STUDY NOTES · BASIC CONCEPT

What Is a Rights Issue & Equity Dilution? What Is the Difference Between Equity and Debt Financing?

Indian Economy

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A. What Is a Rights Issue?

A rights issue is an offer by a company to its existing shareholders to purchase additional shares, usually in proportion to their current holdings.

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Objectives:

1. Raise fresh equity capital.
2. Finance expansion and business operations.
3. Repay or reduce debt.
4. Improve financial flexibility.
5. Give existing shareholders an opportunity to maintain their ownership percentage.
6. Unlike a public issue aimed at the broader investing public, a rights issue initially offers shares to eligible existing shareholders.

B. Face Value vs Issue Price vs Premium

Term	Meaning	Ola Electric example
Face value	Nominal value assigned to a share in the company's capital structure	₹10
Issue price	Price at which the new share is offered	₹27

Term	Meaning	Ola Electric example
Share premium	Amount charged above face value	₹17

Formula:

Issue price = Face value + Share premium

For Ola Electric:

₹27 = ₹10 + ₹17

The share premium forms part of the company's share capital-related reserves under applicable accounting and company-law provisions; it is not the same as operating profit.

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C. What Is a Record Date?

The record date is the date used to determine which shareholders qualify for a corporate action, such as a rights issue or dividend.

For Ola Electric, the announced record date is 13 October 2026.

Eligibility depends on the applicable securities settlement arrangements and the company's announced terms. Investors should verify the relevant deadlines rather than assuming that purchasing shares on the record date will necessarily establish eligibility.

D. What Is a Rights Ratio?

The rights ratio specifies how many new shares an eligible shareholder may apply for relative to existing shares held.

Ola Electric's announced ratio is 2:25.

This means:

- Holding 25 existing shares gives an entitlement to apply for 2 additional shares.

- Holding 250 existing shares gives an entitlement to apply for 20 additional shares.

Fractional entitlements, where relevant, are handled according to the issue's terms.

E. What Is Equity Dilution?

Equity dilution occurs when a shareholder's percentage ownership decreases because the total number of outstanding shares increases and that shareholder does not acquire a proportionate number of new shares.

Example:

Suppose a company has 100 shares, and an investor owns 10 shares. Their ownership is 10%.

If the company issues another 100 shares and the investor buys none, the investor still owns 10 shares, but total shares become 200.

Their ownership falls to 5%.

A rights issue gives eligible shareholders an opportunity to reduce or avoid this dilution by subscribing to their entitlement, although they must invest additional money.

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F. Rights Issue vs Bonus Issue vs IPO

Feature	Rights issue	Bonus issue	IPO
Purpose	Raise fresh equity capital	Capitalise eligible reserves by issuing additional shares	Raise capital and/or enable existing shareholders to sell shares to public investors
Who receives shares?	Eligible existing shareholders initially	Eligible existing shareholders	Public investors, according to the offer structure
Payment by shareholder	Yes, at the issue price	No separate payment for the bonus shares	Yes, at the offer price

Feature	Rights issue	Bonus issue	IPO
Does the company receive fresh funds?	Yes, if subscribed and paid	No	Yes for a fresh issue; not for an offer for sale

G. What Is the Difference Between Equity and Debt Financing?

Equity financing

1. Raises capital by issuing ownership shares.
2. Does not create a contractual obligation to repay principal like a loan.
3. May dilute existing ownership.
4. Shareholders participate in the company's financial upside and bear investment risk.

Debt financing

1. Raises funds through loans, bonds or other borrowing.
2. Creates repayment and interest obligations under the contract.
3. Does not ordinarily dilute ownership.
4. Increases financial leverage and may raise refinancing risk.
5. Companies choose between equity and debt based on their cash flows, borrowing capacity, funding costs and strategic needs.

H. Why Does a Company Raise Capital?

A company may raise capital to:

1. Expand production capacity.
2. Invest in research and development.
3. Develop new products or enter new markets.
4. Meet working-capital requirements.
5. Repay or refinance debt.
6. Strengthen its balance sheet.

The value of a fundraising exercise depends not only on how much money is raised but also on whether the proceeds are used efficiently and generate sustainable returns.

I. Role of SEBI and Stock Exchanges

The Securities and Exchange Board of India (SEBI) regulates India's securities market and protects investor interests under the applicable legal framework.

Rights issues by listed companies are governed by the Companies Act, 2013, and relevant SEBI regulations, including the Issue of Capital and Disclosure Requirements framework.

Stock exchanges provide a regulated trading platform and require listed companies to make prescribed disclosures. Investors should examine the company's formal offer documents for eligibility, payment terms, risks and procedures.

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Relevance for UPSC

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- GS Paper III: Capital markets, corporate financing, investment and financial stability.
- GS Paper III: Business growth, debt management and resource mobilisation.
- Economy: Equity versus debt, share capital, corporate governance and investor protection.