

# Initial Public Offerings (IPOs) : A Boon Or A Bane?

\* *Jigna Trivedi*

\*\* *Bindiya Soni*

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## ABSTRACT

IPOs are the most favoured tool adopted by corporates to raise money from the general public. An IPO is the first sale of stock by formerly a private company. The revolutionary reform which took place in the Indian stock market was fair price discovery of IPOs through the book building mechanism. The present paper tries to comprehend the concept of the book built issue, its importance and advantages over the Fixed Price Regime. The paper also tries to bring forth the short term return available to the subscribers of IPOs. The concept of listing gains and intra day gains are studied with respect to short term investors. IPOs issued in the duration of five years, starting from 2006 to 2010 were taken as a base for computing the return and for commenting on the performance of IPOs. Overall, the reasons for high and low performance of IPOs are discussed in the paper. As a part of the study of pre - subscription of IPOs, the paper highlights the importance of IPO grading to be used as a tool to learn about the fundamentals of the company. The paper highlights the quantum of listing gains derived by the investors on listing of the IPOs.

JEL Classification: G12, G14

Keywords: Initial Public Offerings (IPOs) , Book Building Mechanism, Fixed Price Regime, IPO Grading, Retail Investors

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*Never invest in any idea you can't illustrate with a crayon.*

*- Peter Lynch*

## INTRODUCTION

The Indian Capital Market deals in long term securities of the government and the corporates, which helps the two entities to raise money from the public (Deodhar & Abhyankar, 2007). A capital market constitutes an operation in the new issues and stock market. New issues made by companies form the primary market and trading in the existing securities confer to the secondary market (Avadhani, 1997). Investment is a function of savings. The market for raising funds for capital formation and investment is referred to as capital market, which is vital for economic development of the country (Avadhani, 1997). Savings are made by household and foreign sectors that mobilize the same to the capital market to meet the deficits of government and business sectors, with the expectation of earning revenue income and capital appreciation. Primary markets are treated as an efficient vehicle for mobilization of resources. In the architecture of the Indian Primary market, many reforms have taken place from time to time. The primary market has witnessed key amendments like the establishment of the Securities and Exchange Board of India (SEBI) , end of weekly settlement, end of 'badla' trading, shift to rolling settlement, enlargement of derivatives trading, electronic trading, and de-materialization of securities, etc. One of the biggest improvements in the primary market consists of issuing shares through the book building process, which endeavors at efficient price discovery. The present study is an attempt to comprehend the concept of the book building issue and analyze the returns of 100 per cent book built IPOs (issued in the duration of five years i.e. 2006 to 2010) in the short run.

## LITERATURE REVIEW, RESEARCH GAP AND NEED FOR RESEARCH

Research on the Indian Book Building Process explains the spirit behind the introduction of book building, which is, to discover the right price for a public issue, which in turn would eliminate unreasonable issue pricing by greedy promoters. Researchers feel that the mechanism has not reached the expected heights for the investors in the Indian Capital market (Gangadhar & Reddy, 2008). Performance of the IPOs in the long run and short run is a well researched topic in the capital markets. The major areas studied are the reasons of under-pricing of IPOs. Global literary works

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\* *Assistant Professor*, Shri Jairambhai Patel Institute of Business Management and Computer Applications, Near Infocity, Opposite Fun World, Koba-Gandhinagar Highway, Gandhinagar-382007, Gujarat. E-mail: jigna2804@gmail.com

\*\* *Assistant Professor*, Anand Institute of Management, Shri Ram Krishna Seva Mandal Campus, Opp. Town Hall, Anand-388 001, Gujarat. E-mail: bindi\_pathak@yahoo.com

