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Importance of an IPO for SMEs

SME IPO to Main Board IPO

SME IPO: Introduction

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What is SME IPO?

An SME IPO allows Small and Medium Enterprises (SMEs) to raise equity capital by listing their shares on a stock exchange's SME platform (e.g., BSE SME, NSE Emerge). It is a simplified IPO process designed for smaller companies with fewer compliance requirements and reduced costs.

Purpose

- Access to public capital.
- Increased visibility and brand trust.
- Market-based valuation.
- Corporate governance discipline.

SME IPO: Introduction

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Eligibility

- Post-issue paid-up capital ≤ ₹25 crore.
- Company should not be a large cap.
- Track record and promoters' background are assessed

Pre-IPO Phase: Planning and Preparation

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Goal: Make the company IPO-ready. This phase can take 6–12 months.

Key Steps:

1. Eligibility Check

- Review financials, legal status, promoter track record.
- Ensure company is operational and profitable (preferably).

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2. Corporate Structuring

- Convert into a Public Limited Company.
- Dematerialization of shares.
- Cleaning up shareholder structure.

3. Appointment of Intermediaries

- Lead Manager/Merchant Banker.
- Registrar to the Issue.
- Legal Advisor, Auditor, Underwriter, Bankers.

4. Due Diligence

- Legal, secretarial, financial review.
- Identify risks and compliance gaps.

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5. Restructuring of Pre-IPO Capital

- Align shareholding structure as per SEBI and exchange norms

6. Preparation of DRHP (Draft Red Herring Prospectus)

- Company profile, financials, risk factors, business model, purpose of IPO.

7. Capital Structure Planning

- Evaluate debt-equity mix, authorized capital, promoter holding.
- Capital structure helps determine share issue price.
- Balanced structure attracts investors and supports optimal pricing.

8. Valuation and Issue Pricing

- Determine valuation based on financials and industry comparables

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9. Dematerialisation of Shares

- Ensure all shares are in demat form for eligibility to list

10. Preparation of Public Issue Offer Document

- Draft DRHP and final prospectus based on due diligence

11. Appointment of Other Intermediaries

- Includes auditors, legal advisors, bankers to the issue

12. Filling with Exchange and SEBI

- DRHP is filed with stock exchange and SEBI for review

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13. Clearance from SME Exchange

- Exchange processes and grants approval post-due diligence

14. Filing of Final Prospectus with RoC

- Once cleared by exchange, file prospectus with Registrar of Companies

During the IPO Process

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Objective: Launch and complete the IPO

Key Steps:

1. Regulatory Approval

- DRHP reviewed by SEBI and Exchange.
- RHP (final prospectus) published post-approval.

