

SME IPO Market in India - Growth, Performance, And Regulatory Challenges

Table of Contents

Executive Summary.....	3
What the Data and Cases Reveal.....	3
Where Regulation Has Evolved.....	3
Global Lessons with Local Relevance	3
Policy & Regulatory Recommendations.....	3
Introduction	5
Growth And Development of The SME IPO Market in India.....	5
Performance Trends and Volatility in SME Stocks	8
Fraud Cases and Governance Challenges in The SME Segment.....	10
Regulatory Measures in India's SME Segment.....	14
International Perspectives: SME Boards in UK, Hong Kong, and Japan	18
Policy Recommendations and Conclusion	22

Executive Summary

India's SME IPO platforms were launched with a bold vision—to democratize capital access for small businesses. However, a decade in, mixed outcomes demand a sharper regulatory lens. While capital-raising has expanded, the segment also exhibits structural cracks: speculative listings, price manipulation, weak governance, and retail investor vulnerability.

What the Data and Cases Reveal

- **Performance divergence:** A few SME stocks have delivered exceptional post-IPO returns, but many have stagnated or collapsed.
- **Fraud triggers:** Cases like Gensol (which migrated to the main board), LSIL, and Synoptics reveal patterns—IPO cornering, post-listing price spikes, poor disclosures, and related party misuse.
- **Migration misuse:** SMEs using backdoor migration to the main board without genuine scale or governance capacity erode credibility.

Where Regulation Has Evolved

- Exchanges have gradually tightened listing/migration norms (e.g., profit track record, tangible assets, capital thresholds).
- SEBI introduced surveillance, issuer eligibility refinements, and investor protection rules. Yet, post-listing supervision and real-time risk detection remain thin.

Global Lessons with Local Relevance

- **UK's AIM** uses nominated advisers (Nomads) as gatekeepers—placing accountability on market intermediaries.
- **Hong Kong's GEM** prevents shell creation via float restrictions, lock-ins, and IPO allocation scrutiny.
- **Japan's TSE Mothers** shows how robust oversight and pre-listing governance norms can allow even pre-profit firms to list safely.

Policy & Regulatory Recommendations

1. **AI-based anomaly detection:** Use machine learning to flag red flags like price-volume divergence, IPO cornering, or sudden shareholder splits.
2. **SME governance scorecard:** Introduce a regulatory risk index combining governance and market signals to tier oversight.

3. **Gatekeeper model:** Evaluate a Nomad-like regime where certified intermediaries take ongoing accountability for listed SMEs.
4. **Tighten migration filters:** Add qualitative checks beyond financials—like board composition, ESG disclosures, and capital deployment records.
5. **Investor suitability filters:** Consider higher entry barriers for retail in high-volatility SME scrips—through suitability disclosures or graded access.

Bottom Line: The SME platform is vital for inclusive capital markets. But unless India shifts from relaxed entry to risk-based supervision and proactive deterrence, it risks becoming a playground for manipulation—not growth.

Introduction

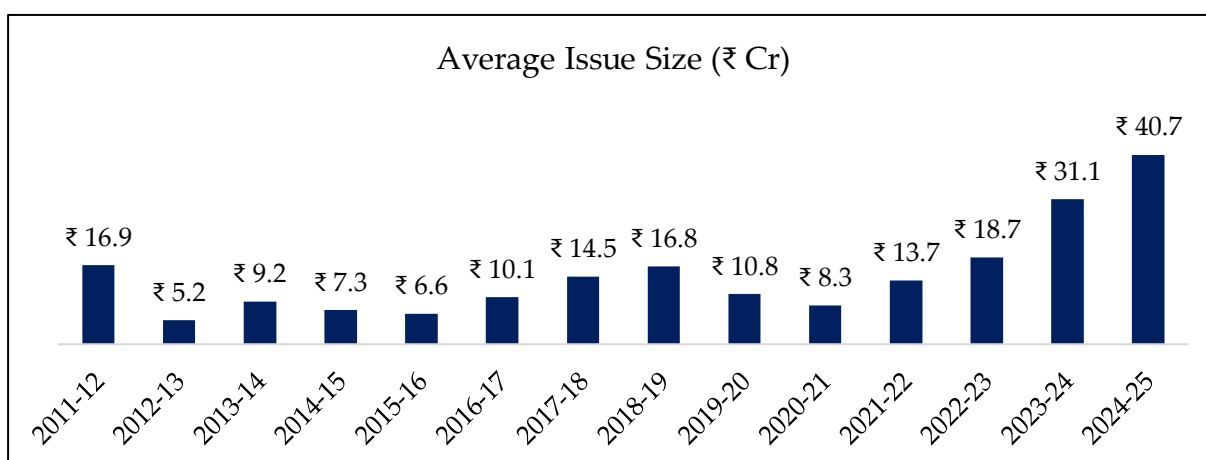
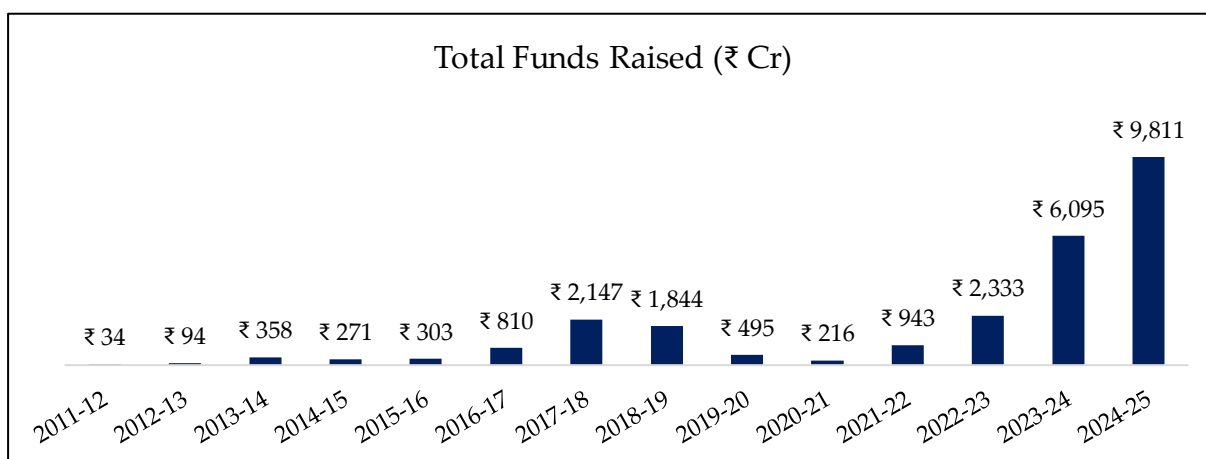
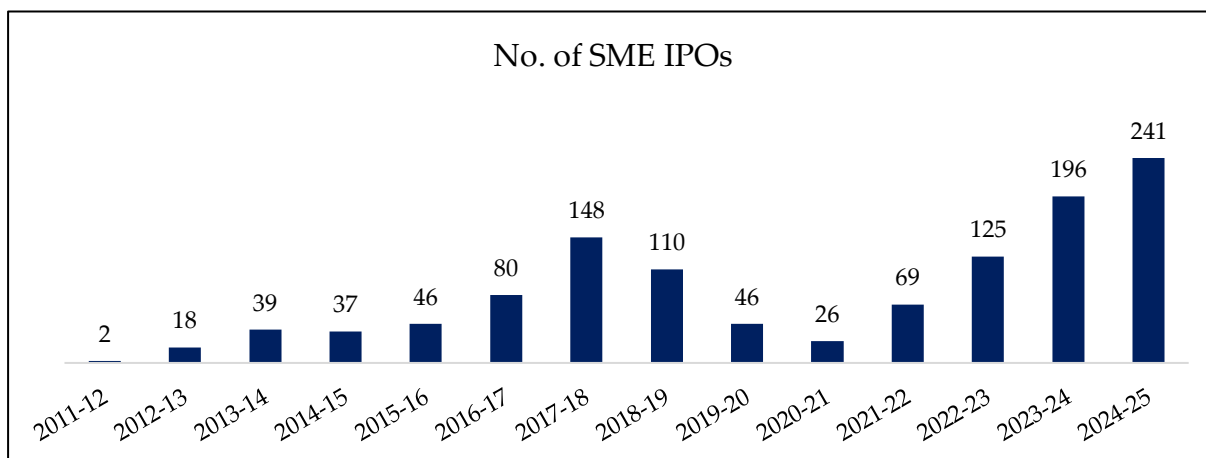
India's Small and Medium Enterprise (SME) IPO market started in 2012 with dedicated SME platforms (BSE SME and NSE Emerge) to help smaller companies raise capital through stock listings. Over the past decade, this segment has expanded rapidly in terms of listings and investor interest. It has offered an alternative funding source for emerging businesses and delivered impressive returns in some cases. However, alongside this growth, concerns have arisen about extreme price swings, governance issues, and cases of fraud and manipulation. Regulators—including stock exchanges and the Securities and Exchange Board of India (SEBI)—have introduced various measures to strengthen the framework and protect investors. This report looks at the development of the SME IPO market since its start, analyzes its performance and notable fraud cases, reviews regulatory responses, and suggests additional policy measures. It also draws on the experience of SME boards in the UK, Hong Kong, and Japan to gain insights on improving governance in this space.

