

BOOK BUILDING PROCESS: A MODERN WAY OF ISSUING SECURITIES

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ABSTRACT

When companies are on the look out to raise money for their business operations, they use various means for the same. Two of the most popular means to raise money are Initial Public Offer (IPO) and Follow on Public Offer (FPO). During the IPO or FPO, the company offers its shares to the public either at fixed price or offers a price range, so that the investors can decide on the right price. The method of offering shares by providing a price range is called as book building method. The Issuer who is planning an IPO nominates a lead merchant banker as a 'book runner'. The Issuer specifies the number of securities to be issued and the price band for orders.

A Book should remain open for a minimum of 5 days. Book building is actually a price discovery method. In this method, the company doesn't fix up a particular price for the shares, but instead gives a price range, e.g. Rs 80-100. When bidding for the shares, investors have to decide at which price they would like to bid for the shares, for e.g. Rs 80, Rs 90 or Rs 100. They can bid for the shares at any price within this range. Based on the demand and supply of the shares, the final price is fixed. The lowest price (Rs 80) is known as the floor price and the highest price (Rs 100) is known as cap price. The price at which the shares are allotted is known as cut off price. The entire process begins with the selection of the lead manager, an investment banker whose job is to bring the issue to the public. Both the lead manager and the issuing company fix the price range and the issue size. Next syndicate members are hired to obtain bids from the investors. Normally the issue is kept open for 5 days.

KEYWORDS: Book Building Process, Business Operations, Book Building Guidelines

INTRODUCTION

What is Book Building?

Book Building is the process of determining the price at which an Initial Public Offering will be offered. SEBI guidelines, 1995 defined book-building as “a process undertaken by which a demand for the securities proposed to be issued by a body of corporate is elicited and built up and the price for such securities is assessed for the determination of the quantum of such securities to be issued by means of a notice, circular, advertisement, document or information memoranda or offer document”.

In general, the word “Book building” is a method of marketing the shares of a company whereby the quantum and the price of the securities to be issued will be decided on the basis of the ‘bids’ received from the prospective shareholders by the lead merchant bankers. According to this method, share prices are determined on the basis of real demand for the shares at various price levels in the market.

Book building is a common practice in developed countries and has recently been making inroads into emerging markets as well. When companies are on the look out to raise money for their business operations, they use various means for the same. Two of the most popular means to raise money are Initial Public Offer (IPO) and Follow on Public Offer (FPO).

During the IPO or FPO, the company offers its shares to the public either at fixed price or offers a price range, so that the investors can decide on the right price. The method of offering shares by providing a price range is called as book building method.

TYPES OF INVESTORS

There are three kinds of investors in a book-building issue.

- The retail individual investor (RII)
- The non-institutional investor (NII)
- The Qualified Institutional Buyers (QIBs)

There are Two Types of Public Issues

Fixed Price Issue: When the issuer at the outset decides the issue price and mentions it in the offer document, it is commonly known as fixed price issue.

Book Built Issue: When the price of an issue is discovered on the basis of demand received from the prospective investors at various price levels, it is called as book built issue.

