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Initial Public Offering (IPO's) Under-pricing or Overpricing: An Empirical study of Selected IPO's in NSE and BSE

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ABSTRACT

Study has made an attempt to analyse the Indian IPO's in order to observe the phenomenon of underpricing as well as overpricing in the Indian context between the duration 2012 to 2015of which 85 IPO's are been considered. Of which it includes companies listed in NSE as well as in the BSE. An observation is been made in the study that is underpricing exists in the years 2014 and 2015; the phenomenon of overpricing has been existed in the year 2012 and 2013 in the context of India. But for the year 2014 and 2015 we can observe the phenomenon of underpricing, as it is also been suggested by the Ritter for the risk which is undertaken by the uninformed investors for making a venture in the IPO. So finally it can be said that underpricing as well as overpricing exists in the Indian IPO market for the period which is been mentioned in the study.

Keywords: Initial Public Offering, Securities and Exchange Board of India, Stock Exchange, Book Building.

INTRODUCTION:

For any business for that matter investing in Public Offering can open a number finance gates. The basic need for an IPO usually arises when a company requires money to grow and expand, which is done by issuing or borrowing shares and the company must invite public investors to buy its shares if the company decides to issue shares for general public. This referred to as the company's initial public invitation in the stock market and is hence, called as initial public offering. Investors get the ownership of the company equals to the value of your shares, when investors buy these shares. After which these shares will be listed on the stock exchange or the stock market.

How Does IPO Work in India?

The complete process of IPO is controlled and managed by the Securities and Exchange Board of India (SEBI). The company which is expecting to issue the IPO shares, first it registers itself with SEBI. SEBI being the governing body, thoroughly studies and analyse the documents which is been submitted by the concerned company and approves it only after being convinced by SEBI. Hence the company prepares its prospectus mentioning that the SEBI approval is pending, by the time the company gets approval from SEBI.

The company fixes the price of the share and the number of shares it plans to issue, once it gets the approval. Generally there are two types of issue of IPO's: One is fixed price and the other is the book building. So in the former, the company in advance decides the price of the share whereas in the latter, the company offers a range of prices. An investor then needs to bid for the shares within this particular range only.

So the company makes the shares available for the general public only after deciding on the type of issue it wishes to go ahead with. Then by showcasing their interest in buying the shares, the investors submit the applications. So the company goes ahead with the allotment of shares, only after the company gets the subscriptions from the public. And the final step in this procedure is to make listing of shares in the stock market. Shares get listed in the secondary market, once the shares are issued to the investors in the primary market. And after listing trades in these shares shall become on a daily business in the stock market.

REVIEW OF LITERATURE:

Michael B. Heeley, Sharon F. Matusik and Neelam Jain (2007) have made the observation concerning the under-pricing and have reported that under-pricing scholars have well established the prominence of general quality indicators in minimizing the under-pricing and information asymmetries. Study concentrates to identify the role of innovation in under-pricing using the theory of information asymmetries. A model have been tested, the patents will reduce the asymmetries of information in those industries where the relation between the inventive returns and the patents is transparent, thus by dropping the under-pricing of IPO. On the other hand study observes that increased information asymmetries reflected by the patents and also under-pricing of IPO in those industries where the relation is not transparent. By examining a sample of 1,413 IPO's, study finds a strong support for the hypotheses framed. Study have made an important contribution theoretically that IPO market contextualizes the firms information.

Saurabh Ghosh (2005) has identified the various factors explaining the underpricing of IPO's in an emerging economy like, India, by considering a sample of around 1,842 companies which have listed in the BSE between the periods 1993 to 2001. Study has found that the uncertainty played a role in perverse underpricing in the primary market of India. The IPO issues which went with the bulk issue size and also that went for seasoned offering had lesser underpricing. Contrary to the evidence which is obtained internationally, underpricing was less during the high volume period means the hot period compared to the slump period means cold period in the Indian IPO market. The new issues belonging to the business group was underprized more compared to their stand-alone counterparts during the hot period. And the small issues belonging to the private standalone firms had less underpricing during the hot period and they did not come to the market subsequently to raise the capital. Large issues belonging to business group's under-priced more and hence subsequently raised funds required from the market. Results obtained from the study support the predictions of signalling theory for the IPO's which is listed in the Indian stock markets over the last decade.

David R. Williams, W. Jack Duncan and Peter M. Ginter (2010) have analyzed the relationship among secondary-market, Pre-market, and the primary-market characteristics. Signalling theories and the agency theories have been utilized in the study. Study examines the high-technology firms which are seeking for an IPO for the agency and market signals which is related to a sample chosen for the study. For the purpose of examining for IPO offer process in high-technology firms a model have been tested. The results of the study indicates the secondary market factors have not affected the offer price of the IPO but the offer price is affected by certain primary market and Pre-market factors which is received by the entrepreneurs and the investors.