Growth And Development of The SME IPO Market in India

Starting with a modest beginning in 2012, the SME IPO segment has grown quickly. In the first fiscal year (2011–12), only 2 SMEs went public, but by 2017–18, the pace had increased to nearly 150 IPOs annually. After a brief slowdown around 2019–20—partly due to economic conditions and the pandemic—the market rebounded strongly. In 2022–23 and 2023–24, record numbers of SME IPOs were launched, showing booming interest. The table below summarizes the annual trend in SME IPO issuances and funds raised:

Fiscal Year	No. of SME IPOs	Total Funds Raised (₹ Cr)	Average Issue Size (₹ Cr)
2011-12	2	34	16.9
2012-13	18	94	5.2
2013-14	39	358	9.2
2014-15	37	271	7.3
2015-16	46	303	6.6
2016-17	80	810	10.1
2017-18	148	2147	14.5
2018-19	110	1844	16.8
2019-20	46	495	10.8
2020-21	26	216	8.3
2021-22	69	943	13.7
2022-23	125	2333	18.7

2023-24	196	6095	31.1
2024-25	241	9811	40.7



Source: Compiled from SEBI and exchange data.

Several clear patterns emerge. The number of SME IPOs has surged in recent years, with 2024–25 seeing over 240 offerings—an all-time high. The total capital raised has also increased significantly; in FY 2024–25, SMEs raised around ₹9,811 crore, compared to just ₹34 crore in 2011–12. Additionally, the average issue size has gone up, from single-digit crores in earlier years to over ₹41 crore per company by 2024–25. This indicates a greater capacity of slightly larger SMEs to access the market and possibly more ambitious fundraising by issuers.

The growth has been driven by several factors. On the supply side, easier entry standards for SME exchanges (compared to main board IPOs) and fewer regulatory hurdles have attracted many companies. These platforms enable companies with limited capital or short operating histories to list, something that wasn't possible before 2012. On the demand side, investors—including high-net-worth individuals and specialized funds—have been attracted by the potential for high returns, as some SME stocks have delivered multibagger performance. Additionally, India's strong equity environment in recent years and the success stories of a few SME firms moving to the main board have increased confidence in this segment.

Notably, many SMEs that listed have later “migrated” to the main exchanges after meeting specific criteria. By mid-2025, over 340 companies had moved from the SME platforms to the main board, including around 147 from NSE Emerge and 196 from BSE SME. This migration mechanism was built into the system to allow proven companies to access a larger investor base and enjoy greater liquidity as they grow. The consistent flow of migrations indicates the success of the SME platform in nurturing smaller firms until they are ready for the broader market. However, it also means that investors in the SME segment often expect that the best companies will not stay on the SME board forever, which could affect long-term liquidity on the SME exchanges.

Overall, the SME IPO market's development has been strong, contributing over ₹27,000 crore in total capital to smaller businesses since it started. It has expanded the reach of the capital market into new sectors and regions—many SME listings are from tier-2 and tier-3 cities and niche industries. The rapid growth in recent years, however, also raises questions about whether the quality of issuances has been maintained or if the boom has attracted weaker companies riding on investor appetite.

Performance Trends and Volatility in SME Stocks

SME stocks are characterized by a relatively low float because promoters often hold a large share, and public shareholding is distributed among fewer investors due to minimum lot size requirements. Coupled with typically limited analyst coverage and lower liquidity, this can lead to high price volatility. Many SME IPOs have exhibited extreme price movements on the listing day and in subsequent months.

