INDIAN SME STOCK EXCHANGE

Following the bliss…

NITIN PAHILWANI

[*Chartered Accountant*]

31st May, 2012

FIRST SME LISTING [BCB Finance was maiden listing on BSE SME Exchange]

The **Prime Minister's Task Force** (Jan. 2010) has recommended to set-up a dedicated **Stock Exchange/ Platform for SME**. SEBI on May 18, 2010 has laid down the regulation for the governance of SME Exchange/Platform [CIR/MRD/DSA/17/2010].

On 13th March, 2012, BCB Finance became the first company to be listed on BSE SME Exchange. BCB Finance raised Rs. 8.85 crore through public issue of 35.4 lakhs equity shares and opened with 8% premium on listing day on BSE's SME Exchange.

SME INdia [a quick snapshot of SMEs in India]

Small and Medium Enterprises (SMEs) play a vital role for the growth of Indian economy. India has nearly 30 million MSMEs, According to SME Chamber of India. Collectively, they account for almost 50% of industrial output, 42% of India's total exports, employing 60 million people, create 1.3 million jobs every year and produce more than 8000 quality products for the Indian and International markets. SME's Contribution towards GDP in 2011 was 17% which is expected to increase to 22% by 2012. SMEs are the fountain head of several innovations in manufacturing and service sectors, the major link in the supply chain to corporate and the PSUs.

The sector has been clamoring for higher fund flows since long time. According to the Secretary, Ministry of Micro, Small and Medium Enterprises (MSMEs), R.K. Mathur, the Sector needs Rs. 2.5 lakh crore equity and Rs. 4.7 lakh crore loans.

Eligibility norms for Listing on SME Exchange

The exchange will provide opportunity to entrepreneurs to raise equity capital for the growth and expansion of SMEs. It will also provide immense opportunity for investors to identify and invest in good SMEs at early stage.

1. Net Tangible Assets of at least Rs. 1 crore as per the latest audited financial results.
2. Net worth (excluding revaluation reserves) of at least Rs. 1 crore as per the latest audited financial results.
3. Track record of distributable profits in terms of Sec. 205 of Companies Act, 1956 for at least two years out of immediately preceding three financial years and each financial year has to be a period of at least 12 months. Extraordinary income will not

be considered for the purpose of calculating distributable profits. Otherwise, the net worth shall be at least Rs. 3 Crores.

4. Other Requirements
   - The post-issue paid up capital of the company shall be at least Rs. 1 crores
   - The company shall mandatorily facilitate trading in demat securities and enter into an agreement with both the depositories.
   - Companies shall mandatorily have a website

5. Certificate from the applicant company / promoting companies stating the following –
   - The Company has not been referred to the Board for Industrial and Financial Reconstruction (BIFR). Note: Cases where company is out of BIFR are allowed.
   - There is no winding up petition against the company that has been accepted by a court.

6. Listing Process will also involve: For listing on BSE SME platform promoters will mandatorily be required to attend an interview with the Listing Advisory Committee

7. Migration from BSE SME Exchange to the main Board of BSE:
   - The companies seeking migration to Main Board of BSE should satisfy the eligibility criteria as specified in 26(1) of SEBI (ICDR) Regulations, 2009 either at the time of initial listing on SME platform or at the time of seeking migration to Main Board. However, same will not be applicable where the company had sought listing on SME platform by following the process and requirements prescribed in 26(2) (a) of SEBI (ICDR) Regulations, 2009.

SEBI's Listing Framework

ENTERPRISES

Companies in the growth phase tend to get over-leveraged at which point, banks are reluctant to provide further credit. Equity capital is then necessary to bring back strength to the balance sheet. The option of equity financing through the equity market allows the firm to not only raise long-term capital but also get further credit due through an additional equity infusion. The issuance of public shares expands the investor base, and this in turn will help set the stage for secondary equity financings, including private placements.

MSME's are not able to access the capital markets through existing Stock Exchanges due to the stringent regulatory, disclosure and financial requirements. The creation of a separate Stock Exchange/ separate platform on existing exchanges for MSME's designed to cater to the needs of Indian MSME's has been on the policy makers agenda for some time now. A dedicated stock exchange for the SME sector would allow the SME's to access capital markets easily, quickly and at lower costs. The dedicated exchange is expected to provide better, focused and cost effective service to the SME sector.

