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# A STUDY ON THE PERFORMANCE OF THE INITIAL PUBLIC OFFERINGS IN INDIAN STOCK MARKET

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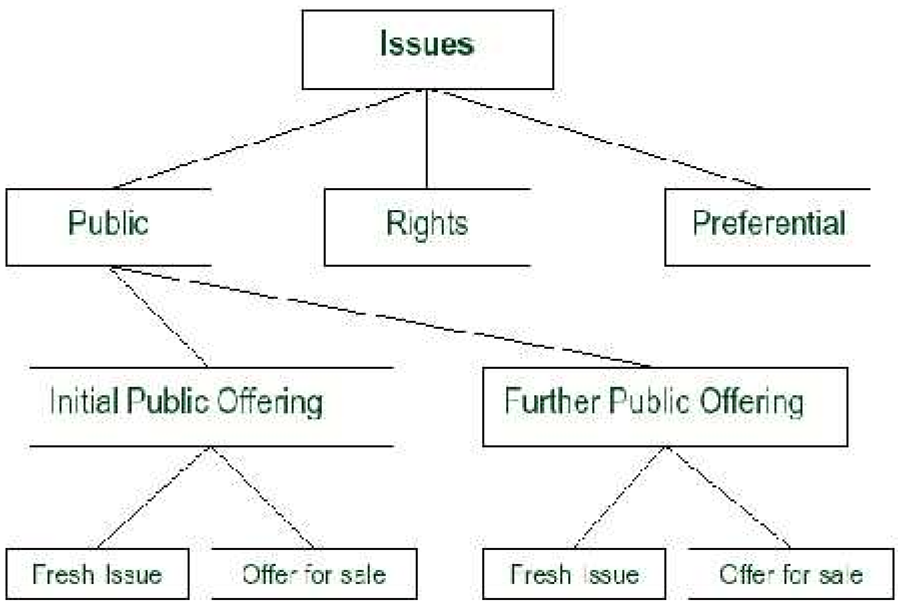
## 1. INTRODUCTION

Post 1992, the Indian equity market has undergone series of reforms through the initiatives of Securities and Exchange Board of India (SEBI), the statutory regulating body of securities market in India which include the introduction of the initiatives to set-up some important institutional mechanisms for both primary as well as secondary market segments particularly after 1998 in order to bring up the Indian securities market comparable to best of the world's any securities market in terms of safety and security of investment and transparency in transactions.

## 2. ISSEUE OF SHARES

Primarily, issues can be classified as a Public, Rights or preferential Issues (also known as private placements). While public and rights issues involve a detailed procedure, private placements or preferential issues are relatively simpler. The classification of issues is illustrated below:




## 3. OVERVIEW OF INITIAL PUBLIC OFFERING

The primary market came into its own in the eighties when a large number of companies came out with public issues. An entire industry of merchant bankers, brokers, agents and publicity managers were built around the primary issues market. The interest in new issues rose so high that investors were willing to pay for application forms. The trend continued in the early nineties as many large projects were launched after the economy was liberalized. Many of these companies came out with public issues and the retail participation increased dramatically. But many of the companies which raised money during this period just disappeared without a trace.

The IPO market continues to buzz in the recent years as well. Taking advantage of the strength in the secondary market, many high profile companies are lining up to raise money from the market. With a number of primary issues coming out, many who have never invested in stocks before are considering applying for some of these issues. Many have had bad experiences investing in new issues during the nineties. But the incredible returns made by investors in some of the recent issues keep their interest alive.

And thus from 1998 onwards Indian IPO market has witnessed changes that tend to focus on better realization to the issuers of stocks and better stocks for the investing public. This study is undertaken to analyze such IPOs in terms of underpricing or over pricing in Indian market over different time frames in the study period.

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**4. NEED FOR THE STUDY**

The performance of the initial public offerings in Indian stock market has been the research interest of many academicians and practitioners. But almost in all such studies focus, the focus has been only on underpricing of the stocks. All such studies agree that IPOs tend to be profitable only during short term period since IPO's are underpriced. This study is felt needed to analyze such IPOs in terms of underpricing or over pricing in Indian market over different time frames in the study period in order to shape the exit route for the investors.