It is common for SME IPOs to debut with a sharp rise or fall. Recently, many SME IPOs have listed at a significant premium to their issue price, providing immediate “listing gains” to subscribers. For example, in late 2024, Ganesh Infraworld shares nearly doubled on the first day (around +90% from the IPO price), and Sathlokhar Synergys E&C rose over 75% on debut. On the BSE SME platform, Yash Highvoltage experienced a first-day gain of nearly 100%. Such large listing jumps are rare on main boards (where price bands and larger investor bases tend to reduce extreme swings) but have occurred on SME exchanges when there is enthusiastic oversubscription and a small float. Conversely, some issues have listed below their IPO price—for example, ATC Energies Systems in April 2025 closed about 9% lower on the first day, suggesting the market was not as excited as the IPO valuations had hoped.

Beyond the listing day, the performance of SME stocks has been a mixed bag – some have delivered multi-fold returns within months, while others have eroded significant value. The table below illustrates a few examples of SME IPO performance (across late 2024 and 2025 listings) to highlight this variability:

Company	Issue Price (₹)	Listing Close (₹)	Listing Gain (%)	Current Price (₹)	Overall Gain/Loss (%)
Sathlokhar Synergys E&C	140	247	+76%	455	+225%
Yash Highvoltage	146	291.25	+99%	514	+252%
Ganesh Infraworld	83	157.7	+90%	224	+170%
Safe Enterprises	138	151	+9%	206	+49%
Delta Autocorp	130	175	35%	70.6	–46%
ATC Energies Systems	118	107	–9%	63.5	–46%

Note: Current prices as of mid-2025; overall gain/loss calculated from issue price.

As shown, some stocks like Sathlokhar, Yash Highvoltage, and Ganesh Infracore have more than doubled or tripled in value shortly after listing, rewarding investors generously. These are often cases where a positive narrative or strong speculative interest pushed the price far beyond the IPO valuation. On the other hand, there are cases like Delta Autocorp (an electric vehicle company) which had a good debut but then fell to less than half its issue price as initial excitement faded and fundamentals were examined closely. ATC Energies also drifted well below its IPO level over time. This variation in outcomes highlights the high-risk, high-reward nature of SME investing. Small-cap businesses can be highly sensitive to business setbacks, with their stock prices reacting accordingly; but when growth prospects look promising, the small trading float can drive dramatic rallies.

Another notable trend has been the heavy oversubscription of some SME IPOs, especially in the last two years. It has become common to see issues subscribed by tens or even hundreds of times, despite the minimum application size (often ₹1–2 lakh) intended to limit participation mainly to HNI and institutional investors. For example, one SME issue in late 2024 (Trafiksol ITS Technologies, discussed later) was reportedly oversubscribed 345 times, a staggering figure indicating a speculative frenzy. Such oversubscription reflects a huge unmet demand on listing, which can drive the stock price higher if even a fraction of that demand chases the limited shares available. This dynamic partly explains the large listing gains seen in certain IPOs. However, it also raises concerns about the quality of demand—whether it is genuine long-term interest or short-term “stag” investors looking to flip for quick profit. In some cases, questions have arisen over whether oversubscription was inflated by coordinated funding arrangements or insider groups—issues that regulators have begun probing.

Liquidity on SME platforms remains lower than on mainboard stocks. Trading volume often drops after initial post-IPO excitement, causing sharp price swings on small trades. Market makers are assigned to each SME stock to provide buy-sell quotes and some liquidity, but their influence usually diminishes once broader trading interest wanes. This illiquidity can trap investors or enable price manipulation in poorly followed stocks. It also means that reported gains on paper might not always be easily realized by large investors without moving the price.

In summary, performance in the SME segment has been a double-edged sword. The segment has undeniably delivered strong returns on average in recent years, which has helped attract more issuers and investors. However, these returns have come with

high volatility. The significant risk of price manipulation and the disparity between winners and losers highlight the need for cautious stock selection and improved regulatory oversight to ensure that price discovery remains fair and truly reflects fundamentals rather than hype.

Fraud Cases and Governance Challenges in The SME Segment

The rapid growth of SME listings has unfortunately been accompanied by an increase in incidents of fraud, misconduct, and corporate governance failures. Several SMEs have come under regulatory scrutiny for serious irregularities, including misuse of IPO proceeds, stock price manipulation, and misleading disclosures. These cases have highlighted the vulnerabilities in the SME ecosystem—such as lighter due diligence requirements, the ease of inflating prices in an illiquid market, and occasionally lax internal controls within these small companies. Below, we discuss a few high-profile cases that have been widely reported, and the governance issues they reveal:

- **Kalahridhaan Trendz Ltd (KTL)** – Deceptive Disclosures and Stock Manipulation: Kalahridhaan Trendz, a textile SME listed on NSE Emerge in early 2024, gained notoriety within its first year of listing. The company made grand announcements about securing a ₹115 crore export order and plans for major expansion, which caused its share price to soar. However, it later came to light that the claimed overseas customer did not exist and the company had also defaulted on undisclosed financial obligations. Essentially, KTL's promoters were allegedly inflating the stock with false news while hiding negative information. SEBI, acting on complaints (including one from a bank regarding unpaid dues), investigated and in early 2025 issued an interim order banning KTL and its promoters from the securities market. The regulator found prima facie evidence that KTL had misled investors with fraudulent announcements and even tried to cover its tracks by fabricating documents when questions arose. The case highlighted how a company could exploit the SME platform by taking advantage of minimal analyst scrutiny and regulatory delays—until action was finally taken. It underscored the importance of strict disclosure norms and the need for exchanges to question unusual corporate announcements proactively.
- **LS Industries Ltd (LSIL)** – *Pump-and-Dump with Collusion*: LS Industries, listed on the BSE SME board, experienced an inexplicable surge in 2024. Despite having negligible revenues and weak financials, its market capitalization soared past ₹5,000 crore as the share price reached ₹267 (from single-digit levels

earlier). SEBI's inquiry revealed that this was not a miraculous turnaround but a scheme orchestrated by insiders. The company's promoter (a finance firm) and associates allegedly allocated a large block of shares (over 10 crore) off-market to a Dubai-based investor for a token price of \$1, creating an unofficial "partner" in the scheme. Subsequently, a network of entities and individuals traded LSIL's shares among themselves to inflate the price (a classic circular trading pattern). Positive announcements by the company, such as plans to acquire Robochef, were timed to sustain the hype. When the stock peaked in late September 2024, the colluding parties offloaded some of their holdings at substantial profit, dumping shares onto unsuspecting public investors. SEBI intervened with an interim order in February 2025, freezing the involved parties from trading and even directing the main perpetrator to impound the illicit gains made (around ₹1.14 crore in profit booked by the NRI investor on sales). The order depicted brazen manipulation – an SME with virtually no real business was inflated to a multi-thousand-crore valuation. This case exposed how low-float SME stocks can be manipulated through insider coordination and raised concerns about potential money laundering or FEMA violations, given the large sums moved overseas under the pretense of the \$1 share transfer and subsequent sales. LSIL's saga has prompted regulators to be far more vigilant about unusual price and volume patterns in SME stocks and to scrutinize off-market transactions around the time of IPOs.