also include studies on under-pricing of IPOs in countries like US, Canada, Germany, Singapore, China and the Asian markets. The research concludes that IPOs are under-priced for the investors to avail the listing gains (Kumar, 2007). As documented by Kumar (2007), the Indian study involves cross sectional performance of IPOs over a range of 5 years. The author briefed that various researchers have made the study of IPOs during the phase of 1991 to 1995. IPOs offered on BSE during 1992 to 1995 were studied by the researchers. The study highlighted the under-pricing of the IPOs to be as high as 105.6% to as low as 36.6% in the short run, versus global under-pricing to the extent of 11%. The long run overpricing in the Indian market was found to be 40.8%. The study of the IPOs issued and listed on the NSE during 1999 to 2006 was made by Kumar (2007). The paper concluded with the analysis of short run and long run performance of the IPOs. Madhusoodanan and Thiripalraju (1997) advocated that book building is a better proposition to avoid mis-pricing, to ensure a fair deal for investors and issuers. The researchers concluded that under-pricing benefits the investors and suggested that the shares should be issued at the true value, rather than at par or at premium value, because this would act as a feasible solution for making the companies work hard for the issue of bonus shares. A study by Chaturvedi, Pandey and Ghosh (2006) explained that despite using the book built issue, the IPOs are under-priced. Over-subscription leads to larger first-day gains for the IPO. The signals of oversubscription are market index, type and nature of business, foreign collaboration and promoter's track record. The work of Allen and Faulhaber (1989) as referred by Kumar (2007) projected that a good IPO issuer, on the account of under-pricing, will come up in the future with a seasoned offering to raise money at improved terms from the market. Hursti and Maula (2007) emphasized the determinants which influence the decision of ventures to become public in a foreign exchange instead of the domestic stock exchange. Daily, Certo, and Dalton (2005) underlined that prospectus information can be used as a signal for investment bankers at the time of determining the offer price and the offer spread. With respect to the IPOs listed on the BSE in the year 2007-08, Gupta (2011) represented in the study that during the boom period, the under pricing depended on the market conditions. Inefficient market conditions provided an opportunity to laggard investors to earn a profit by investing on the first day of the listing. Thus, market conditions affected the underpricing of the issues. In the study of 2008-09, Gupta (2011) highlighted that during the period of downturn, pessimism and slump, there was no underpricing. On the contrary, it showed overpricing. Empirically tested fact of underpricing leading to oversubscription was actually violated in the study of IPOs issued during 2007-08 i.e. the boom period. Thus, pricing of shares did not depict any relation with the market trend, which may be attributed to investors' lower faith in small cap companies (Gupta, 2011). Firms and investors justified IPO underpricing so that an issue could be made attractive. Bansal and Desai's (2012) study showed that in the Indian market during 2007 to 2010, the listing day average volatility was 37.4%, which steeply dropped down to 8.7% on the sixth day (including the listing day). The peak of volatility was found on the listing day. The dwindling interest of the investors was clearly represented by a fall in the volume from the listing day onwards (Bansal & Desai, 2012). Bansal and Desai (2012) suggested three valuable measures to minimize volatility viz., restricting intraday movements of listed IPOs in a 25% range ; promoting anchor investors ; and using the auction method instead of the book-building method for setting a reliable issue price. Providing access to the derivatives market on the listing day could facilitate a better price discovery of the new issue. Madan's (2003) study expressed consensus on the literary fact that the initial excess returns on the IPOs in the Indian primary capital market are very high when compared to the international capital markets. The study further confirmed the findings that in the long run (five years after listing), there was a drastic fall in the IPOs' returns; it was found to be negative from the second year onwards. Sohail and Nasr (2007) explained the reasons of initial returns dependent on under pricing of the IPOs. Their findings revealed that there was no profit opportunity for intra day traders on the day of listing of the IPOs. The profit opportunity only prevailed for those investors who could bear the ambiguity of price in the primary market.

The literature review of IPOs is mainly divided into two themes viz., - the study of the book building process, and the study of the IPO performance. The study of IPO performance varies from time to time. None of the latest literary works which included the study of IPOs listed on the NSE between the periods 2006 to 2010 have been explored. An apparent need was found to address this gap, and to undertake the study of the latest issue of IPOs to evaluate their short-run performance. The past studies have not incorporated the novel concept and importance of IPO grading, which is also addressed in this study. The forthcoming work in the paper discusses the significance of IPOs; the importance of the book building issue, the short-run performance of IPOs (2006-2010), and the meaning of IPO grading.

## RESEARCH OBJECTIVES

- ❖ To understand the meaning and importance of IPOs from the perspective of corporates and subscribers.
- ❖ To comprehend the concept of the book building issue, its importance and advantages over the Fixed Price Regime.
- ❖ To identify the short term returns in terms of listing gains and intra day gains available to subscribers of IPOs with respect to the duration from 2006 to 2010.
- ❖ To explain the prerequisite importance of fundamental analysis before the subscription of an IPO.

## RESEARCH METHODOLOGY

The sample in this study includes the fresh equity issues offered through the book built route on the NSE. A sample of 243 companies (see Appendix 1) which came out with 100 percent book built IPO and got listed on National Stock Exchange (NSE) from the period commencing from 2006 to 2010 was taken as the primary dataset for the short run analysis. The companies offering follow on Issue, or IPOs which were offered in 2010 but got listed in 2011, or the IPOs which only got listed on the Bombay Stock Exchange (BSE) and not on the NSE, were excluded from the dataset. The list of 243 companies - their issue size, price range, grading and the offer price was downloaded from the website of NSE. The data regarding the closing date of the closure of the IPOs was downloaded from the IndiaIPO website. Approximately, 486 Bhav copies were downloaded from NSE's website - to obtain the opening and the closing prices on the day of the IPO listing and the day after the listing of the IPO. Nifty index values were retrieved from the Capitaline database. Closing Nifty index on the last day of the offer, Opening value of Nifty index on the day of listing and Closing value of Nifty index on the day of listing were also obtained. The price performance of IPOs was evaluated for the short run i.e. returns received on the day of the listing and on the day after the listing. Considering the study of Kumar (2007) as a base for present study, the returns realized over the period from the offering of the shares to the first trading day on NSE, called as offer- to- close return were computed. The work of Barry and Jennings (1993) (as referred to and applied by Kumar (2007) in his study) have been applied in this study too. The short run analysis was examined by offer-to-open returns for obtaining a reasonable idea of how much IPOs gained or lost on opening trades and as well as intra day return on the listing day, which is defined as open –to-close returns on the day of listing. Similar returns were analyzed for the next intraday (second day after the listing day). Simple returns, market adjusted returns and excess returns were computed to know the performance of the IPOs. Simple returns ( $R_{it}$ ), Market Adjusted Returns ( $R_{mt}$ ) and Excess Returns ( $ER_{it}$ ) were calculated with the following formulae :

$$R_{it} = \frac{(P_{it} - O_i)}{O_i} \times 100 \quad R_{mt} = \frac{(I_t - I_o)}{I_o} \times 100 \quad ER_{it} = R_{it} - R_{mt}$$