**5. REVIEW OF LITERATURE**

The researcher has reviewed the research articles on the performance of IPOs in Indian stock market. The vivid account of such review has been presented here.

**Tim Laughran and Jay R Ritter (2001)** found that the average first day returns went to 65 per cent during 1999-2000 which were internet bubble years. They stated that the causes for the IPO under pricing depended on the environment.

**Aggarwal et al. (2002)** studied the relation between insider holding and their strategies used in IPO, being specifically focused on under pricing and its impact. It concludes that the lockup period ensures the presence of insider's ownership remains intact. However the liquidation process happens immediately after the lock up period.

The objective of issuers and investment bankers on t he ownership structure in the post market impacts the under pricing phenomena. Investment bank overprices the issue in order to decrement the number of owners or to have the ownership concentrated with few investors. However in order to have scattered ownership IPO offer needs higher participation by various segments of investors.

**As Su (2004)** studied 283 IPOs in China between January 1994 and December 1997 and found maximum underpricing of 692.60%, average underpricing of 129.36% and maximum overpricing of 36.64%.Thus IPOs" pricing is highly deviated from the true value. Further he concluded that firms with higher pre-IPO leverage are more underpriced .Moreover timing of offering also found to be important in China, if issue comes when the market fluctuations are high and market return are low surrounding an IPO then underpricing is higher. Thus underpricing differs with firms capital structure and market conditions during an IPO.

**Rosen, Smart and Zutter (2005)** conducted a sector-specific study wherein they investigated 240 US banks which completed their IPOs between 1981 and 2002. The advantage of doing a study on banking sector was the easy accessibility of required data, even of the private banks. Unlike the other sectors, both public as well as private banks are required to disclose their annual financial data to the regulators. Authors found that: the riskier banks were more likely to go public; the chance of getting acquired increased the probability of going public; the chance of becoming an acquirer also increased the probability of going public, and the banks went public to take the advantage of prevailing market condition.

**Murray Calson et al (2006)** found that equity issues were associated with expectations of the firm. The primary results of the study used real option principles to relate SEOs to an endogenous decrease in expected returns.

**Maria Rosa Borges (2007)** analyzed the underpricing of Portugal IPOs. They found that prior to 1987, the underpricing of Portugal IPOs was very high. The study found lower underpricing of IPOs during 1988 to 2004. The study did not find any evidence to long-run underperformance of IPO firms.

**Vaidayanathan (2007)** studies the price performance of IPOs in the NSE. The study suggests that the demand generated for an issue during book building and the listing delay positively impact the first day underpricing whereas the effect of money spent on the marketing of the IPO is insignificant. The study considers the data from March 2004 to Oct 2006.

**Kumar (2007)** has analyzed the long run as well as short run price performance with respect to the book building process in India and has verified the presence of underpricing phenomenon in Indian IPOs up to the time span of twenty four months from the date of listing

**Janakiramanan (2007)** has examined the evidence of the long run underperformance in the Indian market, by using CAPM and three factor models as benchmarks.

**Singh and Kumar (2008)** have analyzed short and long run underpricing of IPOs in the Indian Capital markets by looking at different factors affecting them. The study proposed a model of underpricing taking oversubscription.

**Kohli (2009)** studied 499 IPOs from April 1994 to March 2006 and found that stock markets in India suffered from the excessive optimism and poor valuation because he found that high prices of new issues are not related with their future profitability and growth in the sample.

**Asquith, Jones and Kieschnick (2010)** studied the role of politics in IPO pricing by taking a sample from 59 countries of 630 share issues. They found that the government favor domestic investors in share allocation, put a restriction on private firms, hires national investment banker as main underwriter, and adopts fixed pricing mechanism as against book building or auctions in order to give benefit to some interested parties.