- **Synoptics Technologies Ltd – IPO Funds Siphoning Scam:** Not all misconduct appears as market manipulation; some relate to how IPO funds are managed. Synoptics Technologies, an IT solutions company, launched an IPO on NSE Emerge in July 2023, raising approximately ₹54 crore (₹35 crore from a fresh issue and the rest from an offer-for-sale by promoters). The issue initially struggled with subscription, but a late surge from certain investors ensured full subscription. However, shortly after listing, red flags emerged regarding the use of IPO proceeds. SEBI found that on the day before Synoptics' shares listed, a large ₹19 crore—over half of the fresh issue funds—was transferred out of the escrow account to three entities under the guise of "issue-related expenses." This was highly irregular since the prospectus had estimated only ₹0.8 crore for IPO expenses, and escrow funds aren't meant to be released before finalizing allotments unless for legitimate payments. The transferees turned out to be shell companies—they had no real operations or offices (their addresses led to empty locations) and had been hastily brought in through unsigned agreements. Essentially, it appeared that Synoptics' management, in collusion

with its lead manager First Overseas Capital Ltd (FOCL), devised a plan to divert a large portion of the raised funds into private hands. Further investigations suggested that some of the ₹19 crore might have even been routed to entities that bought Synoptics' shares on the listing day to inflate the price (creating an illusion of strong demand). In May 2025, SEBI took strict action: Synoptics and its three promoters were barred from the market, and FOCL was prohibited from accepting new IPO mandates. This was an unprecedented move to hold a merchant banker accountable across the board. SEBI also announced it would review 20 other SME IPOs managed by FOCL in recent years for similar irregularities, as the Synoptics case indicated a broader pattern of abuse. The Synoptics episode highlights the governance risks around fund utilization in SME issues—in which smaller oversight has allowed some companies and intermediaries to game the system by siphoning off money under false pretences. It has prompted calls for tighter monitoring of IPO proceeds even for smaller issues (which traditionally were exempt from having a monitoring agency if issue size is less than ₹100 crore).

- **Trafiksol ITS Technologies – Shell Vendor and IPO Cancellation:** In a dramatic move, an SME IPO was stopped before it could defraud investors. Trafiksol ITS, a company providing traffic management software, launched an IPO in late 2024 on the BSE SME platform. The IPO appeared successful on paper – oversubscribed hundreds of times, mainly because the company claimed it had a unique product and planned to use the ₹44 crore funds to buy software from an outside vendor to improve its offerings. However, concerns arose for the exchange when due diligence revealed that the supposed vendor was a shell entity with no real operations or ability to deliver the software. Essentially, Trafiksol's plan for fund usage seemed like a sham—potentially a scheme to funnel IPO money to a related party disguised as a software purchase. Recognizing potential fraud, BSE took the rare step of withholding listing approval and referred the matter to SEBI. In December 2024, SEBI cancelled Trafiksol ITS's IPO entirely and ordered the company to refund all investor money, citing misrepresentation and possibly fraudulent intent. This case was significant because it showed a proactive approach: instead of waiting for the stock to list and then investigating, the regulator and exchange stepped in early to prevent the public from falling victim to a scam. It also highlighted a new modus operandi—raising funds ostensibly to buy an asset or service from a fake third party (often controlled by the promoters themselves), effectively pocketing the IPO's proceeds.

- **Gensol Engineering Ltd – Post-listing Governance Breakdown:** Gensol serves as a cautionary tale demonstrating that issues can surface even after a successful migration to the main board. Gensol, a solar power and EV leasing company, initially listed on the SME exchange and later moved to the main exchange as its market cap grew into the thousands of crores. However, in 2024–25, SEBI began investigating Gensol following complaints of fund diversion and financial misreporting. Investigations revealed that Gensol’s promoters allegedly diverted large loans—intended for purchasing electric vehicles—into their personal businesses and assets. The company also submitted forged documents to credit rating agencies to conceal loan defaults. By mid-2025, SEBI’s confirmatory order upheld findings that the promoters engaged in serious governance violations—including creating fake purchase orders, siphoning off over ₹200 crore from loans, and making false announcements about orders and production that never materialized. Gensol’s case shows that even relatively prominent companies can fall victim to governance failures, and that SME-origin companies might carry weaker internal controls if not strengthened over time. It underscores the importance of ongoing regulatory supervision even after SMEs graduate from the dedicated platform.

These examples demonstrate a range of fraudulent behaviors – from market manipulation (KTL, LS Industries) to misuse of funds (Synoptics, Trafiksol), and broader corporate fraud (Gensol). Common themes in many SME cases include: promoters exploiting information asymmetry (few people scrutinizing their claims), collusion with intermediaries or friendly entities to influence outcomes, and the challenges investors face in verifying the credibility of these smaller firms’ disclosures. Corporate governance at many SME firms is typically weaker – boards often dominated by promoters, internal controls not strong, and even basic requirements like appointing a qualified Company Secretary or compliance officer are sometimes ignored. For example, KTL did not appoint the required compliance officer and falsely claimed to have independent directors. These lapses create an environment where unethical management can act unchecked until regulators catch on.

Another challenge is that by the time regulators act—which, to SEBI’s credit, has been fairly quick in recent cases—the damage may already have occurred. Share prices might have collapsed, or unsuspecting investors might have bought at inflated levels. SEBI’s interim orders that bar entities do help freeze further harm and send a deterrent message, but they cannot fully recover losses suffered by public shareholders in a pump-and-dump scheme. That’s why preventive measures and stronger initial

screening are essential, so that such companies either don't get listed in the first place or are unable to commit fraud post-listing.

Regulatory Measures in India's SME Segment

Regulators have continuously refined the SME IPO framework since its inception to address emerging issues. Both the stock exchanges (BSE and NSE, which operate the SME platforms) and SEBI have issued guidelines, circulars, and rule changes over the years aimed at strengthening listing criteria, trading mechanisms, and investor safeguards for SMEs. Here, we outline the key regulatory measures and how they aim to address the challenges:

- **Entry and Listing Criteria:** SME IPO norms began with relatively easy thresholds—like post-issue capital under ₹25 crore, 2–3 years of operational history, and positive net worth—to encourage broader participation. But as misuse surfaced, exchanges tightened the filters.

