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Performance Evaluation of IPO's introduced in NSE during 2015-2016

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Abstract:
This research paper has examined the trend and performance of IPO introduced in the National Stock Exchange during April 2015 to March 2016. Through the research conducted it was found that found that there were total of 21 companies who raised their funds through IPO in the respective year. The paper also focused on the aspect of identifying the underpricing and overpricing of these IPOs introduced in NSE for raising fund, the amount of fund raised and number of equity shares also included anchor portion of equity. The sum total of the fund raised by all the 21 IPO's was 132750million. 8 out of 21 companies had LTP (last traded price) less than that of the issue price.

Keywords: *Initial public offer (IPO), Last traded price (LTP)*

1. Introduction

A company has different modes of raising funds for capital, which can be classified on the basis of time for which the funds are required in the company i.e. short term funds which are generally less than or equal to one year, and long term funds which are for longer period. Company then chooses the mode of raising fund based on the duration and other factors like risk, rate of interest, liability, credit worth etc. IPO also known as Stock Market Launch is done by Privately Owned Company looking to become publicly traded wherein they offer their stock for raising long term funds to expand their capital, by inviting public to buy its stock and lend them money required by them in return of the stock offered The process involve appointing of an underwriting firm, institutional investor to whom the offer is made that in turn invites public through stock exchange for the very first time. Though IPO is considered as risky investment because market behavior is not known in volatile share market.

2. Review of Literature

Beatty and Ritter (1986), Rock (1986) investigated and found that lack of symmetry between the participants in the IPO market i.e., investors and investment bankers or informed and uninformed investors determines the under pricing of IPO. The evidence in favour of the asymmetric information theory has been widely discussed by Beatty and Ritter (1986), Kon & walter (1989), Megginson & Weiss (1991), and Hanley (1993).

Qiming Wang (2009) in his study on IPOs in the Secondary market stated that the integer price clustering of IPOs in the secondary market trading in the first 240 days trading days after their IPOs dates indicate the huge difference between the integer price frequency of IPOs in the primary market and that of matched stocks in the secondary market almost disappears on the first trading day after IPO. The integer price frequency of IPOs is still significantly higher than that of matched stocks during the first 240 trading days. However after controlling the price level, trading characteristics and IPO price support, the integer price frequency of IPOs conforms to that of matched stocks and that those IPOs with integer offer prices have the same integer price frequency as IPOs without.

Under the study conducted by Tinic (1998), it was found that underpricing of Initial public offerings is a lawsuit avoidance hypothesis. The lawsuit avoidance hypothesis states that firms that are subject to higher litigation risk underprice their issues more to reduce the likelihood of being sued in connection with their IPO. In addition, by underpricing their issues firms can limit the amount of damages plaintiffs can claim in the lawsuit.

3. Research Significance

Since India has become a global market hub and the rapid growth and development is further contributed by the firms who raise the funds from the IPOs through the capital market. So, this paper examines that while the companies raise the funds from the IPOs and use it for the purpose of growth and expansion, does the similar thing happen with the investors too? E.g., when an investor invests in IPOs of a particular company, his/her main motive is to earn a handsome return. Now, the companies are earning a handsome return by raising the capital but buying an IPO will give an investor and underpricing stock or the overpricing stock? This is being examined in this paper. Moreover, the focus in on the IPOs who have been launched in NSE during the financial year 2015-16.

4. Objectives of the study

- The main objectives of the study include
- To analyze the trend and performance of IPO's issued in NSE for the year 2015-2016
- To ascertain the underpricing and over pricing of stock of NSE.
- To study the factors leading in the underpricing and overpricing of the stock.

5. Research Methodology

- **Time duration of study:** To ascertain the performance of stock in NSE, the data for the same has been taken from April 2015-March 2016, which include all the IPO's of NSE during that period.
- **Data collection:** The data has been extracted from the official website of NSE for the period April 2015-March2016. This study includes the data set of 21 IPOs, out of which 8 companies had LTP lower than their issue price.
- **Sample selection:** Number of IPOs listed in NSE from the year 2010-2016 is total of 134 firms out of which the sample selection used in this study consists of all the Indian private companies, which went public on National Stock Exchange (NSE) from 2015-2016.
- **Sources of data:** The study in this research paper does not contain any primary data and is completely based upon secondary data which has been taken from the official website of NSE and includes information of stock , issue price, issue size, information on listing , LTP etc.

5.1 Data Analysis Method

There are different methods to measure the difference between the first trading price and the issue price.

Under pricing- It is pricing of a stock below market value; whenever the stock is first traded below the offer price it is called under pricing.

Under pricing = (First day Closing price - Offer price) /offer price *100%

Where the first day closing price is equal to the amount against the stock which investors are willing to pay, if the offer price is less than first day closing price it is then said to be under pricing.