**Tian (2010)** studied the IPOs issued in Chinese market from 1991 to 2000. The IPOs in China were found to be regulated by the government to a large extent with a cap on the price and also the quantity of shares to be offered to the public. This strict restriction on number and issue price of share had led to a very high average underpricing (267%) as the demand for shares generally tend to be high after the listing of shares.

**Gade Surendar and Dr. S. Kamaleshwar Rao (2011)** state that companies raise capital in the primary market by way of an initial public offer, rights issue or private placement. An Initial Public Offering (IPO) is one through which an unlisted company makes either a fresh issue of securities or an offer for sale of its existing securities or both for the first time to the public. This paves way for listing and trading of the issuer's securities. IPOs deepen the market, diversify investor's portfolios, reduce volatility in stock prices, bring domestic investors' money into the market and attract Foreign Institutional Investor funds too.

**Pandey** (**2012)** analyzed 84 fixed priced and book build Indian IPOs from 1999 to 2002 for a period of 500 trading days. It was found that fixed price IPOs performed the worst and all types of IPOs, on an average underperformed till about two years subsequent to listing.

**Singh and Mittal (2012)** analyzed the long-run performance of 500 Indian IPOs offered during 1992 to 1996 up to three years. The Indian IPOs earned excess returns up to six months from the listing date and after that the returns declined sharply, though remained positive at the end of first year. However, the investors who held their investments for a period of 2-3 year experienced negative returns.

**Tian and Megginson** (**2012)** studied the China's primary market by taking a sample of 1397 IPOs issued from 1991 to 2004 and found that IPOs in Chinese market were highly underpriced and they attributed this to strict regulation in China. The government puts a restriction on IPO quota and on IPO pricing [14]. They found that this strict regulation and lack of proper information about the firm leads to high degree of under pricing.

**Engelen and Essen (2012)** have studied the relationship around the world between the underpricing of IPOs and the prevalent legal framework in that country. Their findings show a negative relationship between the legal framework of the country and the IPO underpricing. They concluded that countries with robust investor protection give an advantage, in terms of cost to the public, to the companies in comparison to the countries where investor protection is weak.

## 6. STATEMENT OF THE PROBLEM

Since the primary market is dominated by the new issue market, the investors always come across IPOs every now and then. Understanding the performance of IPOs in raising long term equity funds is very much problem for the retail investors who intends to participate in the IPO market. So the problem sated for the study is how to understand and analyze the performance of the recent IPOs in the Indian market. This study mainly focuses on performance of new issue market in India as IPOs are important to raise long term equity funds for companies understanding their relative performance versus the secondary market is useful.

## 7. OBJECTIVES OF THE STUDY

- To study the performance of IPOs in terms of over pricing, underpricing and fairly pricing.
- To analyze the return on the listing day, next day, one week, one month, three months and six months from the issue price perspective.
- To suggest suitable exit route for the investors of IPOs.

**8. METHODOLOGY**

To analyze the performance of the IPOs, all the IPOs made during the year 2012-2013 have been considered. The researcher has collected data from the National Stock Exchange (NSE). Returns of the IPOs were calculated from the point of listing day, next day, one week, one month, three months and six months. Returns were calculated by comparing the issue price with the price prevailed on the selected days. The formula used to find out the return of the stock is-

Return = (P1 – P0) * 100/ P0, where, P1 = closing price on the listing day and other days in consideration and P0 = the offer price of the IPO

**9. LIMITATIONS OF THE STUDY**

- The study is limited to only performance of IPOs in the stock market for one year period (2012-2013).
- The study depends only on the IPOs made in National Stock Exchange (NSE) Mumbai during the study period.
- The study is only limited to 11 performing companies of the study period.

**10. ANALYSIS AND DISCUSSION**

In order to achieve the first and foremost objective of the study, the performance of the IPOs during the study period has been analyzed in terms of returns of IPOs on listing day, next day, one week, one month, three months and six months during the study period of 2012-2013. Table 1 exhibits the details of the IPOs made during the study period through NSE.