In 2015, BSE added checks like a ₹3 crore tangible asset minimum and profit/net worth criteria to block shell firms. By 2016, migration to the main board required a ₹10 crore capital floor, market cap thresholds, and shareholder approval to deter backdoor listings.

In April 2025, NSE followed suit—raising its migration bar further to ensure only scaled, credible SMEs move up. The shift signals a clear regulatory intent: ease of access, not ease of abuse.

- **Minimum Application Size and Allotment:** One distinctive rule from the beginning was that SME IPOs have a minimum application and trading lot size of ₹1 lakh (or even higher in some cases. This was designed to keep very small retail investors out, based on the idea that SME stocks are risky and should only be in the hands of investors who understand and can absorb losses (usually HNIs or institutional investors). While this has limited retail participation, it has also meant that relatively few investors hold the float of an SME stock, unintentionally making price corners easier. Regulators have stuck to this rule so far, though there are ongoing discussions about whether reducing the lot size could expand the investor base and improve liquidity.
- **Market Making Requirement:** To address liquidity concerns, regulations require each SME IPO to appoint one or more market makers who must provide two-way quotes for a minimum period (at least 3 years from listing) and for a certain minimum quantity of shares. Market makers are meant to

facilitate trading and reduce volatility by acting as ready buyers and sellers. In practice, this mechanism has had mixed results—while it offers initial support, market makers themselves often have limited capacity and interest if there is no broader market demand. Nonetheless, the requirement ensures someone is obligated to make a market, and exchanges have issued detailed guidelines for market makers (including inventory management and spread) to prevent undue price manipulation. BSE's circular in 2012 on inventory management for market makers aimed at clarifying how they can build or reduce positions without destabilizing the market.

- **Trading Mechanism Safeguards (Call Auction and Price Bands):** Recognizing the potential for wild swings when a stock first lists, SEBI in 2012 introduced a call auction mechanism for the IPO opening day. Under this, on the first trading day, instead of continuous trading immediately, a 60-minute call auction session occurs at market open where buy and sell orders accumulate, and an equilibrium price is determined. This approach was designed to improve price discovery and prevent situations where low float could lead to rapid 100% upside or downside within minutes. After the call auction sets the initial price (the listing price), regular trading begins. Initially, exchanges had separate call auctions and price bands, which sometimes caused disparities—one exchange's price band being significantly higher than another's if their equilibrium prices differed. In April 2023, SEBI refined this process by requiring that if the two exchanges' discovered prices differ beyond a specified range, they will calculate a volume-weighted common equilibrium price and apply uniform price bands based on that. Additionally, SEBI introduced fixed price band limits for the first day of trading for re-listed stocks and IPOs: for example, if an IPO opens via call auction, it may carry a band (such as $\pm 5\%$ or $\pm 20\%$, depending on criteria) for the rest of the first day to prevent extreme moves beyond the auction-determined price. These measures have helped temper day-one volatility, although, as observed in 2024, swings of 70–100% still occurred in some cases—possibly because the price bands on SME stocks were not as tight, or because the equilibrium price was set very high by exuberant orders).
- **Use of Unified Payment Mechanism (UPI) and ASBA:** In 2021, SEBI expanded the use of the ASBA (Applications Supported by Blocked Amount) and UPI payment system to SME IPOs, simplifying the application process. Previously, SME IPO subscriptions were sometimes managed by brokers and sub-brokers with less transparency, and there were reports of funding arrangements where

a financier would fund multiple applications to inflate HNI subscriptions. By mandating ASBA—where investor funds are blocked in their own bank account and released only upon allotment—and UPI for retail bids, the process became more secure and aligned with mainboard IPOs. In mid-2024, after noticing some malpractices, NSE issued circulars about systemic improvements in the bidding process for SME IPOs, including testing sessions (mock bidding) to ensure all stakeholders understood the new procedures. By June 2025, new SEBI (Issue of Capital and Disclosure Requirements) regulations came into effect, requiring SME issues to adhere more closely to the standard IPO bidding process—essentially eliminating any differential treatment that allowed opacity. These changes aim to prevent artificial oversubscription and ensure each application is individually verified (for example, one PAN equals one application in retail), making it more difficult for a single party to manipulate the system with multiple benami applications.

- **Monitoring of Funds:** Traditionally, only main-board IPOs above ₹100 crore required the appointment of a Monitoring Agency (usually a bank or financial institution) to track the use of issue proceeds and report deviations. Most SME IPOs are below that threshold, so they were exempt from this requirement. However, in light of cases like Synoptics, the regulator has begun to tighten oversight on fund usage. As an immediate step in 2025, SEBI directed that ongoing IPOs managed by the tainted merchant banker (FOCL) must appoint independent monitoring, even if smaller, and more broadly, there is consideration to lower the threshold for SMEs. Additionally, SEBI regulations already mandate that companies periodically disclose the status of utilization of IPO proceeds in their financial reports until the money is fully utilized – this rule applies to SMEs too. The enforcement of this (ensuring SMEs publish and audit those utilization statements) is an area being strengthened.
- **Disclosure and Governance Requirements:** Once listed, SME companies are subject to simplified versions of the SEBI Listing Obligations and Disclosure Requirements (LODR). Some relaxations were initially granted—for example, SMEs can submit abridged annual reports, and certain corporate governance norms, like mandatory board composition, were slightly eased. However, after observing misuse, SEBI and exchanges have moved closer to aligning with mainboard standards. For instance, timely disclosure of material events, quarterly results, and shareholding patterns are now required for SMEs just as they are for other companies. SEBI has also emphasized that SME firms must have independent directors and audit committees, with some flexibility on

composition due to smaller board sizes. Enforcement of LODR on SMEs has increased: exchanges now penalize SMEs for failing to file results or for non-compliance, similar to mainboard companies—though fines are sometimes lower. The KTL case, where no compliance officer was present, likely prompted exchanges to verify that newly listed SMEs have appointed the required compliance officer and company secretary as per norms.