Overpricing- It is pricing of a stock above the market value; whenever the stock is first traded above the offer price it is called overpricing.

Overpricing = (Offer Price - First day Closing price) / First day Closing price *100%

Where the first day closing price is equal to the amount against the stock which investors are willing to pay, if the offer price is more than the first day closing price it is then said to be overpricing.

6. About IPOs and its Process

The companies are broadly classified into two types publicly held company and private company. A public company is the one which has its stock freely traded into the stock market and where investors can freely participate in trade, whereas private company is the one which is owned by private entrepreneurs which does not means that they cannot raise their capital through issuing of stocks, but limits them from trading their stocks in public exchange. IPO is a process wherein private companies wishing to go public offer their stocks to the public for the first time called as initial public offer.

IPO is a dream of every entrepreneur who starts their own company (private) to get them listed in the stock exchange. There are various reasons, for which a company chooses to go for IPO as stated,

- A public company enjoys the option of raising additional revenue through additional offerings.
- Once a private company goes for IPO then it can sell their future equity stakes and can have increased access to the debt market.
- When a company goes public it results in rise of the value of company, which increases the share price resulting in growth of total net worth of the company.
- IPO or trading in equity increases the liquidity of the company, which help the company in various manners like attracting top talent and introducing new schemes and plans for the employees of company.

6.1 The Underwriting Process

For IPOs a private company starts with the appointing of an underwriter or an investment institution. In India trading requires the involvement of a broker/middleman and so is the underwriter acting as a middle person between the company and the market. The process starts with the meeting of both the parties and deciding upon the things like issue size, price range, type of securities (debt, equity) , bidding , issue date etc. and negotiating the deal. After the negotiation and final appointment of bank the actual role of the underwriter comes into action. It then file a statement of registration with Securities and Exchange Commission (SEC) with all the required documents i.e. companies document of financial statements, characteristics of top management of the company, details of upcoming projects and answers to the need of money. SEC, then inspect that all the information is adequately provided and is true in all aspects, and only after the proper investigation, SEC approves the offering with an offer date. By the time underwriter issues an initial prospectus to interest and inform the general public about the company and the projects taken upon except the offer date and offer price which is yet to be decided. Before the offer date approaches both the parties sit together for making a decision about the offer price keeping in view the worth of the company, demand and current market conditions. On the effective date the securities are then sold to the investors and money from them is procured.

6.2 Under pricing and overpricing

Whenever the opening price of any stock is more than that of its closing price it is then said to be overpricing as, when the demand for the stock increases in the market the price for it rises and the difference then measured between the offer for the IPOs stock and its closing price on the first trading day is said to be Overpricing. Whereas under pricing is when the price of the IPO is below the market price of that IPO. Though under pricing is a very short term affair, where the price of the stock are ragged up by the market forces of demand and supply.

6.3 Why under pricing and overpricing of IPOs

There are various reasons for which any company or underwriter go for under pricing and overpricing of IPO which include asymmetric information, Disagreement between Management , role of underwriters, uninformed investors and behavioral explanations.

6.3.1 Asymmetric Information

This is the most common reason for under pricing of an IPOs as the theory of it involves around the inconsistency of information to investors. According to this theory majority of the investors in the market are uninformed and they bid without paying any regard to the quality of IPO whereas the informed put his money where he can see great returns, and so lack of information results in losses of uninformed investors which force them to exit the IPO market, whereas the underwriters need uninformed buyers to bid for their IPO because very few in the market exist those who are informed investors, therefore to solve the problem underwriters usually go for under pricing of IPO.

6.3.2 Role of Underwriters

Underwriters play the major role in the pricing of stock and so sometimes they create excessive demand for stock to ensure that after the contractual period, the price for the IPO rises. So under pricing of stock initially ensures that there are many purchasers of the shares. Though this theory lack any practical evidence.

6.3.3 Behavioral Explanations

It is seen that uninformed investors get excited and irrationally bid for the IPOs, where they bid for the price which is extremely beyond the actual and fundamental value of IPO, the trend is not followed by the other investors they overlook to the response of earlier investors and invest accordingly. In the process Managers gain from the irrational act of the investors and therefore this result in one of the reason to under price IPO.

7. Conclusions and Findings

7.1 Conclusions

From the study we found that for all the 21 companies' major book leading Managers are Axis Capital Ltd, Kotak Mahindra capital co. ltd, Citigroup global, Edelweiss Financial Services ltd and ICICI securities ltd.

The below table contain all the IPOs issued in the year 2015-2016 in NSE, with the evaluation of their performance.