2. IPO Launch

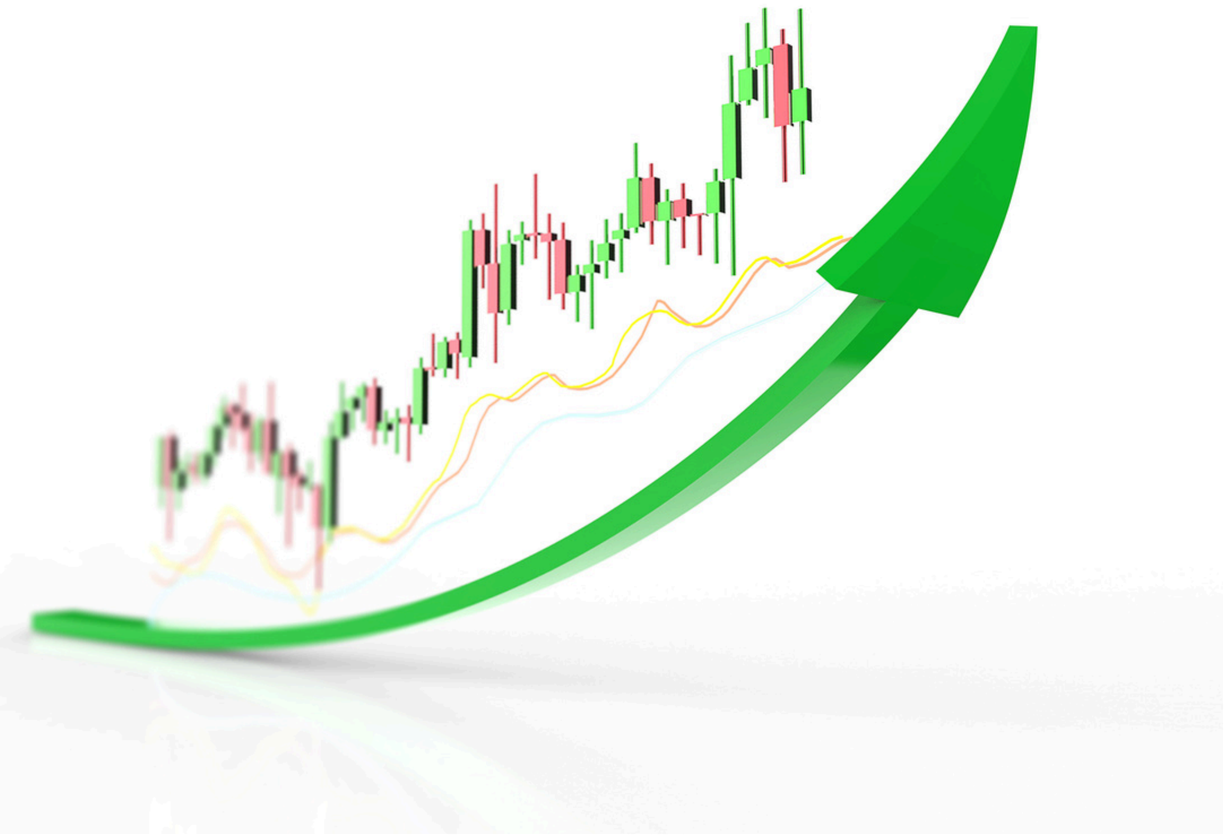
- Public subscription is opened for 3–5 days.

3. IPO Structuring

- Decide issue price, lot size, and overall issue size.
- Fixed price or book-building method.

4. Pricing Linked to Capital Structure

- Issue price influenced by:
  - Net worth and reserves.
  - Debt-equity ratio.
  - Equity dilution and promoter holding.



5. Marketing & Roadshows

- Investor presentations to promote IPO.
- Build investor confidence.

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6. IPO Opening

- Open for 3–5 working days.
- Investors apply via ASBA (Applications Supported by Blocked Amount).

7. IPO Management - Application & Other

- Manage investor subscriptions and application process

8. IPO Closure

- Close subscription window and prepare for allotment

9. Assist in Finalization of Basis of Allotment

- Finalize allotment ratio based on oversubscription levels.

10. Share Allotment & Listing

- Shares allotted to subscribers.
- Listing on SME exchange.
- Stock starts trading post listing

11. Getting Stock Exchange Approval

- Apply and receive approval to commence trading

12. Refunds/Allotment Process

- Refund excess funds and complete allotment confirmations.

Post-IPO Responsibilities

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After the listing, a company becomes answerable to public shareholders and regulators.

Post-IPO Compliance

1. Ongoing Disclosure Requirements

- Quarterly, half-yearly, and annual financial reporting.
- Shareholding pattern and outcome of board meetings.

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2. Corporate Governance

- Appoint Independent Directors.
- Formation of Audit and Nomination Committees.

3. Investor Relations

- Dedicated team to address investor queries.
- Timely press releases and announcements.

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4. Utilization of IPO Proceeds

- Funds used only for disclosed purposes.
- Auditor-certified reports submitted to stock exchange.

5. Legal Compliance

- Annual listing fees.
- Secretarial audits.
- Internal controls and statutory audits.

Transition to Main Board from SME Exchange

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Why migrate?

- Larger investor base.
- Higher valuation and liquidity.
- Better market image.
- Inclusion in institutional investment radar.

WHEN Can a Company Migrate?

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As per SEBI & Exchange rules:

- Minimum 2 years of listing on SME platform.
- Paid-up capital post-issue ≥ ₹10 crore.
- Net worth ≥ ₹15 crore.
- Minimum average operating profit ≥ ₹15 crore in the past 3 years.
- Minimum 250 public shareholders.

HOW Does Migration Happen?

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1. Board Resolution & Shareholder Approval
   - Special resolution required for migration.