- **Surveillance and Enforcement Actions:** Both BSE and NSE have dedicated surveillance teams monitoring SME trading. Unusual price movements, high volumes without news, or bulk deals are scrutinized. Exchanges have, on a few occasions, moved SME stocks to the trade-to-trade segment (where no intraday trading is allowed) or even suspended trading when extreme manipulation is suspected. SEBI, for its part, has become quicker to issue interim orders in serious cases. The use of interim orders to immediately bar companies and perpetrators (as seen in KTL, LS Industries, Synoptics, etc.) demonstrates a no-tolerance stance – even when investigations are ongoing, the regulator opts to freeze activity to prevent further harm. This is a powerful tool in a relatively illiquid market, as it stops the suspect stock from trading further, protecting new investors from wandering in. SEBI has also begun taking action against intermediaries: aside from the FOCL ban, SEBI fined a few merchant bankers in the past for due diligence lapses on SME IPOs. In 2019, one merchant banker (Corporate Capital Ventures) was barred for launching several questionable SMEs without proper checks. These enforcement actions send a message to the ecosystem that investment bankers and other advisors must thoroughly vet SME issuers or face consequences.

Despite all these measures, the question remains: are they enough? The regulatory approach has mostly been reactive — tightening rules after scams have already occurred. For example, SEBI only cracked down on merchant bankers after multiple IPO fund diversions; the bidding process was only revamped after extreme oversubscriptions. There may still be gaps in prevention. The SME platform inherently sacrifices some investor protections for easier access, creating a natural tension. Some argue that fundamental reforms, like those in the Recommendations section, are necessary to prevent issues before they happen rather than just fixing them afterward. However, regulators have also shown increasing agility recently — intervening in real time (as with Trafiksol) and continuously updating guidelines. The adequacy of these measures is an ongoing challenge: as fraudsters discover new loopholes, regulators must adapt and close these gaps.

International Perspectives: SME Boards in UK, Hong Kong, and Japan

India is not alone in grappling with the challenge of balancing SME capital access with investor protection. Many countries have secondary boards or alternative investment markets for smaller companies. The experiences of the UK's AIM, Hong Kong's GEM, and Japan's Mothers (now reorganized as the TSE Growth Market) offer valuable insights into regulatory approaches for SME listings and governance.

- **United Kingdom – AIM (Alternative Investment Market):** The London Stock Exchange's AIM, launched in 1995, is one of the earliest and most successful SME-focused markets globally. AIM has a distinctly different regulatory approach: it operates on a “comply or explain” basis with no minimum financial requirements for listing—no profit or revenue thresholds—yet it relies heavily on the role of Nominated Advisers (Nomads). Every AIM-listed company must have a SEBI-registered Nomad—an approved investment bank or advisory firm—that essentially vouches for the company's suitability at admission and oversees its compliance continuously. The Nomad conducts due diligence before the IPO, ensuring the company meets governance standards and discloses all risks. After listing, the Nomad guides the company on fulfilling all AIM rules and must be informed of any major developments; if a company loses its Nomad, trading in its stock is suspended, highlighting how crucial this sponsor role is. This framework places the responsibility for regulation on private advisors under exchange supervision rather than direct regulatory vetting of the companies. The advantage is increased flexibility and speed—small companies can list relatively quickly if a Nomad is willing to sponsor them—which has made AIM home to thousands of companies (including many from outside the UK). However, this approach has faced criticism whenever scandals occur, as it's sometimes alleged that Nomads overlook red flags due to conflicts of interest (they earn fees from bringing companies to market). Over the years, AIM authorities have tightened oversight of Nomads, even revoking licenses of those found negligent, and they introduced a Nomad code of conduct. They also raised the standards slightly by requiring an auditor's report and minimum free float. Overall, AIM's experience demonstrates that delegated regulation via nominated advisors can be effective, but it requires strong accountability mechanisms for those advisors. An important aspect is that AIM has no lock-in requirement for promoters beyond what Nomads might insist, which some argue can lead to quick share dumps. By and large, however, the reputation of the Nomad and

the necessity of maintaining investor confidence have kept outright fraud on AIM relatively low, though not zero.

- **Hong Kong – GEM (Growth Enterprise Market):** Hong Kong's GEM was established in 1999 as a secondary board to complement the main HKEX board, targeting emerging companies and those that couldn't meet the main board's profit track record. Initially, GEM had very lax rules – no profit requirement and a relatively low market cap requirement – and it operated on a disclosure-based regime with a sponsor system (similar to Nomads) for IPOs. In the early years, GEM became notorious for speculative stocks and shell companies. Many small firms listed on GEM not so much to raise growth capital but seemingly to attain a listing status and then sell their listed shell to others (shell value trading). There were instances of extreme volatility and manipulation, where controlling shareholders allegedly placed most of the IPO shares with friendly “investors” who would then trade among themselves to inflate prices (similar to what we've seen on Indian SME exchanges). Hong Kong regulators responded with a series of reforms. In 2017–2018, GEM listing requirements were made more stringent to improve quality: the minimum cash flow or revenue criteria were increased, and the minimum market capitalization at listing was doubled (to HK\$150 million). A key change was lengthening the lock-up period for controlling shareholders – originally, GEM founders could sell after one year, but it was extended to two years lock-up to ensure they remain committed. Also, the earlier rule that allowed GEM companies to migrate to the main board after just one year of good compliance was abolished (now they must essentially meet main board criteria to uplist). Hong Kong's Securities and Futures Commission (SFC) also issued guidelines to sponsors, underwriters, and placing agents to prevent inflated IPOs with concentrated ownership. It became expected for sponsors to ensure a diverse investor base in the IPO (not just a few insiders taking all shares). The regulators increased scrutiny of GEM IPO allocation – any suspicious clustering of shareholders (like many with the same address or network) could trigger an inquiry. These measures significantly reduced shell activities. While GEM remains smaller than the main board, its governance standards have improved: companies now must follow nearly the same continuous disclosure rules as main board firms, and sponsors can be held liable for any misstatements in prospectuses (imposing diligence duties). Hong Kong's experience highlights the need to close loopholes that enable price rigging, such as ensuring adequate free float

and genuine investor participation, and enforcing lock-ups to align promoter incentives.

