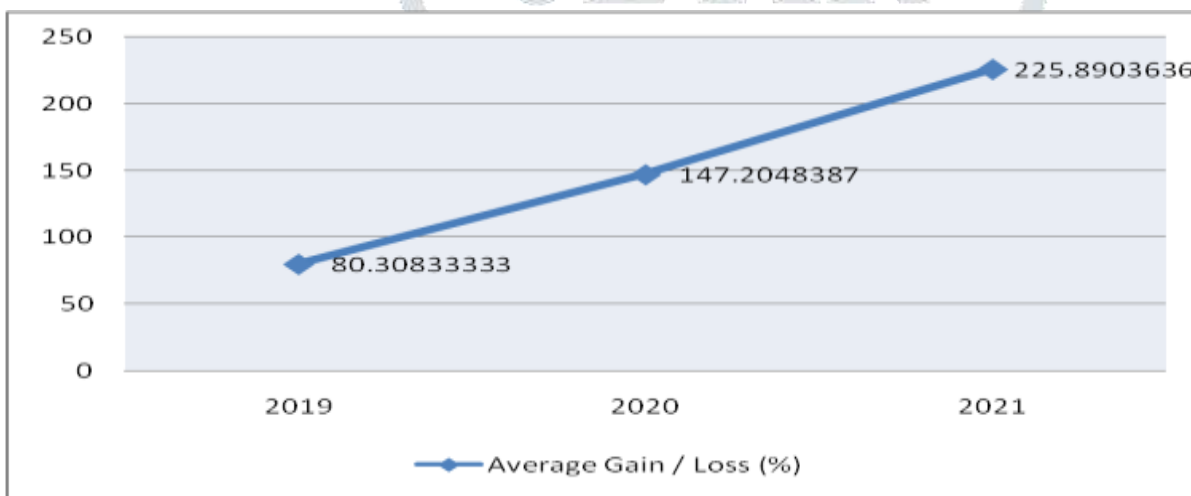


Figure 3 Average Gain/Loss (%) shown by SMEs in last 3 years

The average gain increase from the time of listing till 2021 was remarkable for a number of firms listed in the recent three years (i.e. 2019, 2020, and 2021).The preceding data clearly reveal that the majority of firms have seen exceptional revenue growth after their IPO. It indicates that by raising capital through an IPO, they were able to increase their gains significantly. It's also proof that firms gain exposure in the eyes of customers once they become public.

According to the National Sample Survey Office, there are around 6.33 crores small and medium-sized businesses in the nation. But over the past 10 years, only 627 small and medium-sized businesses have been listed to date. The three primary areas that have seen the most SME issuances are information technology, textiles, and financial services. It's a no-brainer for IT and financial services companies to take advantage of the primary market since new-age technology companies have more transparent procedures, making it easier for them to fulfill disclosure standards than companies in more conventional sectors. As a result, SMEs must be educated on how to take advantage of the capital market and how it may assist them raise cost-effective financing.

Because financial literacy in India is very low, most SMEs are unable to comprehend the benefits of equity financing. When the SME platform was first established in 2012, most market intermediaries were apprehensive, and many individuals doubted its success, owing to the collapse of the OTCEI. OTCEI was also a SME Exchange, with standards identical to those issued by SEBI in 2010 for the SME platform. Aside from that, the notion of three-year market-making and 100% underwriting was adopted, putting a lot of burden on merchant bankers' shoulders. Merchant bankers were unprepared for this novel notion at the time. So, at first, BSE SME had to put in a lot of work to persuade merchant bankers, but as time went on, a new generation of merchant bankers emerged, and from 2015 onwards, the SME platform explode as merchant bankers began to list SMEs.

The merchant banker must conduct extensive due diligence and paperwork in order to prepare the prospectus. Merchant bankers and promoters have a legal obligation to provide full disclosure. It takes time to do these tasks. In terms of preparing the prospectus, all of the documentation and paperwork requirements on the SME and main boards are the identical. They have reduced the physical inspection of firm officials and industrial facilities by BSE officials to speed up the process of listing in the breakout of the second wave of Covid. The promoters and merchant bankers now have the responsibility of sending the video clip of the factory and the official premises, as well as the supporting documentation confirmed by the merchant banker and the statutory auditor.

According to the CII, the industry employs about 120 million Indians and accounts for 33.4 percent of India's industrial output. In terms of exports, the contribution of SMEs is projected to be around 45 percent of overall exports. Despite the fact that SMEs account for a significant portion of India's GDP, conventional inefficient business practices and a low rate of technology adoption have prevented smaller businesses from achieving excellence. According to Google's research, which was conducted in partnership with KPMG, 68 percent of the 51 million SMEs are not linked to the internet. According to the report, digitalization of SMEs may increase their contribution to India's GDP by ten percentage points by 2020, bringing it to 46-48 percent. The Bombay Stock Exchange (BSE) announced in June 2021 that it has partnered with the Electronics and Computer Software Export Promotion Council (ESC) to raise awareness about the benefits of listing among small firms and start-ups.

#### 4. CONCLUSIONS & RECOMMENDATIONS

The SME platform has now established itself as the most cost-effective means for SMEs to obtain finance and get awareness. BSE SME has grown to become India's largest SME platform as a result of government's persistent efforts. The current study aids us in comprehending how IPOs support SMEs. It is valuable in determining the relevance of SME exchanges and determining the impact of initial public offerings on SMEs. Companies from 17 industries are listed, and the capital markets have raised about Rs. 7656 crores through IPOs and follow-on offerings. It is focusing on equity capital to help SMEs develop; therefore it has set up a fund of funds where it would invest Rs 10,000 crore, which will be leveraged to Rs 50,000 crore. The MSME ministry is collaborating with a range of stakeholders to ensure that funding is implemented as soon as possible. This would offer a significant boost to SMEs' growth. The sooner the fund is established, the better for SMEs that would get equity capital through it to expand.

There is a need to establish a large number of alternative investment funds (AIFs) that can invest in the equity of SMEs who are planning to list on the stock exchange. To encourage long-term investment in SMEs, the government may implement laws that provide tax incentives to long-term investors.

The need of the hour is for industry players, government policymakers, and businesses to collaborate to allow SMEs that have been left behind to become digitally empowered. Big tech companies have recognized the



opportunity and are actively assisting Indian SMEs in adopting newer technologies such as cloud, AI, process automation, and data analytics to improve enterprise processes such as accounting, inventory management, sales, marketing, HR, and customer service.

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