2. Application to Exchange
   - Re-draft information memorandum or refile offer documents (if required).

3. Compliance Check
   - Ensure company meets all main board norms (governance, reporting, net worth).

4. Public Notice and Announcement
   - Information to all stakeholders.
   - New trading symbol assigned after approval.

Post-IPO Transactional Costs and Legal Fees

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Major Post-IPO Costs:

Expense Category	Description
Registrar Fees	For managing allotments and shareholder data
Listing Fees	Annual fees paid to stock exchange
Audit & Compliance	Secretarial audits, statutory filings
Legal Advisory	Post-listing contracts, disputes, and board advisory
Investor Relations	Tools and platforms to maintain investor communication

Role of Underwriters in an IPO

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Underwriters play a vital role in the success of an IPO.

Key Responsibilities:

- **Assess Valuation:** Help set fair issue price.
- **Risk Management:** Take underwriting responsibility in case of under subscription.
- **Due Diligence:** Ensure disclosures are accurate and fair.
- **Marketing:** Promote the IPO to institutional and retail investors.
- **Investor Network:** Tap into HNIs, institutional clients, and mutual funds.
- **Capital Structure Advice:** Assist in creating a balanced capital structure that supports optimal pricing and attracts investors.

Role of Market Makers in SME IPO

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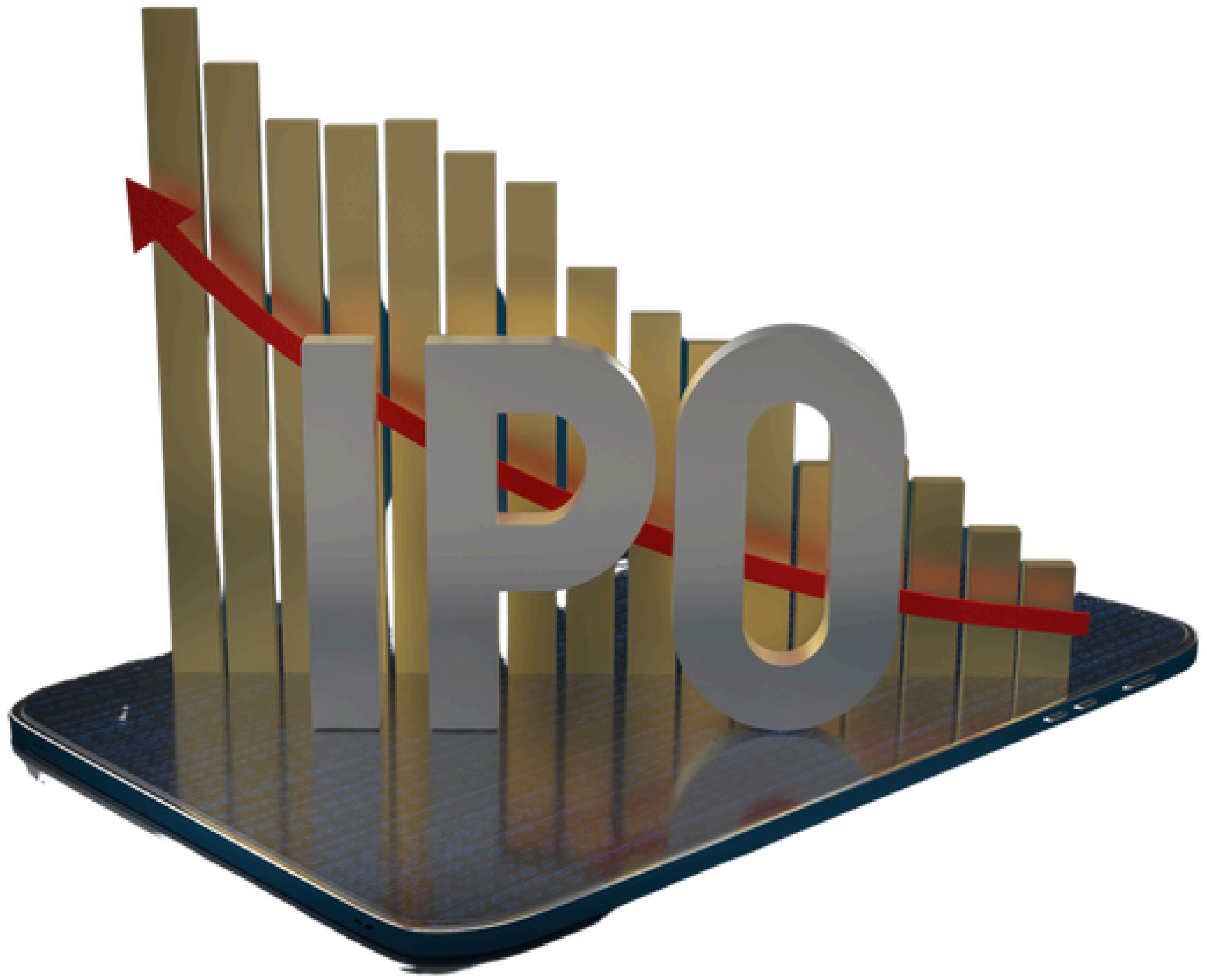
Market makers are SEBI-registered intermediaries who provide liquidity and depth to shares listed on SME exchanges.