- **Japan – Mothers / TSE Growth Market:** Japan's Tokyo Stock Exchange operated multiple sections for listings, and in 1999, it created "Mothers" (Market of the High-Growth and Emerging Stocks) as a platform for startups and SMEs with high growth potential but not necessarily a profit history. Mothers had no profitability requirement, unlike the main board, which required cumulative profits. However, Japan compensated with a very meticulous vetting process: lead underwriters (sponsors) in Japan perform rigorous due diligence and essentially guarantee a certain level of corporate governance. Companies had to produce detailed prospectuses, and the exchange could refuse listing if it weren't satisfied with business viability or the integrity of management. An interesting feature in Japan is the role of the exchange's self-regulatory body – the TSE has a division that reviews listing applications thoroughly, and even after listing, monitors compliance. Companies on Mothers were required to have periodic reporting, internal controls review, and at least one independent director. Insider trading laws and penalties for false disclosures are strict in Japan, which deters egregious fraud. Consequently, while Mothers saw volatile stocks (due to speculative fervor in tech startups, especially), it did not face as many outright scams as seen in some other emerging markets. In 2022, Japan restructured its markets into new segments: Prime, Standard, and Growth. The Growth Market largely replaced Mothers and continues to cater to early-stage companies. Under the new framework, listing standards on the Growth Market still don't require profit, but companies must present a reasonable business plan and meet criteria like market cap $\geq$ ¥4 billion (approx ₹240 crore) and shareholder distribution requirements. Notably, Japan emphasizes transparency and investor awareness – for example, companies listing on the Growth Market often provide business outcome metrics and risk factors extensively, and regulators require alerting investors that these are high-risk stocks. If a Growth Market company fails to show progress (for instance, if it remains loss-making with no growth), the exchange can designate it for delisting or transfer to a lower segment, thereby maintaining overall quality. Japan's approach underscores the value of robust self-regulation and a culture of compliance. Even small firms there are accustomed to proper books and audits (often due to Japan's corporate culture and the presence of seasoned independent directors in many firms). Governance issues can still occur (there have been cases of accounting

fraud in small tech firms), but the system's emphasis on constant oversight and the fact that investor lawsuits are a real threat in Japan tend to keep management in check.

Key Takeaways from International Markets: A common theme is that SME boards worldwide face the risk of becoming dumping grounds for dubious companies if not closely monitored. The UK, Hong Kong, and Japan all adjusted their regulatory frameworks over time to curb abuses:

India's SME markets—though designed with the intent to support early-stage, growth-oriented companies—have faced persistent challenges in ensuring credible listings and safeguarding investor interests. In light of repeated instances of price manipulation, corporate governance failures, and misuse of public capital, it is instructive to examine how global SME platforms address these vulnerabilities.

The **UK's Alternative Investment Market (AIM)** offers a model that India could adapt with contextual care. Rather than subjecting issuers to rigid financial thresholds, AIM relies on **Nominated Advisers (Nomads)** as professional gatekeepers who vouch for the company's credibility and regulatory preparedness. This sponsor-based approach enables greater flexibility in access to capital markets while placing accountability squarely on intermediaries.

For India, introducing a similar Nomad-like structure for SME IPOs could create a layer of professional due diligence that goes beyond compliance checklists—particularly given the uneven quality of merchant bankers currently serving the segment.

The **Hong Kong GEM Board** experience highlights another critical lesson for India: the dangers of **shareholding concentration and shell creation**. Several Indian SME IPOs have seen disproportionate allocations to connected parties or small groups of investors, followed by sharp price movements post-listing. GEM addresses this by mandating

- Genuine public float distribution,
- Applying lock-in periods for key shareholders, and
- Subjecting IPO subscriptions and secondary market activity to regulatory scrutiny for manipulation patterns.

India's exchanges have begun introducing similar guardrails (e.g., enhanced surveillance measures and IPO grading), but enforcement and real-time analytics must improve to prevent fraudulent recycling of capital and artificial price ramping.

Meanwhile, **Japan's Mothers and TSE Growth boards** demonstrate how even early-stage or pre-profit companies can be effectively regulated—if robust listing reviews, mandatory governance structures, and exchange-led self-regulation are implemented with cultural and institutional discipline. In India, the governance structure of SME-listed companies is often weak, with promoter dominance and board independence more symbolic than real. Drawing from Japan, Indian exchanges could consider:

- Mandatory governance scorecards,
- Pre-listing board independence verification, and
- Post-listing disclosures on operational milestones, which would shift the narrative from compliance to stewardship.

Together, these models point to a core regulatory principle India must adopt: focus less on eligibility thresholds and more on systemic accountability, gatekeeping quality, post-listing enforcement, and investor protection protocols.

These lessons can inform improvements in India's SME regulatory framework. In particular, adopting aspects of the Nomad/sponsor system for continuous oversight, ensuring better float and lock-in conditions to deter pump-and-dump, and strengthening exchange surveillance and diligence at entry are useful strategies.

Policy Recommendations and Conclusion

The SME IPO segment in India has unlocked capital for hundreds of entrepreneurs and provided investors with opportunities for high-growth investments. To ensure its sustainable development and to protect investors from recent frauds, additional regulatory and policy measures should be considered. Below are several recommendations that stem from the analysis of current gaps and global best practices:

- **Enhance Due Diligence and Accountability of Intermediaries:** Enhance the responsibility of merchant bankers (lead managers) in SME IPOs, similar to the Nomad concept. Regulators could require the lead manager for an SME issue to assume a continuous advisory role for, say, 1-2 years after listing. This “sponsor” would be held accountable to the exchange for the company's compliance and must certify annually that the company follows governance norms. If a company is found to have misled investors, both the company and the sponsoring intermediary should face sanctions. This creates a strong incentive for merchant bankers to thoroughly vet issuers (beyond merely completing the IPO). SEBI can formalize this through regulations by defining

the role and duties of such a sponsor, drawing from elements of the AIM Nomad rulebook.

- **Tighten IPO Fund Utilization Oversight:** Introduce mandatory monitoring of issue proceeds for SME IPOs above a reasonably low threshold, such as ₹25 crore—significantly lower than the current ₹100 crore threshold. An independent monitoring agency should oversee the deployment of funds and publish reports. Even below that threshold, require the company’s audit committee to submit a quarterly report to the exchange on fund utilization until the proceeds are fully used. Any deviations from the intended use should be flagged and require prior shareholder approval. Additionally, escrow release of funds could be made conditional on specific verifications — for example, if ₹X crore is allocated for purchasing software or assets, verify that the supplier is legitimate and the contract is valid before releasing the funds.
- **Improve Transparency and Disclosure:** Mandate more detailed disclosures from SME IPO aspirants. For instance, if an SME’s business plan or valuation heavily depends on a few key contracts or clients, the issuer should be required to disclose those names (or at least the nature and current status of those contracts) in the prospectus. This reduces the risk of a “fake order” scenario like KTL. Additionally, require disclosure of any previous regulatory or legal proceedings against promoters or directors in the offer document (some already do this, but ensuring full transparency helps investors assess promoter integrity). After listing, exchanges should ensure SMEs quickly disclose all material developments. If an SME makes aggressive forward-looking statements (like large expansion plans), regulators could request clarification or a progress update filing after a few months, thereby deterring blatant lies.
- **Revise Minimum Lot Size and Investor Participation Norms:** Re-evaluate the ₹1 lakh minimum investment rule. While it was introduced to protect small investors, its side effect of concentrated ownership is problematic. A potential middle ground is to reduce the minimum lot size to, say, ₹25,000 or ₹50,000 – still enough to discourage casual small bets, but allowing a broader base of investors. A wider investor base makes manipulation more difficult, as holdings aren’t concentrated in a few hands. Additionally, consider mandating that a small portion of each SME IPO is allocated to institutional investors (for example, at least 10% to mutual funds, AIFs, etc., if they bid). Institutional participation typically improves due diligence and post-listing oversight. If institutions show zero interest, that alone signals issues with the issue quality.

