Anchor Investor - Roles & Challenges

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The concept of 'Anchor Investor' was introduced by SEBI in July 2009 in the backdrop of the global economic, credit and capital markets crisis and in response to requests from issuers/merchant bankers that if some institutional investors are ready to come in with prior commitments, it will enhance their ability to sell the issue and generate more confidence in the minds of retail and other investors. As the anchor investors were to commit a percentage of the issue even before the issue opened with a 30-day lock-up, the same was expected to establish a benchmark as regards quality and pricing of the public issue for other investors. This move was also expected to generally improve the primary market activities in India.

SEBI had ordered abolition of discretionary allotments for institutional investors in public issues few years back. Though this measure was introduced to fix certain malpractices in the system prevailing at that time, the new proportionate system of allotting shares to institutional investors took away the flexibility of issuers/ merchant bankers to recognize investors who committed their investments early and/or were willing to remain invested for a longer duration after listing. The new system made no distinction between investors who were bidding in the last hours of a public issue based on the overall book size vis-à-vis those who bid at initial stage of the book.

The concept of anchor investors has in a limited sense brought back some of these flexibilities, which recognize that all investors, even if they are institutional, are not equal. In the anchor portion of the public issue, the issuers/ merchant bankers can prioritize allotment of shares to investors based on certain qualitative aspects, which according to them are important for the issuer and success of the issue.

The concept of anchor investor is not unique to India and is prevalent with variations in other advanced markets.

The experience so far

Since the introduction of anchor investor concept by SEBI in July 2009, 38 corporates have raised ~Rs. 45.78bn through anchor investments, which is ~21% of the total amount raised from all QIBs and ~13% of the total amount raised by private sector corporates through public issues.

Of the total anchor investments in public issues so far, ~69% and ~27% have been invested by FIIs and mutual funds respectively with balance ~4% coming from all other types of QIBs including banks, financial institutions and insurance companies.

Anchor investment concept is a win-win situation for issuers, anchor investors as well as other investors in public issues because of the following:

- The very concept of coming a day in advance and not able to exit mandatorily for 30 days gives comfort to all residuary investors especially to retail investors,
- Mandatory 30-day lock-in for anchor investors ensures lower selling pressure on the stock in initial days after listing,
- In all fairness, allotment to anchors is not exposed to oversubscription in public issues. They get allocation the same day they bid and have the flexibility to bid for more in the institutional quota should they have more appetite for investment in that public issue.

The Indian experience - Select facts & figures

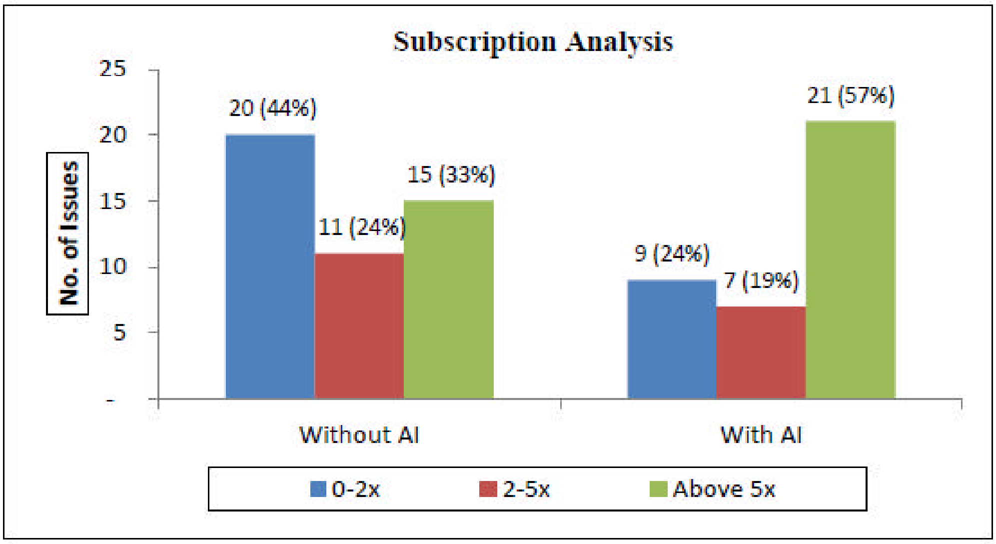
The Department of Disinvestments as well as public sector corporates have not yet opted for anchor investments. Out of aggregate fund raising of ~Rs. 1,267bn through public issues over last 2 years since the anchor investment concept was introduced in July 2009, 73% of the issues have been made of public sector corporates alone. Despite strong investors' appetite in several of these public sector issues, the Department of Disinvestments/public sector issuers so far have decided not to use this concept reportedly because of the element of discretion involved in making allocations to anchor investors.