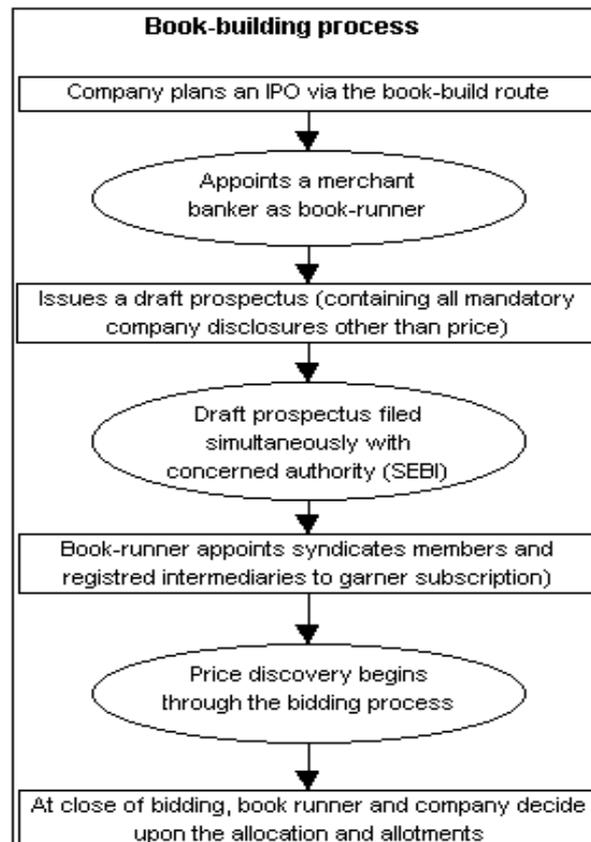


Figure 1

BOOK BUILDING PROCESS IN INDIA

Book Building is fundamentally a procedure utilized in IPOs for effective price discovery. It's a method where, during the time period for which the initial public offer is open, bids are gathered from traders at different prices, which are higher or equal to the ground price. The IPO offer price is decided following the bid ending date.

GUIDELINES BY SEBI

- On the recommendations of Malegam committee, the concept of Book Building assumed significance in India as SEBI approved, with effect from November 1, 1995, the use of the process in pricing new issues.
- SEBI issued the guidelines under which the option of 100% book-building was available to only those issuer companies which are to make an issue of capital of and above Rs. 100 crore.
- These guidelines were modified in 1998-99. The ceiling of issue size was reduced to Rs. 25 crore.
- SEBI modified book-building norms for public issues in 1999 and allowed the issuer to choose either the existing or the modified mode of book building.

Modified Guidelines

- Compulsory display of demand at the terminals was made optional.
- The reservation of 15% of the issue size for individual investors could be clubbed with fixed price offer.
- The issuer was allowed to disclose either the issue size or the number of securities being offered.
- The allotment of the book built portion was required to be made in Demat mode only.
- In April 2000, SEBI modified guidelines for the 100% book-building process. i.e. a maximum of 60% of the issue was allowed to Institutional investors and at least 15% to non-institutional investors who had applied for more than 1,000 share.

Types of Book-Building

The Companies are bound to adhere to the SEBI’s guidelines for book building offers in the following manner:

- 75% book building
- 100% book building

75% Book-Building Process

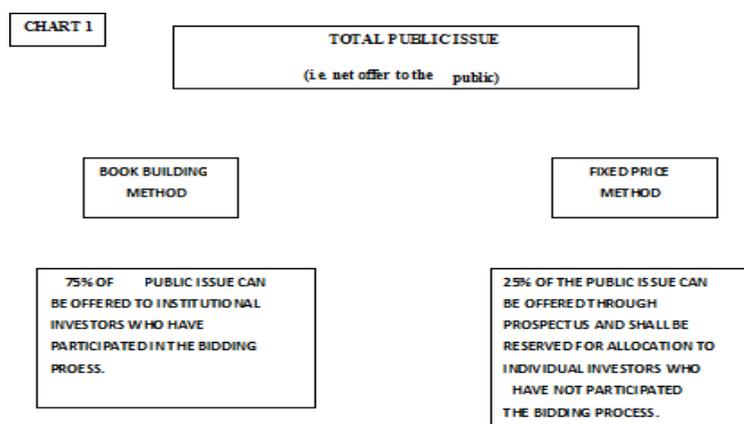


Figure 2

Under this process 25 per cent of the issue is to be sold at a fixed price and the balance of 75 per cent through the Book Building process.

The process specifies that an issuer company may make an issue of securities to the public through prospectus in the following manner:

- 100 per cent of the net offer to the public through book building process, or
- 75 per cent of the net offer to the public through book building process and 25 per cent of the net offer to the public at a price determined through book building process.