**Table- 1,IPOS Issued During the 1st April 2012 To 31st March- 2013**

| Sl. No. | Name of the Companies | Issue Open | Issue Close | Issue Price | Listing Price |
|---|---|---|---|---|---|
| 1 | National Building Construction Corporation Ltd | 22-Mar-12 | 27-Mar-12 | 106 | 96.95 |
| 2 | M T Educare Ltd | 27-Mar-12 | 29-Mar-12 | 80 | 90.35 |
| 3 | Tribhovandas Bhimji Zaveri Ltd | 24-Apr-12 | 26-Apr-12 | 120 | 111 |
| 4 | Speciality Restaurants Ltd | 16-May-12 | 18-May-12 | 150 | 159.6 |
| 5 | VKS Projects Ltd | 29-Jun-12 | 04-Jul-12 | 55 | 55 |
| 6 | Tara jewels ltd | 21-Nov-12 | 23-Nov-12 | 227 | 229.9 |
| 7 | Credit Analysis & Research Ltd | 07-Dec-12 | 11-Dec-12 | 750 | 922.55 |
| 8 | P C Jeweller Ltd | 10-Dec-12 | 12-Dec-12 | 135 | 149.2 |
| 9 | Bharati Infratel Ltd | 11-Dec-12 | 14-Dec-12 | 220 | 191.65 |
| 10 | V-mart Retail Ltd | 01-Feb-13 | 05-Feb-13 | 210 | 203.3 |
| 11 | Repco Home Finance Ltd | 13-Mar-13 | 15-Mar-13 | 172 | 161.8 |

Source**:** National Stock Exchange of India Ltd.

It is evident from Table 1 that there were 11 companies issued IPOs during the study period 2012 – 2013) in National Stock Exchange (NSE). In order to analyze the issue price of these companies, the researcher has tabulated the issue prices in Table 2.

**Table- 2, list of companies on the basis of issue price of IPOs**

| Issue price (in Rs) | 001 -200 | 201-400 | 401-600 | 601-800 | 801-1000 |
|---|---|---|---|---|---|
| No. of Companies | 7 | 3 | 0 | 1 | 0 |
| Percentage | 64% | 27% | 0% | 9% | 0% |

Source: Compiled and Calculated

From Table 2, it is understood that among the eleven companies issued IPOs, the number of companies is more (64%) in the issue price range of less than Rs. 200, three companies issued IPO between Rs. 201 to Rs. 400 and no companies have been found having issue price more than Rs 800 during the study period.

**10.1 performances of IPOs in terms of pricing**

The researcher has analyzed the performance of IPOs on Listing day, the next day, one week, one month, three months and six months. Performance of the IPOs on the listing day by comparing the issue price and listing price to find out whether the IPOs are overpriced, underpriced or fairly priced is presented in Table 3.

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**Table- 3 Performance of IPOs on listing day**

| Name of Companies | Issue Price Rs) | Listing Price (Rs) | Performance |
|---|---|---|---|
| National Building Construction Corporation Ltd | 106 | 96.95 | Over priced |
| M T Educare Ltd | 80 | 90.35 | Under priced |
| Tribhovandas Bhimji Zaveri Ltd | 120 | 111 | Over priced |
| Speciality Restaurants Ltd | 150 | 159.6 | Under priced |
| VKS Projects Ltd | 55 | 55 | Fairly priced |
| Tara Jewels Ltd | 227 | 229.9 | Under priced |
| Credit Analysis & Research Ltd | 750 | 922.55 | Under priced |
| P C Jeweller Ltd | 135 | 149.2 | Under priced |
| Bharati Infratel Ltd | 220 | 191.65 | Over priced |
| V-mart Retail Ltd | 210 | 203.3 | Over priced |
| Repco Home Finance Ltd | 172 | 161.8 | Over priced |

Source: Compiled and Calculated

It is evident from Table 4, in the year 2012 to 2013 among eleven IPOs issued, five companies were overpriced, five companies were underpriced and only one company has fairly priced. It is inferred here that the IPOs are not at all fairly priced during the study period which is an evident for the existence of defects of pricing mechanism in the new issue market of India.

