LITERATURE REVIEW

The published work relating to the topic is reviewed by the Researcher. The relevant literature is reviewed on the basis of Books, Periodicals, News Papers and Websites. The detailed review is given below:-

Arwah Arjun Madan (2003), in his article ‘Investments in IPOs in the Indian Capital Market’, published in Bimaquest conclude that in the long run (five-year after listing), there is a drastic fall in the return on IPOs returns; returns are found to be negative from the second to the fifth year of listing.


Atul Mehra (2010) “IPO Boom”, Business Today, point out that promoters are in hurry to IPO because they do not want to be left out.

Aggarwal, R., P. Conroy (2000), “Price Discovery in Initial Public Offerings and the Role of the Lead Underwriter”, Journal of Finance, conclude that the price discovery process of initial public offerings (IPOs) using a unique dataset. The first quote entered by the lead underwriter in the five-minute preopening window explains a large proportion of initial returns even for hot IPOs. Significant learning and price discovery continues to take place during these five minutes with hundreds of quotes being entered. The lead underwriter observes the quoting behaviour of other market makers, particularly the wholesalers, and accordingly revises his own quotes. There is a strong positive relationship between initial returns and the time of day when trading starts in an IPO.
Ansari Abdul Aziz and Jane Samiran (2009), in their article “Stock Price Decision of Indian Investors”, published in The Indian Journal of Commerce concluded that rational traders are using both fundamental analysis and technical analysis as stock selection tools, which does not support the view of finance theorist.

Bhupal Sing (2009), in his article “Changing Contours of Capital flows to India, published in Economic and Political Weekly, pointed out that the most striking feature of change in the cross-border capital flows to emerging market economies during the 1990s is the emergence of portfolio equity inflows. It was further stated that portfolio investment in India started in 1993 by way of the equity and debt investment by FIIs in the Indian Stock Markets and Global offerings of ADRs and GDRs by the Indian Corporate. The FIIs turnover accounts for a significant share of the cash segment turnover of stocks. The stocks have potential for large volatility in the asset prices.

Chowdhry, B., V. Nanda, in their article “Stabilization, Syndication, and Pricing of IPOs”, published in Journal of Financial and Quantitative Analysis point out that in the after-market trading of an IPO, the underwriting syndicate, by standing ready to buy back shares at the offer price (“price stabilization”), compensates uninformed investors ex post for the adverse selection cost they face in bidding for IPOs. This dominates ex ante compensation by underpricing. The reason is that stabilization exploits ex post information about investor demand whereas underpricing must be based on ex ante information. However, liquidity and syndication costs constrain the use of stabilization which, in equilibrium, generates some underpricing as well. We develop a model that formalizes this intuition and generates several empirical implications.

Dhananjay Rakshit (2008), in his article “Capital Market in India and Abroad – A Comparative Analysis”, published in Indian Journal of Accounting, December, concluded that Indian Market is being continuously preferred by the foreign investors and the only cause of concern is its high analyzed volatility.
Dhruv Gogoi (2010), in his article “Big, Bold and Beautiful?” published in the Businessworld, pointed out that Coal India’s IPO has raised great expectations among investors.

India could herald global IPO recovery, published by FE Bureau, in The Financial Express according to the Eanst & Young, Institutional Investor IPO survey, 2009. IPOs in these emerging markets would show recovery from the economic downturn by the year end. Of the over 300 institutional investors surveyed, as much as 57% believed India and Brazil are the most likely to lead the recovery, in terms of new forms entering the local capital market by the end of 2009. IPO activity in the last two quarters confirms that markets are making an early recovery, notably in emerging economies of India, China and Brazil. A stable government and booming sensex has led to the revival of IPO activity.

Jagannadham Thunuguntla (2011) in his article “IPOs: More Misses Than Hits”, published in the Dalal Street Investment pointed out that, the age old philosophy of understanding the company and sticking to the basics should be given due respect. Let the buyer be made aware that the investor has to put a price tag to his hard earned money. There is a need for investor education and awareness and the connections should be on a stable income than an becoming rich overnight.

Jain, B. A., O. Kini (1994), in their article “The Post-Issue Operating Performance of IPO Firms”, published in Journal of Finance point out that the change in operating performance of firms as they make the transition from private to public ownership. A significant decline in operating performance subsequent to the initial public offering (IPO) is found. Additionally, there is a significant positive relation between post-IPO operating performance and equity retention by the original entrepreneurs but no relation between post-IPO operating performance and the level of initial underpricing.
Jain, B. A., O. Kini (1995) in their article “Venture Capitalist Participation and the Post-Issue Operating Performance of IPO Firms”, published in Managerial Decision Economics mention that by comparing the post-issue operating performance of venture capitalist-backed IPOs with a matched sample of non-venture capitalist-backed IPOs. We find that venture capitalist-backed IPO firms exhibit relatively superior post-issue operating performance compared to non-venture capitalist-backed IPO firms. Further, the market appears to recognize the value of monitoring by venture capitalists as reflected in the higher valuations at the time of the IPO. Finally, we find that proxies for the quality of venture capitalist monitoring are positively related to post-issue operating performance.