100% Book Building Process

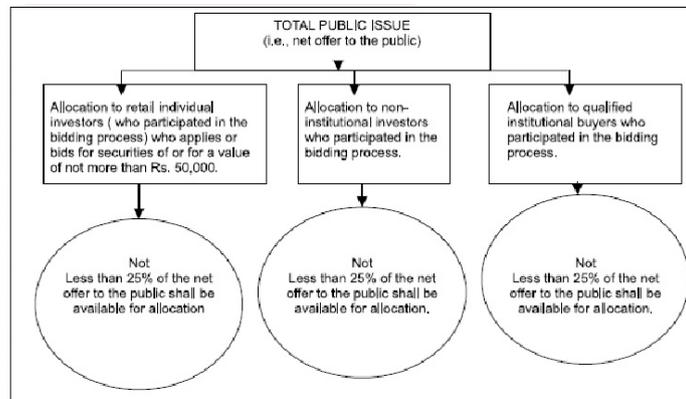


Figure 3

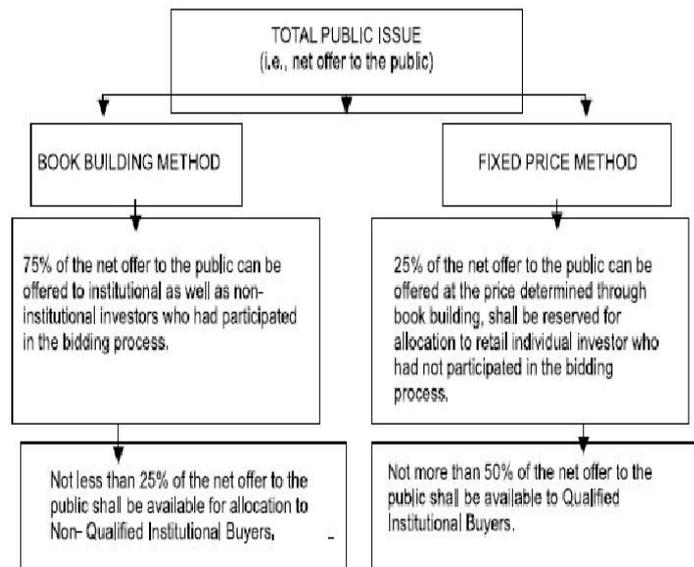


Figure 4

**75% OF THE NET OFFER THROUGH BOOK BUILDING PROCESS
ROLE OF INTERMEDIARIES**

Merchant Bankers to the issue or Book Running Lead Managers (BRLM), syndicate members, Registrars to the issue, Bankers to the issue, Auditors of the company, Underwriters to the issue, Solicitors, etc. are the intermediaries to an issue.

The issuer discloses the addresses, telephone/fax numbers and email addresses of these intermediaries. In addition to this, the issuer also discloses the details of the compliance officer appointed by the company for the purpose of the issue.

Role of Merchant Bankers in Public Issues

- Deciding on the size and timing of a public issue in the light of the market conditions.
- Preparing the base of successful issue marketing from the initial documentation to the preparation of the actual launch.
- Optimum underwriting support.
- Appointment of bankers and brokers as well as issue houses.
- Professional liaison with share market functionaries like brokers, portfolio managers and financial press for pre-selling and media coverage.
- Preparation of draft prospectus and other documents.
- Wide coverage throughout the country for collection of applications.
- Preparation of advertising and promotional material

Who is Eligible to be a BRLM (Book Running Lead Manager)?



Figure 5

A Merchant banker possessing a valid SEBI registration in accordance with the SEBI (Merchant Bankers) Regulations, 1992 is eligible to act as a Book Running Lead Manager to an issue.

What is the Role of a Lead Manager? (Pre and Post Issue)

In the pre-issue process, the Lead Manager (LM) takes up the due diligence of company's operations/ management/ business plans/ legal etc. Other activities of the LM include drafting and design of Offer documents, Prospectus, statutory advertisements and memorandum containing salient features of the Prospectus. The BRLMs shall ensure compliance with stipulated requirements and completion of prescribed formalities with the Stock Exchanges, RoC and SEBI including finalization of Prospectus and RoC filing. Appointment of other intermediaries viz., Registrar(s), Printers, Advertising Agency and Bankers to the Offer is also included in the pre-issue processes.