$P_{it}$  = represents the opening or closing price of stock 'i' at time 't' - i.e. at the time of listing.

$O_i$  = represents the offer price of the stock 'i'.

$I_t$  = represents Nifty index closing or opening value on the day of 't' i.e. on the day of listing.

$I_o$  = represents closing level of Nifty on the last day of the IPO offering.

Descriptive research design has been used for the study. Descriptive statistics like mean, 5% trim mean, median, SD were applied for computing the significance of returns on the listing day and the next day. Inferential statistics - like the cross sectional 't' statistic - was used to test the hypothesis on significance of the samples mean return. For gauging the concept of the book built issue, IPO grading, fixed price regime, and importance of IPOs, various secondary sources of offline data like newspaper, journals, books and online research papers and periodicals have been studied. The primary dataset was analyzed and interpreted with the help of SPSS 17 and Microsoft excel programmes.

## SIGNIFICANCE OF IPOs

IPOs are the first sale of stock by the company to the public. A company makes the transformation from being privately held to becoming publicly traded (Taulli, 2000). IPO is a process through which an unlisted company can be listed on the stock exchange by offering its securities to the public in the primary market. Companies issue IPOs for its expansion activities, for setting up new projects, to get its existing equity shares listed, etc. (National Stock Exchange of India, n.d.). IPOs are often offered by smaller, younger companies to seek capital for expansion of their businesses (Funding Post, n.d.). Capital is the blood for corporates. Companies have umpteen alternatives to raise capital like issue of ordinary shares ; issue of preference shares (with variants of cumulative, convertible, redeemable,

participating) ; debentures (with variants of registered, convertible, redeemable, partially convertible, perpetual rights) ; bonds (with variants of Discount, Deep Discount, Zero coupon, Zero coupon convertible, floating rate, capital indexed bonds) ; secured premium notes ; loyalty coupons ; warrants ; derivatives (with variants of forward, futures, swaps, call option, put option, currency options) ; domestic borrowings from banks and Financial Institutions (FIs); and external commercial borrowings (ECBs). Companies have three broad ways of floating a new issue, i.e. by issue of a prospectus to the public, by private placements, and through rights issue. The fundamental reason for companies going public are for gaining prestige, getting rich, cash infusion, increase in liquidity and leverage capacity, and stocks are used as currency to purchase other businesses. IPOs often result in huge expense escalation, stringent compliance requirement, and a loss of privacy (Taulli, 2000). Investors have diverse objectives for subscription of IPOs. Retail investors subscribe to IPOs for availing listing gains or trading gains, or intraday gains in the short run. Holding the allotted IPO stock for a long time indicates that the investor's intention is to derive benefit of long term gains and capital appreciation. IPOs are a favoured tool of investment of high as well as moderate risk takers.

## MEANING AND IMPORTANCE OF THE BOOK BUILT ISSUE

The Indian IPO market in the pre-reforms period was controlled by the Controller of Capital Issues (CCI). The firm would set the quantity of the issue to be raised, but CCI would decide at what price the shares would be issued. These prices were set at either ₹10 or ₹ 100. In 1992, the CCI was closed down. Today, firms issue shares at market determined prices, through a variety of market intermediaries and market mechanisms (Shah A., Thomas S. and Gorham M., 2009). IPOs can be made through the fixed price method, book building method, or a combination of both. Under the fixed price regime, companies have the freedom to issue shares at a price determined by themselves in consultation with the lead manager (Kumar, 2007). Book building is the process used by companies to aid price and demand discovery. It is a mechanism where during the period for which the book for the offer is open, the bids are collected from investors at various prices, which are within the price band specified by the issuer. The process is directed towards both the institutional as well as the retail investors. The issue price is determined after the bid closure based on the demand generated in the process (Bombay Stock Exchange of India, n.d.). The theoretical comparison between Fixed Price Issues and Book Building Issues is discussed in the Table 1.

