

## Should you invest in low free-float stocks?

When a company issues shares, not all of them are made available to the public for trading. A big chunk is typically held by the promoters or the government, which is not open to public trading. The portion of shares that is publicly traded is referred to as the 'free float' or 'public float' of the company.

Traditionally, promoters of Indian companies have been wary of sharing their prized asset with public. In fact, the free-float capitalisation of Indian firms is among the lowest in both the developed and emerging markets. Many companies are managed by families, which prefer to exert control by way of a higher level of ownership in the firm. While this leaves very little in the hands of the small investor, careful stock selection can help them benefit from companies with a low free float, or limited number of actively traded shares.

### Rewarding option

Low [free-float stocks](#) can be a good investment bet because their prices can move up quickly. If such a stock attracts the attention of even a few investors, the demand-supply mismatch can push up its price. [Vikas Gupta](#), Executive Vice-President, Arthveda Fund Management, says, "The low free-float stocks tend to have lesser liquidity, which can result in a possible mispricing of the stock. Investors with a low ticket size can capitalise on this mispricing." Besides, low-float companies are prime candidates for de-listing.

### *Low-float stocks with high institutional holding*

| Company            | Non-promoter holding (%) | Institutional holding (%) | Inst. holding as % of public float |
|--------------------|--------------------------|---------------------------|------------------------------------|
| Adani Enterprises  | 25.00                    | 21.59                     | 86                                 |
| HCL Technologies   | 38.47                    | 32.71                     | 85                                 |
| Marico             | 40.31                    | 33.90                     | 84                                 |
| Mahindra Finance   | 47.95                    | 42.61                     | 89                                 |
| Jubilant Foodworks | 50.45                    | 46.70                     | 93                                 |
| Hathway Cable      | 52.49                    | 48.06                     | 92                                 |
| Zee Entertainment  | 56.93                    | 52.23                     | 92                                 |
| Max India          | 59.52                    | 50.86                     | 85                                 |

*Data compiled by ETIG*

If the company does not follow the rule of a minimum public shareholding of 25%—as prescribed by the Securities and Exchange Board of India—it is likely to buy back its shares at a premium to the existing price and de-list from the exchanges. This can yield a windfall for the investor.

### Watch out for

However, experts flag some issues related to low free-float stocks. There are very few that are good for investment. Typically, shares with a higher float are associated with better governance since the promoter has lesser influence and other shareholders have more power to exercise their rights. The stocks with a low public float are open to the promoters' whims. "The promoters who hold their stocks closely for the purpose of exercising control over the company find it easy to manipulate the stock price for their gain," says Yogesh Nagaonkar, Vice-President, Institutional Equities, Bonanza Portfolio.

Free-float shares are held by domestic and foreign financial institutions, corporate entities, high net worth individuals and retail investors. In several cases, institutions hold a sizeable chunk of the float. "If institutions hold more than 80% of the company's public float, it leaves little room for further play. This could expose the stock to a risk of price drop. [Retail investors](#) can consider stocks where institutional holding is still a small portion of the overall public float," says Gupta. Some low-float stocks with a comparatively lower institutional holding include Berger Paints, Godrej Industries, Oracle [Financial Services](#), Emami, [GlaxoSmithKline](#) Consumer Healthcare, Bosch and [Pidilite Industries](#).

### ***Low free-float stocks with low institutional holding***

| Company           | Non-promoter holding (%) | Institutional holding (%) | Inst holding as % of public float |
|-------------------|--------------------------|---------------------------|-----------------------------------|
| Essar Oil         | 9.46                     | 3.15                      | 33                                |
| Videocon Ind      | 23.17                    | 11.67                     | 50                                |
| Wipro             | 24.63                    | 13.64                     | 55                                |
| Reliance Power    | 24.99                    | 11.69                     | 47                                |
| JSW Energy        | 25.00                    | 12.15                     | 49                                |
| Siemens           | 25.00                    | 13.46                     | 54                                |
| Adani Power       | 25.00                    | 7.59                      | 30                                |
| GlaxoSmith Pharma | 25.00                    | 11.57                     | 46                                |
| L&T Fin Holdings  | 25.02                    | 5.85                      | 23                                |
| Berger Paints     | 25.04                    | 14.25                     | 57                                |
| Cadila Healthcare | 25.20                    | 14.51                     | 58                                |
| Wockhardt         | 25.34                    | 8.27                      | 33                                |
| Oracle Fin Serv   | 25.44                    | 14.05                     | 55                                |
| Dish TV           | 27.53                    | 14.98                     | 54                                |
| GlaxoSmith C H L  | 27.54                    | 12.93                     | 47                                |

Investors also need to be wary of the valuations of low-float stocks, say experts. Due to the low supply, stock prices can rise high and valuations can become stretched. "If institutions are already holding 80-90% of the free float, it is likely that valuations will be on the higher side," says Gupta. Low-float stocks also tend to be volatile. The faster they rise, the sharper the likelihood of their fall, and the smaller the float, the higher the risk of volatility.