Following is a summary of all private sector public issues since introduction of anchor investment concept in July 2009 till date showing trends of anchor investments:

Anchor Investor (AI) participation	No. of public issues	% of total nos.	Amount raised through public issues (~Rs. bn)	% of total amount
With AI	38	44%	276	81%
Without AI	48	56%	66	19%
Total	**86**	**100%**	**342**	**100%**

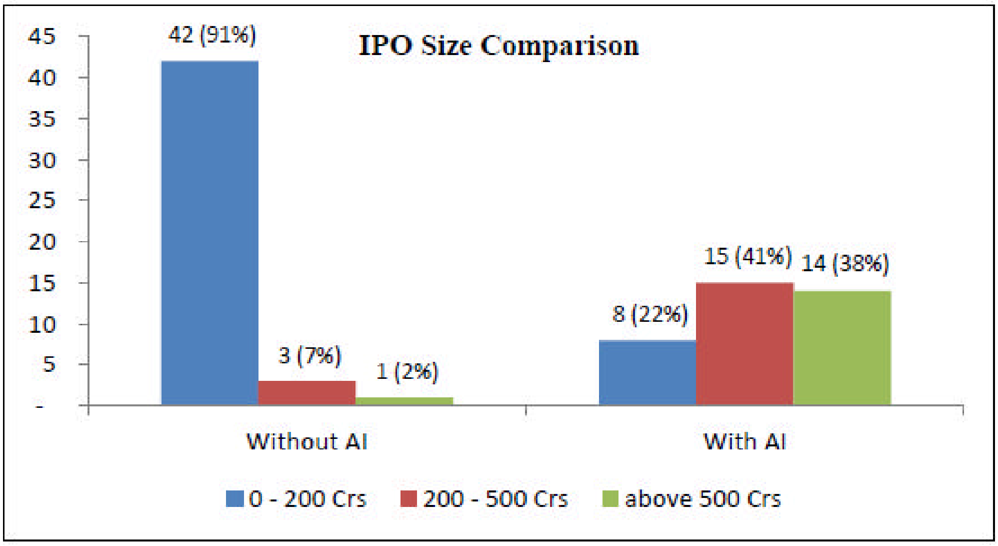
Further analysing the acceptance and the effect of anchor investment concept in private sector public issues during this period reveals some interesting facts:

1. Subscription numbers for public issues without Anchor Investors Vs. those backed by Anchor Investors



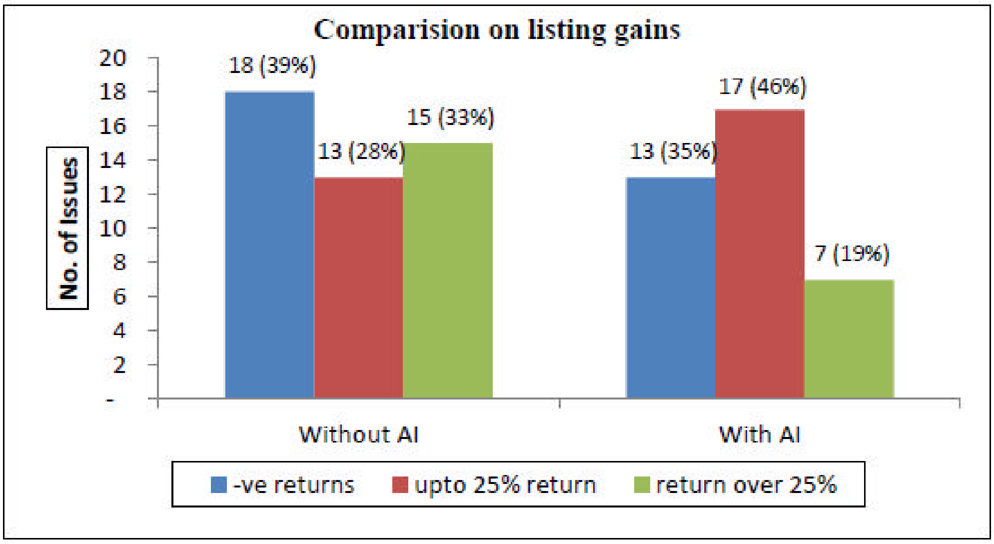
As can be seen from the above chart, ~44% public issues without anchor investors got lukewarm response from the market vs only ~24% in case of anchors backed public issues. On the other hand, ~57% public issues backed by anchor investors were subscribed over 5 times vs ~33% in case of non-anchors backed public issues. Quite clearly, anchor investors backed issues have been better accepted by investors.