<b>Table 1: Theoretical Comparison of Fixed Price Issue Versus The Book Building Issue</b>				
<b>Issue Type</b>	<b>Offer Price</b>	<b>Demand</b>	<b>Payment</b>	<b>Reservations</b>
Fixed Price Issues	Price at which the securities are offered and would be allotted is made known in advance to the investors.	Demand for the securities offered is known only after the closure of the issue.	100 % advance payment is required to be made by the investors at the time of application.	50 % of the shares offered are reserved for applications below ₹ 1 lakh and the balance for higher amount applications.
Book Building Issues	A 20 % price band is offered by the issuer within which investors are allowed to bid and the final price is determined by the issuer only after closure of the bidding.	Demand for the securities offered, and at various prices, is available on a real time basis on the BSE website during the bidding period.	10 % advance payment is required to be made by the QIBs along with the application, while other categories of investors have to pay 100 % advance along with the application.	50 % of the shares offered are reserved for QIBs, 35 % for small investors, and the balance for all other investors.
Source: Bombay Stock Exchange of India (n.d.), ( <a href="http://www.bseindia.com/bookbuilding/about.asp">http://www.bseindia.com/bookbuilding/about.asp</a> )				

Book building is a mechanism to gauge the issue price from the market with the help of the demand and supply forces. The process helps to discover the demand and the prices of the shares. Furthermore, the costs of public issue are much reduced and the time taken for completion of the entire process is much lesser than the one in the normal public issue (The Times of India, n.d.).

Year	Nos. of Issues	IPOs taken for Study
2006	68	55
2007	83	83
2008	30	30
2009	20	20
2010	56	55
Total	257	243
Source: Authors' Compilation		

## **FINDINGS AND DISCUSSION ON IPOs (2006 - 2010)**

The Table 2 gives a details of the IPO activity from 2006-10. Simple returns ( $R_{it}$ ) were calculated to capture the market movements during the period between offer closures to listing.  $R_{it}$  measures whether an investor gained or lost by buying the shares during the IPO at the offer price and selling at the prevailing price on the listing day. If  $R_{it}$  is positive, one may infer that the issue is under-priced. If  $R_{it}$  is negative, one may understand that the issue is over-priced. If  $R_{it}$  is zero, it means that the issue is aptly priced (Kumar, 2007). The work of Kumar (2007) is extended by comparing the offer price with the opening as well as the closing price in order to identify the impact on the investors. For the primary dataset of 2006 to 2010, when the average percentage  $R_{it}$  is computed by taking the offer (opening) price and the listing price of the 243 IPOs under study, we can obtain the categorization of IPOs in the category of overpriced, under-priced and aptly priced, which is described in the Table 3. The results of the average percentage  $R_{it}$  with closing price and offer price of the IPOs are mentioned in the Table 4.

Number of IPOs	Average % $R_{it}$	Interpretation	Impact on Investors
36	-11.81%	Over-Priced	Winner's Curse
194	23.93%	Under-Priced	Boon
13	0.00%	Aptly Priced	Neutral
*Note: Offer Price and Opening Price is used in the computation of $R_{it}$ .			
Source: Authors' Computation			

Number of IPOs	Average % $R_{it}$	Interpretation	Impact on Investors
86	-15.15%	Over-Priced	Winner's Curse
157	40.21%	Under-Priced	Boon
0	0.00%	Aptly Priced	Neutral
*Note: Offer Price and Closing Price is used in the computation of $R_{it}$ .			
Source: Authors' Computation			

There are two ways in which IPOs can be priced - that is fixed price and book built. From the data obtained out of 243 book built IPOs, it may be inferred that in overpricing, if the stock is offered to the public at a higher price than what the market will pay, then the stock tends to fall in value on the first day of trading, and it may eventually lose its marketability and value in the future. For an overpriced issue, underwriters too have a trouble in selling the shares and meeting their commitments. Under-pricing of an IPO generates additional interest in the stock when it first becomes publicly traded. This can lead to significant gains for the investors. From the perspective of the company's underpricing an IPO, it results in - "money left on the table"- lost capital that could have been raised for the company, had the stock been offered at a higher price (IPO, n.d.). The price observed in the market on the listing day may vary from the offer price. This may be due to the overall market movements. Computations of market adjusted return ( $R_{mt}$ ) of the

IPOs are made for the same period. To compute the market adjusted return, adjustment is first made by calculating the returns on the market index (Nifty) during the same period. If  $R_{mt}$  is positive, it is considered that the market on the whole has moved up. If it is negative, it may be measured that there is a decline in the overall market, and if it is equal to zero, it may be accomplished that the market remained unchanged during the interval between IPO offering to its listing (Kumar, 2007). The work of Kumar (2007) is further extended by comparing the opening nifty index and closing nifty index on the last day of the IPO offering in order to identify the overall market sentiment. For the primary dataset of 2006 to 2010, when the average percentage  $R_{mt}$  is computed by taking the opening value and by alternatively taking the closing value of the Nifty Index on the day of listing and closing Nifty Index on the last day of the IPO offering, we may get to know about the overall market movements. The results of the same are presented in the Table 5 and Table 6.