The LM also draws up the various marketing strategies for the issue. The post issue activities including management of escrow accounts, coordinate non-institutional allocation, intimation of allocation and dispatch of refunds to bidders etc are performed by the LM. The post Offer activities for the Offer will involve essential follow-up steps, which include the finalization of trading and dealing of instruments and dispatch of certificates and demat of delivery of shares, with the various agencies connected with the work such as the Registrar(s) to the Offer and Bankers to the Offer and the bank handling refund business. The merchant banker shall be responsible for ensuring that these agencies fulfill their

functions and enable it to discharge this responsibility through suitable agreements with the Company.

What is the Role of a Registrar?

The Registrar finalizes the list of eligible allottees after deleting the invalid applications and ensures that the corporate action for crediting of shares to the Demat Accounts of the applicants is done and the dispatch of refund orders to those applicable are sent. The Lead manager coordinates with the Registrar to ensure follow up so that that the flow of applications from collecting bank branches, processing of the applications and other matters till the basis of allotment is finalized, dispatch security certificates and refund orders completed and securities listed.

IMPORTANCE OF UNDERWRITING IN BOOK BUILDING

Underwriting is a good technique of marketing the securities. The importance of under-writing can be adjudged by the following advantages:

- Assurance of Adequate Finance
- Benefit of Expert Advice
- Increase in Goodwill of the Company
- Geographical Dispersion of Securities
- Service to Prospective Buyers

BOOK BUILDING - A PRICE DISCOVERY METHOD

Book building is actually a price discovery method. In this method, the company doesn't fix up a particular price for the shares, but instead gives a price range, e.g. Rs 80-100.

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Once the offer period is over, the lead manager and issuing company fix the price at which the shares are sold to the investors. If the issue price is less than the cap price, the investors who bid at the cap price will get a refund and those who bid at the floor price will end up paying the additional money. For e.g. if the cut off in the above example is fixed at Rs 90, those who bid at Rs 80, will have to pay Rs 10 per share and those who bid at Rs 100, will end up getting the refund of Rs 10 per share. Once each investor pays the actual issue price, the shares are allotted.

Case Study: Birla Pacific Medspa Limited



Figure 6

Incorporated in 2008, Birla Pacific Medspa Limited is an India based healthcare provider. Birla Pacific Medspa is a joint venture of Yash Birla Group, a Rs 30 billion group of over 20 diversified companies and Pacific Healthcare, East Asia's leading healthcare provider, with healthcare facilities in Singapore, Hong Kong, and China.

Birla Pacific Medspa provides **beauty related medical procedures** in India. Using state-of-the-art equipments, the internationally qualified panel of doctors provides patient centric solutions and offers the latest and safest treatments.

Company operates its healthcare centers under the brand name **EVOLVE**. Company operates 3 healthcare centers in Mumbai and has 2 franchises in Thane and Chennai. Company's expertise includes Cosmetic Dermatology, Cosmetic & Plastic Surgery, General & Specialist Dentistry and Maxillo Facial Prosthesis. It has introduced i-lipo, a non-surgical inch loss treatment, for the first time in India.

Company Promoters

Company is promoted by Mr. Yashovardhan Birla and one of his group companies, Birla Wellness & Healthcare Private Limited.

Objects of the Issue

The objects of the issue were:

- To meet the capital expenditure towards establishing 55 outlets of Evolve Med spa across various cities and places.
- To meet expenses towards brand promotion.
- To meet the working capital requirements for running the centers.
- To meet Issue related expenses.
- To enlist the Company's Shares on Bombay Stock Exchange Limited (BSE).