Who Are They?

- Typically appointed by the company or the merchant banker during the IPO.

- Registered brokers or market intermediaries with the stock exchange.



Key Responsibilities:

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- **Provide Two-Way Quotes:** Maintain buy and sell quotes continuously.
- **Ensure Liquidity:** Prevent price manipulation or illiquidity in early trading days.
- **Stabilize Stock Price:** Manage price volatility by standing ready to trade.
- **Compulsory Appointment:** As per SEBI norms, every SME IPO must appoint at least one market maker.
- **Initial Holding:** May hold inventory of shares post-listing to facilitate trades.

Market makers are usually appointed forminimum period of 3 years after listing to support healthy market activity in the SME segment.

Role of QIB (Qualified Institutional Buyers) in IPOs

QIBs are large institutional investors who are considered financially sophisticated and capable of evaluating investment risks.

Who Qualifies as QIB?

- Mutual Funds.
- Foreign Portfolio Investors (FPIs).
- Insurance Companies.
- Scheduled Commercial Banks.
- Alternative Investment Funds (AIFs)

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Key Roles:

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- **Anchor Investment:** QIBs often act as anchor investors who invest before the IPO opens, signaling confidence.
- **Price Discovery:** Their participation helps in fair price setting.
- **Market Credibility:** QIB interest enhances market reputation and retail investor confidence.
- **Allocation:** In book-building IPOs, a minimum 50% of the net offer is reserved for QIBs (not mandatory for SME IPOs but indicative of scale readiness)

QIBs bring both credibility and stability to the IPO process.

Real-World Example

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IdeaForge Technology Ltd. (Listed on NSE SME platform)

- QIBs such as Tata Mutual Fund and ICICI Prudential Mutual Fund participated as anchor investors in its IPO.
- Their involvement improved subscription levels and enhanced investor confidence in the issue.

QIBs bring both credibility and stability to the IPO process.

Bonus Shares vs. Rights Issue (Post-IPO Capital Actions)

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Feature	**Rights Issue**	**Bonus Shares**
Objective	Raise fresh capital	Capitalize reserves, reward shareholders
Issued To	Existing shareholders (optional subscription)	All shareholders (proportionately)
Pricing	Discounted price (below market)	Free (no cost to shareholder)
Fund Inflow	Yes – company receives capital	No – internal adjustment of reserves
Dilution Risk	Yes, if shareholders don't subscribe	No new funds raised; share count increases
Example Ratio	1:3 (Buy 1 share for every 3 held)	1:1 (Get 1 bonus for every 1 share held)

End-to-End Illustration: Real-World IPO Journey

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To illustrate the entire IPO journey, consider the real-world example of IdeaForge Technology Ltd., a company that successfully navigated the SME IPO landscape:

Pre-IPO

- **Planning & Structuring:** IdeaForge, a drone manufacturer, restructured its capital, converted into a public limited company, and completed due diligence.

- **Intermediaries**: Appointed merchant bankers and legal advisors, including JM Financial and IIFL Securities.

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Conclusion

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- SME IPO is a powerful tool for small companies to scale up.
- Transitioning to the main board gives wider exposure and institutional interest.
- Compliance, transparency, and investor communication are crucial post-IPO.
- Underwriters, market makers, QIBs, legal experts, and advisors play a key role throughout.
- Corporate actions like bonus shares and rights issues keep shareholders engaged and help manage capital needs.
- A well-structured capital base defines valuation, pricing, and long-term market performance.