**10.2 Return Analysis**

To fulfill the second objective of the study, the researcher has analyzed the returns of IPOs on Listing day, the next day, one week, one month, three months and six months. The results of such analysis are exhibited in Table 4, 5 and 6.

**Table -4, Return Analysis of Listing Day and Next Day**

| Returns (%) | Listing Day | | Next Day | |
|---|---|---|---|---|
| | No of Companies | % of Companies | No of Companies | % of Companies |
| -100 to -80 | 0 | 0 | 0 | 0 |
| -80 to -60 | 0 | 0 | 0 | 0 |
| -60 to -40 | 0 | 0 | 0 | 0 |
| -40 to -20 | 0 | 0 | 0 | 0 |
| -20 to 0 | 6 | 54.55 | 5 | 45.45 |
| 1 to 20 | 4 | 36.36 | 5 | 45.45 |
| 20 to 40 | 1 | 9.09 | 1 | 9.09 |
| 40 to 60 | 0 | 0 | 0 | 0 |
| 60 to 80 | 0 | 0 | 0 | 0 |
| 80 to 100 | 0 | 0 | 0 | 0 |
| 100 & above | 0 | 0 | 0 | 0 |
| Total | 11 | 100 | 11 | 100 |

Source: Compiled and Calculated

**Listing Day**

It is evident from Table 4 that lot of companies (54.55%) offered returns in the range from 0 to -20% to the subscribers of IPOs on the listing day when 36.36% of companies could offer a return in the range of 1 to 20% and return of 20 to 40% range were offered by only 9.09% of companies which issued IPOs in the study period and other return ranges have not given by any companies.

**Next Day**

As for as next day return is concerned, it is found that 45.45% of companies provided returns ranging from 0 to -20% another 45.45% of companies provided returns in the range of 1 to 20% and return range from 20 to 40 were provided by 9.09% of companies and other ranges of returns were not found in any of the companies issued IPOs during the study period.

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**Table -5, Return Analysis of One Week and One Month**

| Returns (% ) | One Week | | One Month | |
|---|---|---|---|---|
| | No. of Companies | % of Companies | No. of Companies | % of Companies |
| -100 to -80 | 0 | 0 | 0 | 0 |
| -80 to -60 | 0 | 0 | 0 | 0 |
| -60 to -40 | 0 | 0 | 0 | 0 |
| -40 to -20 | 0 | 0 | 0 | 0 |
| -20 to 0 | 5 | 45.45 | 6 | 54.55 |
| 1 to 20 | 3 | 27.27 | 3 | 27.27 |
| 20 to 40 | 3 | 27.27 | 2 | 18.18 |
| 40 to 60 | 0 | 0 | 0 | 0 |
| 60 to 80 | 0 | 0 | 0 | 0 |
| 80 to 100 | 0 | 0 | 0 | 0 |
| 100 & above | 0 | 0 | 0 | 0 |
| Total | 11 | 100 | 11 | 100 |

Source: Compiled and Calculated

**One Week**

Analysis of one week return of IPOs considered for the study reveals that 45.45% of companies were able to offer 0 to -20% returns 1 to 20% was offered by 27.27 and another 27.27% of companies gave 20-40% returns to the shareholders and other ranges of return classified by the researcher were not found in any of the companies.

**One Month**

Table 5 clearly states that 54.55% of companies provide return of 0 to -20% range and 1 to 20% returns were possible in 27.27% of companies and 20 to 40 % range was available in 18.18% of companies and other ranges of return were not found in any companies Issued IPOs during the study period 2012- 2013.