<b>Table 5: Average % Market Adjusted Returns (<math>R_{mt}</math>)*</b>			
Number of IPOs	Average % $R_{mt}$	Interpretation	Market Sentiment
95	-5.01%	Decline in overall Nifty Index	Bearish
148	4.70%	Overall Nifty Index has gone up	Bullish
*Note: Opening Nifty Index and Closing Nifty Index on the last day of the IPO Offering is used in the computation of $R_{mt}$ .			
Source: Authors' Computation			

<b>Table 6: Average % Market Adjusted Returns (<math>R_{mt}</math>)*</b>			
Number of IPOs	Average % $R_{mt}$	Interpretation	Market Sentiment
101	-5.21%	Decline in overall Nifty Index	Bearish
142	7.21%	Overall Nifty Index has gone up	Bullish
*Note: Opening Nifty Index and Closing Nifty Index on the last day of the IPO Offering is used in the computation of $R_{mt}$ .			
Source: Authors' Computation			

From the Table 5 and Table 6, it may be inferred that there is a sharp fall in the market index Nifty at the time of closure of the trade. The market index Nifty has improved by the end of the closure of the day. Overall upward movement in the Nifty index indicates a bullish sentiment in the market at the time of a majority of the listings of IPOs. Anticipation of listing gains and purchasing of value buy stocks (from the secondary market) on the day of the listing could be a valid reason for positive sentiments in the market. On deducting the market returns from the IPO's returns, the resultant returns so obtained is called excess return ( $ER_{,,}$ ). If  $ER$  is positive, one may deduce that the issue is under-priced, after adjusting for the market movements in the intervening period. Negative value of  $ER$  indicates that the issue is overpriced, after adjusting for the market movements in the intervening period. If  $ER$  is equal to zero, it may be inferred that the issue is fairly priced, after adjusting for the market movements (Kumar, 2007). The result of the average  $ER$  is represented in the Table 7.

<b>Table 7: Representation of Excess Returns (<math>ER_{,,}</math>)</b>		
Number of IPOs	Average ER	Interpretation
86	-0.15	Over-Priced
154	0.40	Under-Priced
3	0.00	Fairly Priced
Source: Authors' Computation		

The statistical parameter for studying the short run analysis of IPOs on the day of listing as well as on the next day of listing was applied in this paper in connotation to the fundamental work of Kumar (2007). The average IPO return of both the days, i.e. on the listing day and on the next day of the listing is presented in the Table 8. It may be observed that

<b>Table 8: Average IPO Returns On The Listing And On The Day After The Listing</b>						
<b>Particulars</b>	<b>Listing Day</b>			<b>Next Day</b>		
	<b>Offer -Open</b>	<b>Offer- Close</b>	<b>Open-Close</b>	<b>Offer -Open</b>	<b>Offer- Close</b>	<b>Open-Close</b>
Mean	30.53%	60.32%	3.63%	46.63%	61.92%	1.05%
5% Trim Mean	30.07%	58.39%	3.13%	52.24%	65.32%	0.54%
Median	12.50%	35.19%	-0.55%	22.69%	34.41%	-0.25%
SD	91.41	118.86	65.30	68.79	117.62	27.55
Null Hypothesis (Ho)*	u = 26.35%	u = 27.26%	u = -0.77%	u = 0.03%	u = 0.64%	u = 0.67%
Alternate Hypothesis (H1)	u # 26.35%	u # 27.26%	u # -0.77%	u # 0.03%	u # 0.64%	u # 0.67%
t	4.99	7.11	2.29	8.76	10.19	1.07
p-value	0.00<0.05	0.00<0.05	0.02<0.05	0.00<0.05	0.00<0.05	0.28>0.05
Decision Rule	Ho is rejected	Ho is rejected	Ho is rejected	Ho is rejected	Ho is rejected	Ho is not rejected
N	243	243	243	243	243	243
N>0	194	157	131	119	156	129
Source: Authors' Computation						
*Note: The u values in all the cases are based on the previous similar study undertaken by Kumar (2007).						

on an average, IPOs were listed with a premium of 30.53% over the offer price, and the median premium was around 12.50%. On the listing day, the listed IPO closed at a premium of 60.32% over the offer price, and the median premium was around 35.19%. This implies that the average premium and median premium improved during the first trading session itself, which indicates positive sentiments and a high level of upward volatility in the market. The level of volatility is further confirmed by studying the SD, which is 91.41 and 118.86 during the open-offer and close-offer respectively. To report for the possibility of outlier effect, average trimmed mean (5% i.e. ignoring 5% of the observations or 12 observations -extremely high and low data points) opening returns and the average trimmed mean closing returns marginally decreased to 30.07% and 58.39% respectively, thereby confirming that under-pricing of IPOs is not caused by a few outliers. This indicates that the under-pricing of IPOs was purely due to the price discovery on account of the book built mechanism, which favoured the investor to derive a positive gain. Whether the average returns are statistically significant or not were examined by running a cross-sectional 't' statistic and the corresponding 'p' values, which indicate that the listing day excess returns were statistically significant. The last row representing N>0, indicates that out of the 243 sampled IPOs, 194 IPOs were listed with a positive return, while the rest opened at a discount to the offer price. On the listing day, a noteworthy point which has been found that is that, all those 194 IPOs which listed at a premium did not close at a premium at the end of the day. In fact, 37 IPOs which listed at a premium closed at a discount (when compared to the offer price) on the listing day.