1. An issuer whose post-issue face value capital does not exceed Rs. 10 crore shall make Initial Public Offer of specified securities in terms of Chapter XA of SEBI (ICDR) Reg, 2009
2. An issuer with post issue face value capital between Rs. 10 crore and Rs. 25 crore listed on SME exchange can migrate to Main Board, as specified in the ICDR Regulations and vice-versa, provided they meet the listing requirements of the stock exchange where they propose to list the specified securities and have obtained the shareholders approval in the manner specified in the ICDR Regulations.
3. An issuer listed on SME exchange proposing to issue further capital pursuant to which their post -issue face value capital may increase beyond Rs. 25 crore shall migrate to the main board, subject to obtaining in-principle approval of the main board before issue of such securities.
4. The issuer shall stipulate in the offer document, the minimum application size in terms of number of specified securities which shall not be less than Rs. 1 lakh per application.
5. A minimum number of 50 (fifty) investors is required at the IPO stage only. There shall be no continuous requirement of minimum number of shareholders.

VENTURE CAPITAL

The venture capital fund may enter into an agreement with merchant banker to subscribe to the unsubscribed portion of the issue or to receive or deliver securities in the process of market making under Chapter XA of the Securities and Exchange Board of India (Issue of Capital and Disclosure Requirements) Regulations, 2009

INVESTOR

It will also provide immense opportunity for investors to identify and invest in good SMEs at early stage. However, the minimum investment for IPO or trading lot is Rs. 1 lakh. Typically, high net worth individuals, institutional investors and banks will qualify to subscribe IPOs or play in the secondary market. It provides new level of opportunities for investors with more risk appetite.

MERCHANT BANKS

SEBI has compulsorily mandated market making for all scrips listed and traded on SME exchange.

1. The issue made in terms of Chapter XA of the ICDR Regulations shall be 100% underwritten and the merchant banker(s) shall underwrite 15% in their own account. Merchant Banker(s) can also enter into agreement with nominated investors to subscribe to the unsubscribed portion of the issue. Such arrangements shall be disclosed in the offer document

2. The merchant banker to the issue will undertake market making through a stock broker who is registered as market maker with the SME exchange. The merchant banker shall be responsible for market making for a minimum period of three years from the date of listing of the specified securities. Further, the merchant bankers can also enter into agreement with nominated investors, as defined under ICDR Regulations, to whom the shares bought or sold during the market making process can be transferred. Such arrangements shall be with the prior approval of the SME exchange and disclosed in the offer document.

3. The market makers are required to provide two way quotes for 75% of the time in a day. The same shall be monitored by the exchange.

4. There will not be more than 5 market makers for a scrip.

5. Market makers will compete with other market makers for better price discovery. The exchange shall prescribe the minimum spread between the bid and ask price.

6. During the compulsory market making period, the promoter holding shall not be eligible for the offering to market makers.

TIMINGs

The timings of trading for SME stocks are going to be a bit different. In case of listing, a company may either opt for call auction or continuous auction. The former suggests limited trading hours. For example, the NSE's trading time would be 10.30am to 11.30am under call option while trading will happen throughout the normal trading hours (9.15am to 3.30pm) for the continuous option.

It has been three months since the BSE's SME Exchange saw its first listing. While the exchange is bullish, SMEs say listing is easier. . However, there are still some issues that need sorting out. They add that some of the rules make it difficult for merchant bankers to sell these IPOs. Also, only institutional investors and high net worth individuals can invest in an SME and this means a smaller market. So Merchant bankers are finding it difficult in terms of insuring this kind of market making

The regulatory framework which is designed to safeguard investors, is throwing up obstacles for SMEs who want to list. Analysts warn that the exchange may not achieve its goal of having 100 listings within the next 15 months.

If anyone has any quires/clarification/feedback/anything then it will great to hear from you.

Thank you

Nitin Pahilwani

ntpahilwani@yahoo.com

http://in.linkedin.com/in/ntpahilwani