**Table -6, Return Analysis of Three Months and Six Months**

| Returns (% ) | Three Months | | Six Months | |
|---|---|---|---|---|
| | No. of Companies | % of Companies | No. of Companies | % of Companies |
| -100 to -80 | 0 | 0 | 0 | 0 |
| -80 to -60 | 0 | 0 | 0 | 0 |
| -60 to -40 | 0 | 0 | 1 | 9.09 |
| -40 to -20 | 4 | 36.36 | 2 | 18.18 |
| -20 to 0 | 2 | 18.18 | 2 | 18.18 |
| 1 to 20 | 3 | 27.27 | 0 | 0 |
| 20 to 40 | 0 | 0 | 3 | 27.27 |
| 40 to 60 | 1 | 9.09 | 1 | 9.09 |
| 60 to 80 | 0 | 0 | 1 | 9.09 |
| 80 to 100 | 1 | 9.09 | 0 | 0 |
| 100 & above | 0 | 0 | 1 | 9.09 |
| Total | 11 | 100 | 11 | 100 |

Source: Compiled and Calculated

**Three Month**

It is clearly understood from Table 6 that -40 to -20% ranges of returns have been offered by 36.36% of companies where as 1 to 20% of returns have been provided by 27.27% of companies and -20 to 0% of returns were possible in 18.18% of companies. It is also observed that 40-60% returns range was available in 9.09% of companies and another 9.09% of companies provided 80 to 100% returns to the shareholders.

**Six Month**

In the analysis of six month returns of IPOs, it is known that 20 to 40% returns were offered by 27.27% of companies and -40 to -20 and -20 to 0 % of returns ranges were offered by two set of 18.18% of companies and -60 to -40, 40 to 60, 60 to 80 and 100% and above ranges of returns have been provided by four set of 9.09% of companies. It is the evident here that the investors can get more return from IPOs after six months.

## 11. FINDINGS AND SUGGESTIONS

The findings based on the study are summarized as follows.

1. There were 11 companies issued IPOs during the study period 2012 – 2013) in National Stock Exchange (NSE). Majority of the companies' (64%) issue price is less than Rs 200 and no companies issued IPOs for more than Rs 800.
2. Out of 11 companies, only one company is fairly priced. So it is found that the IPOs are not at all fairly priced during the study period which is an evident for the existence of defects of pricing mechanism in the new issue market of India.
3. On the basis of return analysis of listing day, 54.55% of companies resulted in return range of 0 to -20% and 1 to 20% return range was offered by 36.36% of companies and return of 20 to 40 range was offered by only 9.09% of companies
4. As for as next day return is concerned, it is found that 45.45% of companies provided returns ranging from 0 to -20% another 45.45% of companies provided returns in the range of 1 to 20% and return range from 20 to 40 were provided by 9.09% of companies and other ranges of returns were not found in any of the companies issued IPOs during the study period.
5. It is found that 45.45% of companies were able to offer 0 to 20% returns 1 to 20% was offered by 27.27% of companies and another 27.27% of companies gave 20 to 40% returns to the shareholders and other ranges of return classified by the researcher were not found in any of the companies.
6. The research also finds that 54.55% of companies provide return of 0 to -20% range and 1 to 20% returns were possible in 27.27% of companies and 20 to 40 % range was available in 18.18% of companies and other ranges of return were not found in any companies Issued IPOs during the study period 2012- 2013.
7. It is clearly found that -40 to -20% ranges of returns have been offered by 36.36% of companies where as 1 to 20% of returns have been provided by 27.27% of companies and -20 to 0% of returns were possible in 18.18% of companies. It is also observed that 40-60% returns range was available in 9.09% of companies and another 9.09% of companies provided 80 to 100% returns to the shareholders.
8. In the analysis of six month returns of IPOs, it is found that 20 to 40% returns were offered by 27.27% of companies and -40 to -20 and -20 to 0 % of returns ranges were offered by two set of 18.18% of companies and -60 to -40, 40 to 60, 60 to 80 and 100% and above ranges of returns have been provided by four set of 9.09% of companies.
9. It is the evident here that the investors can get more return from IPOs at the later stages.
10. The investors of IPOs are suggested to exit the market based on the returns of the IPOs on the day of exit.

## 12. CONCLUSION

Subscribers to IPOs are able to generate better return on the listing day and on the next day, investors must also aware of the fact that all companies are not generating positive return on the listing day and on the next day. Since in the long run returns are attractive, investors should exit from the IPOs at the earliest possible time further the study concludes that the investors of IPOs should exit the market based on the returns of the IPOs on the day of exit.

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