The intraday returns were also examined. Intraday refers to a position where the investor buys the shares at the opening price and sells by the end of the day at the closing price. It was observed that there was an average positive return of 3.63%. The corresponding 't' statistic explains that the returns are statistically significant. It can be inferred that the listing of IPOs does provide economically considerable trading opportunities for a day trader. The second day's (next day after the listing day) return analysis shows that all the IPO investors gain on the listing day's performance. 46.63% were the percentage average returns on the next day of the listing with respect to the opening price of the next day. At the closure of the next day of the listing, the returns improved to 61.92%, with a high SD of 68.79 to 117.62. If any trader bought the IPOs on the listing day at the opening or closing price, with an intention of profiting from liquidating the position at the opening or closing levels on the second day, they would have earned a meager return of 1.05%. The corresponding 't' statistic explains that the returns are statistically insignificant. Moreover, the median return is also found to be -0.25%. It is further observed that out of the 194 IPOs which were listed at a premium on the listing day, only 129 IPOs were found to be traded at a premium on the next day of the listing, at the closure of the trade. This indicates a high level of volatility prevalent in the secondary market, which is due to the presence of intraday traders, speculators, and arbitrageurs. These players do offer momentum to the prices of a stock.

## RELEVANCE OF FUNDAMENTAL ANALYSIS OF IPOs

Investors often ignore research, on the contrary, they rely on rumors and tips given by 'questionable experts'. Some investors do engage in 'analysis paralysis' - they do not adhere to the red herring prospectus, IPO grading, and calculative extensive mathematical formulas to derive returns based on sound facts and fundamentals (Taulli, 2000). Investment Information and Credit Rating Agency of India Ltd. (ICRA Ltd.) assigns IPO grading on a scale of IPO grade 5 to IPO grade 1. Institutes like Credit Rating Information Services of India Limited (CRISIL), Credit Analysis and Research Limited (CARE), Brickwork Ratings (BWR) also offer IPO grading services. The grading facilitates the assessment of equity shares offered to the public. The grade 5 signifies strong fundamentals ; the grade 4 represents above-average fundamentals; the grade 3 symbolizes average fundamentals; the grade 2 specifies below average fundamentals, and the grade 1 indicates poor fundamentals. The grade evaluates the prospect of the industry in which the company operates, the company's strength, its risk taking ability, its financial position, risk assessment of Greenfield and Brownfield projects, and the management's capacity to execute the projects. The grade keeps away from commenting on valuation, pricing of the IPO and forecasting of the returns to the shareholders on subscription of the IPOs (ICRA, n.d.). In the list of 243 IPOs under study, it was found that only 90 IPOs were graded. The summary of the grade and its impact is presented in the Table 9.

IPO Grade	Nos. Of Companies	Interpretation
5	2	Strong Fundamentals
4	24	Above Average Fundamentals
3	32	Average Fundamentals
2	26	Below Average Fundamentals
1	06	Poor Fundamentals
<b>Total</b>	<b>90</b>	<b>Graded IPOs</b>

Source: Authors' Compilation

Thus, retail investors must especially use the tools like prospectus and IPO grading before subscribing to an IPO. Volatility of the stock increases once it gets listed on the secondary market. Fundamentally strong IPO picks must only find a place in an investor's portfolio.

## CONCLUSION AND SUGGESTIONS

It is a common fallacy that IPOs are a guaranteed road to riches. Compared to investment in the secondary market, investing in IPOs is a risky business as there is no track record of the performance of the stock. IPO subscription requires more fundamental research, because picking the wrong stock will erode the value of money and result in severe losses. Investors, before investing their kitty in the stock, must study the fundamentals, IPO grade and prospectus, rather than blindly relying on the tips of given by brokers. SEBI must make it mandatory for companies to disclose their IPO grade in their prospectus, and companies without IPO grades should not be allowed to come out with an IPO. An online study module can be uploaded on the websites of NSE, BSE and SEBI for the benefit of the retail investors. The module must incorporate the basic fundamentals - the prospectus and details about IPO grading along with complete interpretation of the same. Prospective investors can make a self-study from such modules before investing in the companies. IPOs are a boon if proper homework is done by the investors for selecting a value buy company. IPOs turn out to be a bane when the groundwork of studying the company is not done. The market regulator SEBI analyzed that there is aggressive movement in the prices of shares on the listing of the IPO. As reported in the Gujarati daily '*Gujarat Samachar*' dated November 18, 2011, some of the IPO operators, speculators and insider traders artificially generate aggressive movement in the prices of the shares, due to which the retail investors often encounter losses and their investments depreciate. To curb this activity, SEBI has planned to implement a circuit limit on the upward and downward price movement in the share, after the few days of its listing (IPO, 2011). This would prove to be a good move to protect the retail investors, and it should be implemented without any delay. Thus, IPOs are like a VIP ticket which gives a privilege of direct entry to the retail investors in a company and also provide a fair

chance to become rich.