Table 1: Details of IPOs introduced companies

Name of the Company	Issue Price	Last Traded Price	Date of Listing	Performance
Ortel communication ltd	181	155	March 19,2015	Overpriced
Adlabs entertainment ltd.	180	102.25	April 6, 2015	Overpriced
Inox wind ltd	325	213.75	April 9, 2015	Underpriced
VRL logistics ltd	205	312	April 30, 2015	Underpriced
MEP infrastructure Developers ltd	63	41.95	May 6, 2015	Underpriced
UFO Moviez india ltd	625	455.20	May 14, 2015	Overpriced
PNC Infratech ltd	378	126.60	May 26, 2015	Underpriced
Manpasand Beverage ltd	320	728	July 9, 2015	Overpriced
Syngene International ltd	250	493.85	Aug 11,2015	Underpriced
Power Mech projects ltd	640	491	Aug 26, 2015	Overpriced
Navkar Corporate ltd	155	196	Sept 9, 2015	Overpriced
Pennar engineered Building system ltd	178	193.85	Sept 10, 2015	Overpriced
Shree Pushkar chemicals and fertilisers limited	65	169.30	Sept 10,2015	Overpriced

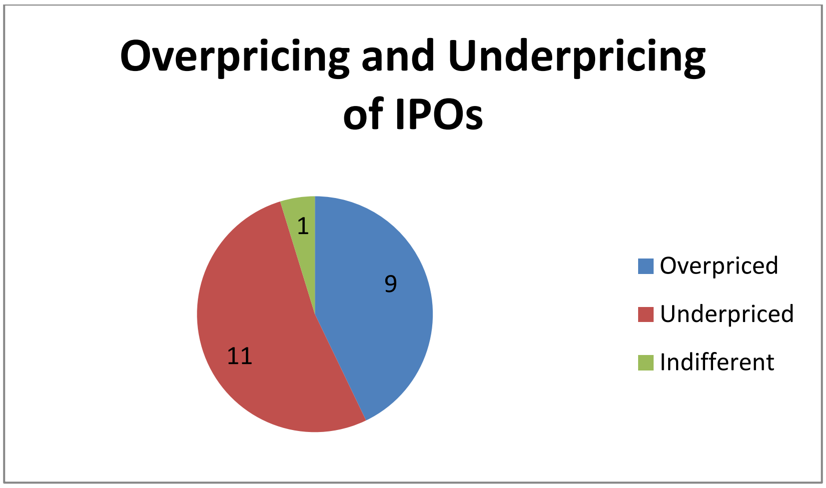
Sadbhav infrastructure project limited	103	106.65	Sept 16, 2015	Underpriced
Prabhat dairy limited	115	124.30	Sept 21,2015	Indifferent
Coffee day Enterprises limited	328	226.50	Nov 2,2016	Overpriced
Interglobe Aviation limited	950	765	Nov 10, 2015	Underpriced
S H Kelkar and company limited	180	297.10	Nov 16, 2015	Underpriced
Dr lal path labs limited	550	1051.10	Dec 23, 2015	Underpriced
Alkem Laboratories limited	1050	1658.00	Dec 23, 2015	Underpriced
Narayana Hrudayalaya	250	334.00	Jan 6, 2016	Underpriced

Source: NSE Website

7.2 Findings

Out of 21 IPOs introduced in NSE during the financial year 2014-15, it was being found out through this paper that 9 companies IPOs were overpriced, 11 companies IPOs were underpriced and 1 IPO price was indifferent i.e., the issue/offer price was equal to the day listing opening price.

Figure 1: Number of overpriced and underpriced IPOs



Since, the number of underpriced IPOs are more than the number of IPOs overpriced, that trend shows that the companies are generally setting the issue/bid price lower than the expectation of the market investors so that the companies may give an opportunity for the investors to get the capital gain in the form of day listing gain on the date of issue of the IPOs in the stock market.

Although we have 9 IPOs who are overpriced too. This trend shows that either the portfolio manager of these companies did not correctly estimated the market sentiments and the true valuation was not there while setting up the bid/offer price for these IPOs otherwise the market could have given the opportunity for investors to gain put of these IPOs too. But, since the theory of efficiency says if the markets are efficient then there will be no difference between the issue/bid price and the day listing opening price of these IPOs.

Out of 21 IPOs chosen during 2014-15, one IPO is there whose market price at day listing and the offer/bid price is same. This shows that the estimators/valuers have correctly estimated the issue/bid price of this IPO.

So, there is a mixed bag of feelings for the investors as out of 21 IPOs, 11 were underpriced and gave a day listing gain to the investors, on the other hand 9 IPOs were overpriced and resulted in capital loss to the investors on the date of day listing and one IPO was indifferent. Therefore, it is further

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observed that IPOs mispricing significantly impacts Investment Banks's reputation and hence pricing of IPOs has long term implications for policy makers, market intermediaries, as well as investors.

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