2. Comparison of public issue size with reference to presence of Anchor Investors



As can be seen from the above chart, ~91% public issues without anchor investors were below Rs. 2bn. Clearly, the concept of anchor investors has not clicked with smaller public issues.

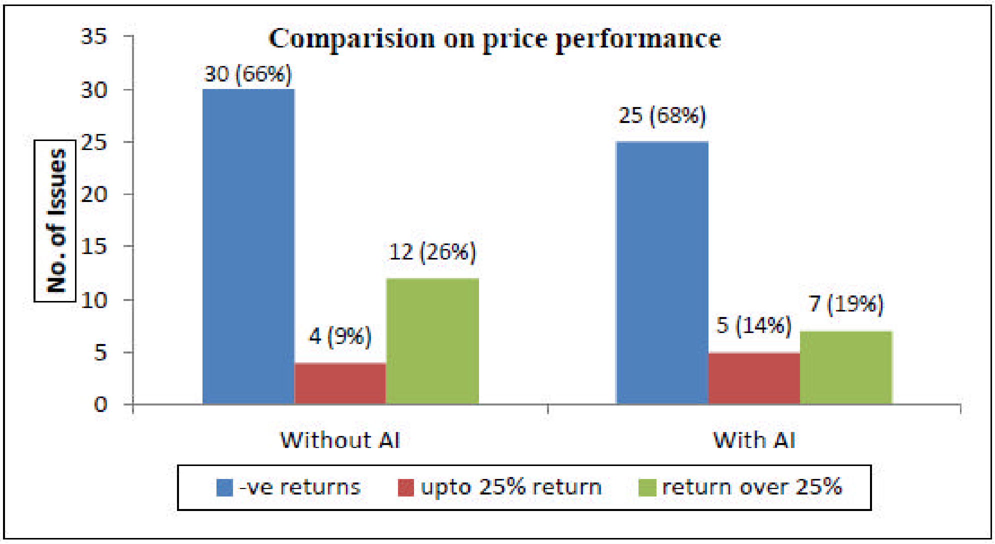
Listing gains in public issues without Anchor Investors Vs. those backed by Anchor Investors



(Closing price on the listing day)

Issues without anchor investors have seen extremes as far as listing performance is concerned. ~39% public issues without anchor investors have listed at a discount. At the same time, ~33% public issues without anchor investors have delivered over 25% listing gains. On the other hand, though ~65% public issues backed by anchor investors have listed at a premium over the Issue Price, a significant portion of the public issues backed by anchor investors, i.e. ~35%, got listed with negative returns.

3. Price performance for public issues without Anchor Investors Vs. those backed by Anchor Investors



(Issue price has been compared with the closing market price as on June 9, 2011)

The recent turbulent secondary market conditions have kept investors on tenterhooks. As can be seen from the above chart, ~66% public issues without anchor investors are currently trading at a discount to the Issue Price. The public issues backed by anchor investors have a similar story with ~68% public issues backed by anchor investors trading at a discount to the Issue Price.

Anchor Investment vs. Pre-IPO placements

With the introduction of anchor investment concept, pre-IPO placements have considerably lost its relevance. The anchor investors are locked in only for 30 days vis-à-vis Pre-IPO investors who are locked in for one year. Some of the important issues faced by issuers in pre-IPO placements, e.g., desire of pre-IPO investors to have rights/ protections typical to private equity investments due to some element of uncertainty involved regarding timing & pricing of the IPO and in case of IPO not getting launched within an agreed time frame becomes non-applicable in case of anchor investors.

Some limitations

SEBI has fixed the minimum bid size by anchor investors at Rs. 100mn which has the following repercussions:

1. It restricts the smaller issuers from having anchor investors in their public issues on a technical ground; and
2. In very large issues it leads to crowding of anchor investors which eventually leads to disappointments either due to rejection of bids of relatively small anchors by the issuers or reduction of the average allocation size.

Linking of minimum bid size of anchor investors with reference to size of the public issues may to some extent address these issues.

Remarks

The above analysis shows that whereas anchor investor backed issues are able to get better acceptability from investors (including retail investors) in public issues, anchor investors seems to have failed to ensure better deal pricing by issuers/merchant bankers. Anchor investors giving a miss to mispriced issues probably would be able to convey this important message to them.