## SCOPE FOR FUTURE RESEARCH

The same type of research can be carried out for analyzing the performance of sector specific IPOs. The same study can be replicated with respect to the listing on BSE. Comparing the study of IPOs listed on the BSE and NSE, one can compare the volatility present in the market and also identify the presence of arbitrage opportunities, if any. A primary research can be undertaken to know the investment habits of retail investors with respect to IPOs. In the primary study, investors can also be educated on the upcoming concept of IPO grading. Such type of studies can be duplicated for those IPOs (if any) which get listed on other regional stock exchanges. Region specific primary studies can be conducted for retail investors to comprehend their IPO investment methods and mechanisms adopted for the same.

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**APPENDIX 1**  
**List of IPOs Used For The Study**

<b>Name of the Company</b>	<b>Name of the Company</b>	<b>Name of the Company</b>
20 Microns Ltd.	Godawari Power and Ispat Ltd.	Onmobile Global Ltd.
Abhishek Mills Ltd.	Godrej Properties Ltd.	Opto Circuits (India) Ltd.
Accel Frontline Ltd.	Goenka Diamond & Jewels Ltd.	Orbit Corporation Ltd.
Action Construction Equipment Ltd.	Gokul Refoils and Solvent Ltd.	Oriental Trimex Ltd.
Adani Power Ltd.	Gravita India Ltd.	Page Industries Ltd.
Adhunik Metaliks Ltd.	GSS America Infotech Ltd.	Paarabolic Drugs Ltd.
Advanta India Ltd.	Gujarat Pipavav port Ltd.	Parsvnath Developers Ltd.
Akruti Nirman Ltd.	Gujarat State Petronet Ltd.	Persistent Systems Ltd.
Alkali Metals Ltd.	GVK Power & Infrastructure Ltd.	Pipavav Shipyard Ltd.
Allcargo Global logistics Ltd.	Gyscoal Alloys Ltd.	Plethico Pharmaceuticals Ltd.
Allied Digital Services Ltd.	Hanung Toys and Textiles Ltd.	Pochiraju Industries Ltd.
Alpa Laboratories Ltd.	Hathway Cable & Datacom Ltd.	Power Finance Corporation Ltd.
AMD Metplast Ltd.	Hindustan Media Ventures Ltd.	Power Grid Corporation of India Ltd.
Aqua Logistics Ltd	House of Pearl Fashions Ltd.	Pradip Overseas Ltd.
Archidply Industries Ltd.	Housing Development and Infrastructure Ltd.	Prakash Steelage Ltd.
Aries Agro Ltd.	HOV services Ltd.	Pratibha Industries Ltd.
ARSS Infrastructure projects Ltd.	ICRA Ltd.	Precision Pipes and Profiles Company Ltd.
Ashoka Buildcon Ltd.	Idea Cellular Ltd.	Prestige Estates Projects Ltd.
Asian Aranito India Ltd.	IL&FS Transportation Networks Ltd.	Prime Focus Ltd.
Astec Lifesciences Ltd.	Indiabulls power Ltd.	Punjab & Sind bank
Aster silicates Ltd.	Indian bank	Purvankara Projects Ltd.
Atlanta Ltd.	Indosolar Ltd.	Pyramid Saimira theatre Ltd.
Austral Coke & Projects Ltd.	Indowind Energy Ltd.	R Systems International Ltd.
Autoline Industries Ltd.	Indus Fila Ltd.	R.P.P. Infra Projects Ltd.
B. L. Kashyap & Sons Ltd.	Infinite Computer Solutions (India) Ltd.	Raj Oil Mills Ltd.
Bajaj Corp Ltd.	Info Edge (India) Ltd.	Raj Rayon Ltd.
Bang Overseas Ltd.	Inox Leisure Ltd.	Raj Television Network Ltd.
Barak Valley Cements Ltd.	Insecticides (India) Ltd.	Ramky Infrastructure Ltd.
Bedmutha Industries Ltd	Intrasoft Technologies Ltd.	Ravi Kumar Distilleries Ltd.
BGR Energy Systems Ltd.	IRB Infrastructure Developers Ltd.	Redington (India) Ltd.
Bhagwati Banquets & Hotels Ltd.	IVR Prime Urban Developers Ltd.	Reliance Power Ltd.
Binani Cement Ltd.	J. K. Cement Ltd.	Religare Enterprises Ltd.
Birla Cotsyn india Ltd.	J. Kumar Infraprojects Ltd.	Renaissance Jewellery Ltd.
Blue Bird (India) Ltd.	Jagran Prakashan Ltd.	Resurgere Mines & Minerals India Ltd.
Brigade Enterprises Ltd.	JHS Svendgaard Laboratories Ltd.	Roman Tarmat Ltd.
Broadcast Initiatives Ltd.	Jindal Cotex Ltd.	Royal Orchid Hotels Ltd.
BS Transcomm Ltd.	JSW Energy Ltd.	Ruchira Papers Ltd.
C & C Constructions Ltd.	Jubilant Foodworks Ltd.	Rural Electrification Corporation Ltd.
Cairn India Ltd.	Jyothy Laboratories Ltd.	Sadbhav Engineering Ltd.
Cantabil Retail India Ltd.	K Sera Sera Productions Ltd.	Sejal Architectural Glass Ltd.
Career Point Infosystems Ltd.	K.P.R. Mill Ltd.	SEL Manufacturing Company Ltd.