Issue Detail

- **Issue Open:** Jun 20, 2011 - Jun 23, 2011
- **Issue Type:** 100% Book Built Issue IPO
- **Issue Size:** 65,175,000 Equity Shares of Rs. 10
- **Issue Size:** Rs. 65.18 Crores
- **Face Value:** Rs. 10 Per Equity Share
- **Issue Price:** Rs. 10 - Rs. 11 Per Equity Share
- **Market Lot:** 500 Shares
- **Minimum Order Quantity:** 500 Shares
- **Listing At:** BSE

Birla Pacific Medspa Ltd IPO Grading

BWR (Brickworks Ratings India Pvt Ltd) has assigned an IPO Grade 2 to Birla Pacific Medspa IPO. This means as per BWR, company has '**Below Average Fundamentals**'. BWR assigns IPO grading on a scale of 5 to 1, with Grade 5

indicating strong fundamentals and Grade 1 indicating poor fundamentals. Read Birla Pacific Medspa IPO Grading Report.

Issue Subscription Detail / Current Bidding Status

Table 1

| Number of Times Issue is Subscribed (BSE + NSE) | | | | |
|---|---------------------------------------|------------------------------------|------------------------------------|-------------------|
| As on Date & Time | Qualified Institutional Buyers (QIBs) | Non Institutional Investors (NIIs) | Retail Individual Investors (RIIs) | Total |
| Shares Offered / Reserved | 32,587,500 | 9,776,250 | 22,811,250 | 65,175,000 |
| Day 1 - Jun 20, 2011 17:00 IST | 0.3300 | 0.0000 | 0.2500 | 0.2500 |
| Day 2 - Jun 21, 2011 17:00 IST | 0.6700 | 0.0000 | 0.3700 | 0.4600 |
| Day 3 - Jun 22, 2011 17:00 IST | 0.9900 | 0.0000 | 0.5800 | 0.7000 |
| Day 4 - Jun 23, 2011 17:00 IST | 1.0400 | 0.1700 | 1.8200 | 1.1800 |

BASIS OF ALLOTMENT

- Public Issue Of 65,175,000 Equity Shares Of Rs.10/- Each At A Price Of Rs.10/- Per Equity Share For Cash Aggregating To Rs. 6517.50 Lakh (The "Issue"), By Birla Pacific Medspa Limited (The "Company" Or The "Issuer"). The issue Constitutes 58.12% Of the Fully Diluted Post Issue Paid-Up Capital Of Our Company.
- The Issue Price Is One Time Of The Face Value
- The equity shares of the Company are proposed to be listed on Bombay Stock Exchange Limited
- ("BSE") and Trading is expected to commence on 7th July 2011

ISSUE PRICE: RS. 10/- PER EQUITY SHARE OF THE FACE VALUE OF RS. 10/- EACH BID/ISSUE OPENED ON JUNE 20, 2011 CLOSED ON JUNE 23, 2011

This Issue was made through a 100% Book Building Process in terms of regulation 26(2)(a)(i) and b(i) of SEBI (ICDR) Regulations, 2009, as amended from time to time, whereby at least 50% of the Issue was to be allocated to Qualified Institutional Buyers (QIBs) on a proportionate basis, subject to valid bids being received at or above the Issue Price. 5% of the QIB Portion was available for allocation on proportionate basis to Mutual Funds only and the remaining Net QIB portion was available for allocation on a proportionate basis to all Qualified Institutional Buyers, including Mutual Funds, subject to valid bids being received at or above Issue Price. Further, upto 15% of the Issue was available for allocation on a proportionate basis to Non Institutional Bidders and upto 35% of the Issue was available for allocation on a proportionate basis to Retail Individual Bidders, subject to valid bids being received at or above the Issue Price. The Issue received 3138 applications for 74670000 equity shares resulting in 1.15 times subscription. The details of the applications received in the Issue from Qualified Institutional Buyers, Non-Institutional and Retail Individual Investor categories are as under: **(Before technical rejections)**

Table 2

| | Category | No. of Applications | No. of Shares | No. of times Subscription |
|----------|-----------------------------------|---------------------|-----------------|---------------------------|
| A | Qualified Institutional Investors | 5 | 33812000 | 1.03 |
| B | Non Institutional Investors | 5 | 1614000 | 0.16 |
| C | Retail Individual Investors | 3128 | 39244000 | 1.72 |
| | Total | 3138 | 74670000 | 1.15 |

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