- **Strengthen Corporate Governance Requirements:** Insist on higher governance standards for SMEs that are proportional to their size. For instance, if an SME exceeds a certain market cap (say ₹500 crore) while still on the SME platform, it should automatically be required to follow main-board corporate governance norms (e.g., have half the board as independent directors, establish all key committees). This approach ensures that companies experiencing rapid growth (like some have) must strengthen their governance, which could help prevent certain abuses. Additionally, enforce the existing rule that each SME must have a qualified Company Secretary and compliance officer; the exchanges should verify this during listing and follow up if the position is vacant. Regular secretarial audits could be mandated for SMEs to ensure compliance with LODR and the Companies Act provisions.

Deploy Focused Surveillance and Early-Warning Systems: The growing misuse of SME IPO platforms—evident in cases like Gensol, Synoptics, and others—calls for proactive, data-driven surveillance rather than reactive regulation. SEBI and stock exchanges must adopt AI-enabled analytics to detect early warning signals of manipulation or governance breakdowns.

Specific patterns should trigger automated alerts:

- IPO cornering by a small set of entities, potentially using related accounts.
- Price surges without corresponding liquidity, indicating illiquid spurts or price rigging.
- Sharp increase in shareholder count, which may stem from artificially splitting holdings to meet listing or migration norms.

Beyond flagging red flags, SEBI could implement a surveillance risk index specifically for SME scrips. This index can score companies across two dimensions:

- **Governance risk:** compliance track record, auditor remarks, board independence, related party transactions.
- **Market risk:** price volatility, ownership concentration, low float liquidity, and unusual trading behavior.

Scrips with elevated risk scores can be subjected to additional regulatory measures:

- Mandatory quarterly audited financial disclosures (beyond the statutory half-yearly reporting).
- Trading restrictions, such as narrowing the price band to 5% or limiting order types.

- Enhanced disclosures on promoter activity, capital deployment, and business updates.

This **risk-based supervision model** will help regulators and exchanges concentrate oversight where it matters most—on potentially vulnerable or manipulated listings—without burdening well-run SMEs with excessive compliance.

As SME markets mature, such tiered regulation—enabled by tech, driven by risk, and grounded in market intelligence—can protect investors while sustaining entrepreneurial access to capital.

- **Tighten Lock-in and Vesting Schedules:** Currently, promoters' pre-IPO capital in an SME is locked in for 3 years, similar to the main board rules for promoters in companies without profitability. However, cases like LS Industries demonstrate that creative tactics—such as allotting shares very cheaply to an outside ally just before the IPO—can bypass the definition of who is considered a “promoter” at the time of listing. Regulators should extend lock-in requirements to major pre-IPO shareholders as well, not just those formally classified as promoters. For instance, anyone holding more than 5% pre-IPO should be locked in for at least 1-2 years on the SME platform to prevent quick exit by big shareholders. Additionally, if new investors receive shares within, say, 6 months before the IPO, those transactions should be disclosed and locked to prevent short-term flipping after listing. This measure lessens the incentive for insiders to introduce proxy investors to manipulate the process, such as in the case of the \$1 share transfer in LSIL.
- **Investor Education and Research:** Encourage or mandate the publication of research reports on SME companies. In the early days of BSE SME, there was a system where the exchange or lead broker would produce a research report for each SME issuer. Reviving this in a more effective form could be beneficial. SEBI/Exchanges could create a panel of independent research analysts or firms to cover SME stocks, possibly funded through a small portion of listing fees. Having at least one or two objective analytical reports available makes it more difficult for company management to spin an exaggerated story without challenge. Additionally, investor education programs specifically warning about SME investing should be held—many retail and HNI investors jumping in may not realize that liquidity and information risks are significantly higher. Exchanges can conduct webinars or publish case studies (such as summarizing past frauds) to inform investors.

- **Legal and Penal Deterrence:** Finally, strengthen the legal penalties for fraud in this area. SEBI already enforces bans and monetary fines, but criminal charges should be pursued in serious cases as a deterrent. For instance, if IPO proceeds are diverted (which essentially cheats investors), cases under India's securities laws and even the IPC (Indian Penal Code) for fraud can be filed, possibly leading to jail time. A few high-profile prosecutions (with cooperation from SFIO or CBI for financial fraud) would send a strong message. Also, holding auditing firms accountable—if an SME's auditor is found complicit or grossly negligent in overlooking red flags—SEBI should be able to ban that auditor from auditing any listed company. Building a culture of accountability among all gatekeepers will boost trust in the SME market.

In conclusion, the SME IPO market in India is at a crucial turning point. Its growth pattern is impressive, showing the strong demand for capital from small businesses and the eagerness for expansion among investors. With proper support, it can develop into a lively platform that produces the next wave of mid-cap and large-cap companies. However, protecting the integrity of this market must be a priority through strong regulation and enforcement. The recent frauds and manipulations, while alarming, have served as a wake-up call that has prompted regulators to respond. By adopting the recommendations – drawing on both local lessons and international best practices—exchanges and SEBI can effectively reduce the risks and improve market reliability.

The aim should be to create an environment where genuine entrepreneurs can raise funds efficiently and investors can participate with confidence, knowing that there are adequate checks against malfeasance. Achieving this balance is challenging but attainable. The experiences of markets like AIM, GEM, and Mothers show that continuous adaptation of regulations is key. India's regulators have already taken many positive steps (such as improving transparency in the IPO process and clamping down on offenders swiftly). Going forward, a combination of stricter pre-listing scrutiny, better post-listing monitoring, and a culture of compliance will go a long way in ensuring the SME segment's success is built on a solid foundation.

Ultimately, the credibility of the SME platform is its most valuable asset—and protecting it is crucial for the long-term sustainability of this important part of India's capital markets. With careful policy adjustments and vigilant oversight, the SME IPO market can continue to grow, providing benefits to companies and investors alike, without being hindered by governance issues or failures.