Central Bank of India	Kaushalya Infrastructure Development Corporation Ltd.	Shree Ashtavinayak Cine Vision Ltd.
Cinemax India Ltd.	Kaveri Seed Company Ltd.	Shree Ganesh Jewellery House Ltd.
Coal India Ltd.	Kewal Kiran Clothing Ltd.	Shriram EPC Ltd.
Commercial Engineers & Body Builders Co Ltd.	Kiri Dyes and Chemicals Ltd.	Simplex Projects Ltd.
Consolidated Construction Consortium Ltd.	KNR Construction Ltd.	Sita Shree Food Products Ltd.
Cords Cable Industries Ltd.	Kolte Patil Developers Ltd.	SJVN Ltd.
Cox and Kings (India) Ltd.	Koutons Retail India Ltd.	SKS Microfinance Ltd.
D B Realty Ltd.	KSK Energy Ventures Ltd.	SMS Pharmaceuticals Ltd.
D. S. Kulkarni Developers Ltd.	L.T.Overseas Ltd.	Sobha Developers Ltd.
D.B. Corp Ltd.	Lanco Infratech Ltd.	Solar Explosives Ltd.
Decolight Ceramics Ltd.	Lotus Eye Care Hospital Ltd.	Sun TV Ltd.
Den Networks Ltd.	Magnum Ventures Ltd.	Supreme Infrastructure India Ltd.
Development Credit Bank Ltd.	Mahindra & Mahindra Financial Services Ltd.	Syncom Healthcare Ltd.
Dhanus Technologies Ltd.	Mahindra Holidays & Resorts India Ltd.	Take Solutions Ltd.
DLF Ltd.	Man Infraconstruction Ltd.	Talwalkars Better Value Fitness Ltd.
Eclerx Services Ltd.	Manaksia Ltd.	Tanla Solutions Ltd.
Edelweiss Capital Ltd.	Mandhana Industries Ltd.	Tarapur Transformers Ltd.
Edserv Softsystems Ltd.	Maytas Infra Ltd.	Tech Mahindra Ltd.
Electrosteel Steels Ltd.	MBL Infrastructures Ltd.	Technocraft Industries (India) Ltd.
Emmbi Polyarns Ltd.	Meghmani Organics Ltd.	Technofab Engineering Ltd.
Empee Distilleries Ltd.	MIC Electronics Ltd.	Tecpro Systems Ltd.
Entertainment Network (India) Ltd.	Microsec Financial Services Ltd.	Texmo Pipes & Products Ltd
EROS International media Ltd.	Mindtree Consulting Ltd.	Thangamayil Jewellery Ltd.
ESS DEE Aluminium Ltd.	Moil Ltd.	Thinksoft Global Services Ltd.
Euro ceramics Ltd.	Motilal oswal financial services Ltd.	Time technoplast Ltd.
Euro Multivision Ltd	Mudra Lifestyle Ltd.	Titagarh Wagons Ltd.
Everonn Systems India Ltd.	Mundra Port and SEZ Ltd.	Transformers and Rectifiers (India) Ltd.
Evinix Accessories Ltd.	Nelcast Ltd.	Transwarranty Finance Ltd.
Excel Infoways Ltd.	NHPC Ltd.	Tulsi Extrusions Ltd.
FIEM Industries Ltd.	Nissan Copper Ltd.	United Bank of India
First Winner Industries Ltd.	Nitco Tiles Ltd.	Uttam Sugar Mills Ltd.
Firstsource Solutions Ltd.	Nitesh Estates Ltd.	VA tech Wabagh Ltd.
Fortis Healthcare Ltd.	Nitin Fire Protection Industries Ltd.	Vascon Engineers Ltd.
Future Capital Holdings Ltd.	Nitin Spinners Ltd.	V-guard Industries Ltd.
Gammon Infrastructure Projects Ltd.	NMDC Ltd.	Visa Steel Ltd.
Gitanjali Gems Ltd.	Nu Tek India Ltd.	Vishal Information Technologies Ltd.
Global Broadcast News Ltd.	Oberoi Realty Ltd.	Vishal Retail Ltd.
Global Vectra Helicorp Ltd.	Oil india Ltd.	Voltamp Transformers Ltd.
Globus Spirits Ltd.	Omaxe Ltd.	XL Telecom Ltd.
GMR Infrastructure Ltd.	Omnitech Infosolutions Ltd.	Zylog Systems Ltd.
Source: National Stock Exchange of India (n.d.), ( <a href="http://www.nse-india.com/products/content/equities/ipos/historical_ipo.htm">http://www.nse-india.com/products/content/equities/ipos/historical_ipo.htm</a> )		