James H. Lorie, Peter Dodd and Mary Hamilton, Kimpton (1997), in their book, “The Stock Market – Theories and Evidence”, IFCAI Publication, Hyderabad, pointed out that the value of a corporations stock is determined by expectations regarding future earnings of the corporation and by the rate at which those earnings are discounted. In a world of no uncertainty, all securities would offer a certain return equal to the real rate of return in capital.

Jay R. Ritter (1998) in their article “Initial Public Offerings”, published in the Contemporary Finance Digest summaries that Companies going public, especially young companies, face a market that is subject to sharp swings in valuations. Pricing deals can be difficult, even in stable market conditions, because insiders presumably have more information than potential outside investors. To deal with these potential problems, market participants and regulators insist on the disclosure of material information.

Jignesh B. Shah and Smita Varodkar in their article “Capital Market: Trends in India and abroad – impact of IPO Scam an Indian Capital Market”, published in the Souvenir, All India Accounting Conference, November, S. D. School of Commerce, Gujarat University, Ahmadabad, concluded that the recent IPO Scam indicates that even a highly automated system will not prevent malpractices. But
steps should be taken by SEBI to restrict such IPO Scam by applying know your customer (KYC) and unique identification number to market players and investors.

K. C. John Sasi Kumar in their article “Indian Primary Market – A Review”, published in International Journal of Contemporary Business Studies, concluded that the performance of IPO’s has been cheering to the investors. Retail investors can go for the IPO market for safe and secured investment. Even though the recent economic development has slowed the process of IPO issue we could expect speedy recovery of both the economy and IPO activities.

Madhumita Gosh, Vice President (PM & Research) Unicon Financial Intermediaries in her article “IPOs: More Misses Than Hits”, published in the Dalal Street Investment Journal, pointed out that, in the recent past a majority of IPOs haven’t performed well because valuation wise they are priced more than the fundamentals. This has happened mainly due to the greed of promotors, who want to price their issue invariably at a much higher price. In such cases merchant bankers’ role also comes under scanner as they usually don’t give proper advice to the promotors in the wake of losing the business.

Mahesh Nayak, (2010) in his article, ‘Of Primary Concerns’, published in the Businessworld, point out that, IPOs have grown in size and entered their own brave new world. Further he states that raising money in India’s booming economy cannot be a onetime affair; if a company does not maintain a good relationships with investors and rewards them well it may not able to go back to them when it want to raise money later.

M. S. Narasimhan and L. V. Ramana in their article “Pricing of Initial Public Offerings: Indian Experience, with equity issues”, published in Portfolio Management, Research Series in Applied Finance, the ICFAI Journal of Applied Finance concluded that:
a) Homogeneity in the degree of under pricing across time periods is observed.

b) The extent to which premium issues are underpriced is greater than in the case of the first trading day.

c) Under pricing is not related to the time interval between the offer day and the first trading day.

They further concluded that companies offering their stock at a premium prefer to play it safe in spite of the freedom granted to them operating at suboptimum levels to derive a satisfaction of the issue being fully subscribed may be a major factor in determining the pricing process.

Minakshi Malhotra (1997), in her article, “Free Pricing of Equity :- The Indian Experience”, Published in the Journal of Accounting and Finance Spring, 1997 pointed out that the period immediately after the introduction of free pricing witnessed charging of very high premium over par values and as compared to what would have been suggested by CCI. The majority of the issues failed to qualify the market test of performance as is revealed by the price behaviour of premium issues after a lapse of six months.

Nitish Ranjan & T P Madhusoodanan in their article “IPO underpricing, issue mechanism and size” published in the Social Science Research Network E-Library pointed out that IPOs in India have yielded abnormal returns in the very short term. The abnormal performance is also indicative of pricing errors in the issue process. The issues are under-priced whether the mechanism is fixed price or book building; we find that small size issues are more likely to be under-priced than larger issues. We formulate a model with homogenous investor beliefs to show that size is an important factor and that the underpricing is inversely proportional to size. This mechanism also suggests that IPOs will always be underpriced. However, in the presence of informed investors, a signaling equilibrium doesn’t exist and optimally high value firms don’t signal their value as aggressively as the lower value firms.
Despite such aggressiveness, the lower value firm ends up leaving money on the table, while the high value firm issue doesn’t leave money on the table. The model can explain hot (cold) markets by increased (decreased) sensitivity of the uninformed investor to the signaling by the firm. The hot/cold markets also influence the probability of a high/low value firm coming up with an IPO as imputed by the wider market.

Prithvi Haldea, CMD, Prime Database in his article “IPOs: More Misses Than Hits”, published in the Dalal Street Investment Journal pointed out that, IPOs in India have become an instrument of trading rather than investment and a majority of people are parking their money into such IPOs just to make a fast buck at the time of listing. So, in my view, they are not the investors who are investing money as per the valuations of the company by taking a long term horizon.