Paul A. Gompers and Josh Lerner (2003) by considering that after the formation of NASDAQ stock exchange, study highlights that the financial economist has intensely debated about the performance of IPO's by considering the data. So for a period of five years duration after the listing study examines the performance of 3,661 IPO's of U.S between the duration of 1935 to 1972. The sample considered displays some underperformance when the event-time buy-and-hold abnormal returns are utilized. And the underperformance disappeared when the cumulative abnormal returns are utilized. So over the entire period, IPO returns are as much as the market which is according to the calendar-time analysis. By considering the intercepts in the regressions of CAPM and Fama – French which are insignificantly different from zero, and hence suggesting that the performance obtained is not abnormal.

OBJECTIVES OF THE STUDY:

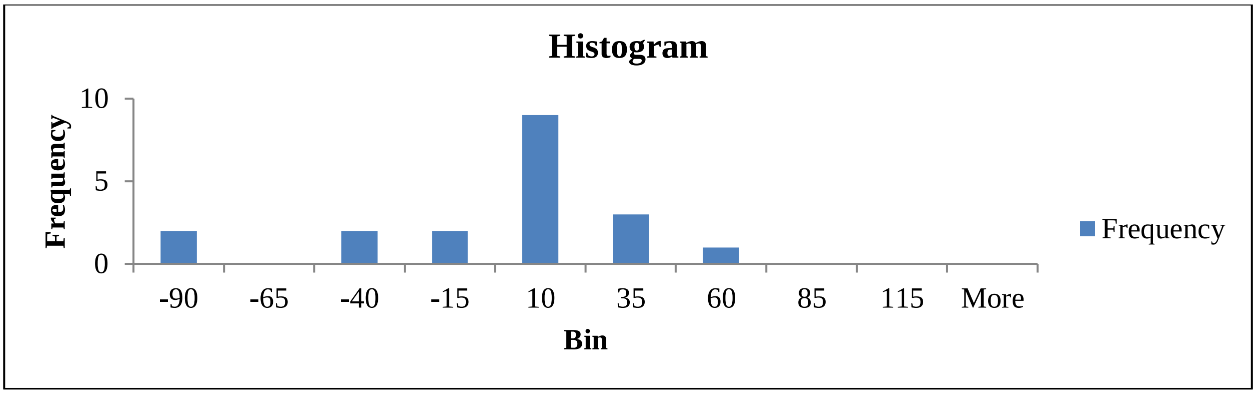
- To examine the different IPO issues in the Indian equity Market.
- To empirically test the underpricing of IPOs.

DATA COLLECTION AND RESEARCH METHODOLOGY:

- The research design for the current study is descriptive and exploratory in nature for which the quantitative approach is been used. Study is based on the secondary sources of data which is collected from the secondary sources of data, publications and from different websites.

ANALYSIS AND INTERPRETATION:

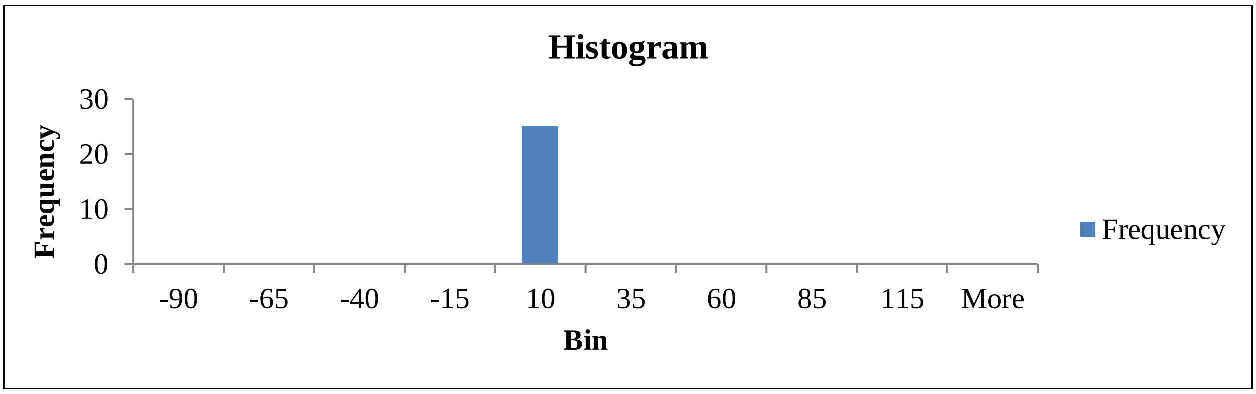
Graph 1: shows histogram for the IPO issues of the year 2012



Interpretation:

- The value of skewness obtained from the data, for the year 2012 histogram is -1.06.
- The value obtained is highly negative which represents the presence of a low degree of negative skewness.
- And also represents that there is an overpricing as the returns obtained for the investors is in terms of negative perspective.
- Finally it represents the overpricing of the IPO issue as investors are obtaining negative returns.

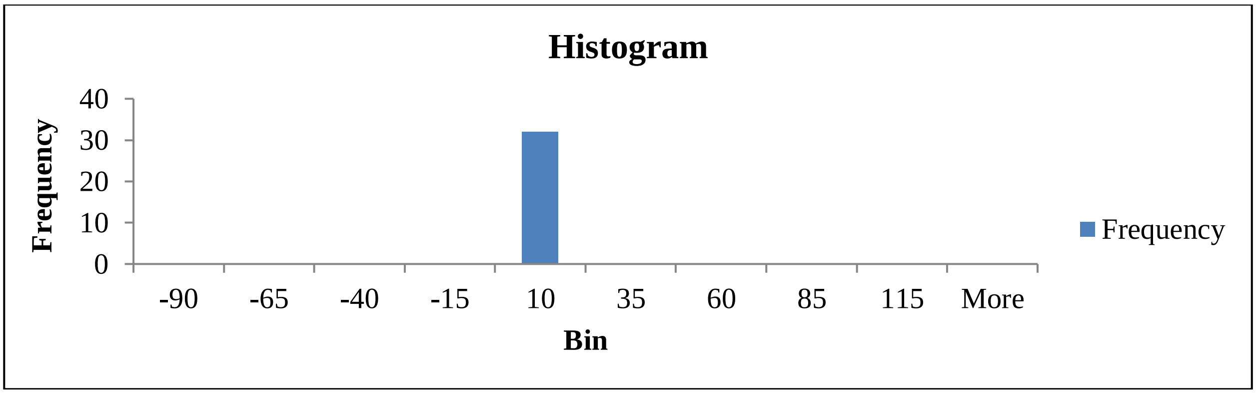
Graph 2: shows histogram for the IPO issues of the year 2013



Interpretation:

- The value of skewness obtained from the data, for the year 2013 histogram is -0.65
- The value obtained is negative which represents the presence of a low degree of negative skewness.
- And also represents that there is an overpricing as the returns obtained for the investors is negative.
- Finally it represents the overpricing of the IPO issue as investors are obtaining negative returns.

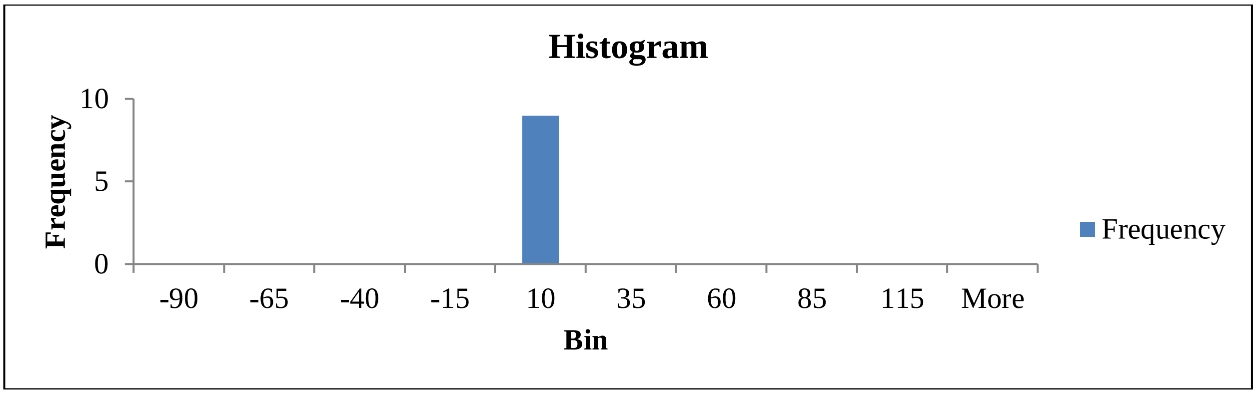
Graph 3: shows histogram for the IPO issues of year 2014



Interpretation:

- The value of skewness obtained for the data for the year 2014 histogram is 1.13 with mode value 0.435.
- The value obtained is highly negative which represents the presence of a low degree of negative skewness.
- And also represents that there is an overpricing as the returns obtained for the investors is negative.
- Finally it represents the underpricing of the IPO issue as investors are obtaining positive returns.

Graph 4: shows histogram for the IPO issues of the year 2015



Interpretation:

- The value of skewness obtained for the data for the year 2015 histogram is 0.20 with mode value 0.01.
- The value obtained is highly negative which represents the presence of a low degree of negative skewness.
- And also represents that there is an overpricing as the returns obtained for the investors is negative.
- Finally it represents the underpricing of the IPO issue as investors are obtaining positive returns.

CONCLUSION:

So finally it can be concluded that from the observation of data for the various years from 2012 to 2015 for around 85 IPO's undertaken for the analysis. Study reveals that in the Indian IPO market, the phenomenon of underpricing as well as overpricing of IPO's exists as per the observation made for the years 2012 and 2015, but overpricing have occurred for the years 2012 and 2013 where as vice versa for 2014 and 2015. As it has been observed from the extant literatures, underpricing is present worldwide and it is not an exception in case of Indian scenario also. So it can be concluded that, the presence of underpricing as well as overpricing is for various reasons in the IPO market, underpricing is supported by many researchers which can be observed by extant literatures. Very few researchers have supported the fact of overpricing, not only in the Indian context but also world-wide.

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