Rajendra Kanoongu, in his article “IPOs: More Misses Than Hits”, published in the Dalal Street Investment Journal, tated that, investors should wait for the project implementation of the company to take place and then take a real value of stock. If they are looking for listing then they better not to apply in the IPO and rather buy from the secondary market. They also mentioned major reasons for the underperformance of new issues; one is the uncertain market trend, wherein investors are not in a position to take a call whether the pricing is right or wrong. Secondly, the investors themselves, who are waiting for the listing gain and want to exit on the first day. And thirdly, to a certain extent there were ambitious valuations and though I will not say it is very high but were optimistic.

Rajiv Bhuva in his article “IPO BOOM - Fever Pitch” published in Business Today; pointed put that the year 2010 becomes record year for IPOs because so many companies comes with huge issue size for the investors.
Reena Agarwal in her article “Allocation of initial public offerings and flipping activity”, published in Journal of Financial Economics concluded that, there is a general perception that the large trading volume in initial public offerings is mostly due to “flippers” that are allocated shares in the offering and immediately resell them. On average, however, flipping accounts for only 19% of trading volume and 15% of shares offered during the first two days of trading. Institutions do more flipping than retail customers and hot IPOs are flipped much more than cold IPOs. Institutions do not quickly flip cold IPOs to take advantage of price support activities by the underwriter. Explicit penalty bids are rarely assessed against flippers.

Saurabh Ghosh (2004) in his article “Boom and Slump Periods in the Indian IPO Market”, published in the Reserve Bank of India Occasional Papers concluded that the Indian IPO market experienced a dramatic swing in terms of volume of new IPOs. The IPO volume series was auto correlated over the entire period and especially during the hot period. This shows a firm’s decision to go public over the last decade depended on the number of other companies that were getting listed over the previous months. The autocorrelation in the underpricing series was weak as compared to the IPO volume series. Turning to the interrelation of volume and initial return, the empirical exercise (Granger causality test) found no significant relation between IPO volume and initial returns during the hot and cold period. This suggests that Indian Issuers’ did not depend on the information content of the initial returns while taking their decision to go public. A key reason for these findings could be that, unlike the developed countries, it took a long time (more than six months on an average) for Indian companies to get actually listed on the stock market after the promoters decided to go public. Underpricing derived from the price changes over the six months (or more) perhaps also captured the changing investors’ expectation with the availability of new information rather than investors’ optimism *perse*. So Indian corporate bodies might have depended more on long lasting market sentiments to decide on the timing of their IPOs.
Subhojit Banerjee and Devesh Ranjan Tripathi in their article “Comparative Perspective of Foreign Banks in India: – Strategies and Trends” published in the Indian Journal of Accounting, pointed out that the Indian Equity Market has been of interest to many foreign investors in the recent times. With Indian Capital Markets performing far better than their Asian Counterparts are fast becoming hot destinations for investors far and near.

Subrahmanyam, A., S. Titman (1999) in their article “The Going Public Decision and the Development of Financial Markets”, published in the Journal of Finance mention that stock price efficiency, the choice between private and public financing, and the development of capital markets in emerging economies. Generally, the advantage of public financing is high if costly information is diverse and cheap to acquire, and if investors receive valuable information without cost. The value of public firms generally depends on public market size, which implies that there can be a positive externality associated with going public, so that an inferior equilibrium can exist where too few firms go public.

Sunil Damania in his article “Primary Issues” published in Dalal Street, mention that, the primary market has been always been a great area of interest for retail investors. But over the last few years the quality of IPOs and their issue prices have been a matter of concern. Due to this investors are losing faith in the IPO system and this is a very dangerous sign for the country. For any new investor to enter the market, the primary market is the first step. If that first experience of investment is not a happy one, it is unlikely that investors would continue investing in the market.

Vaidyanathan R. & Alok Pande (2008) in their article “Determinants of IPO under pricing in the national stock exchange of India”, published in the Social Science Research Network E-Library pointed out the degree of under pricing in the Indian stock markets has reduced over the years which is good for the firms getting listed as under pricing is an indirect cost to the firm. A unique contribution of this study is that the after market in India regards the final offer price which has been set
after book building as a credible signal for the firm’s under pricing. Another important parameter driving the under pricing positively is the listing delay whereas the money spent on marketing the issue is not reducing the under pricing of the firms significantly. This study also finds that the gains from IPOs get diffused within one month of the listing of the firms and on an average the gains in one month after listing are lesser than those of the market.

Vikkraman P. and K.C. John Sasi Kumar (2009) in their article “Investor’s preference on IPOs in India” presented in the Global Business & Management Forum (GBMF) Second International Conference, Dhaka, Bangladesh, find out the fundamental risk and returns involved in investment of IPOs and the performance of initial public offers for the last five years. The researcher assumes that the investments in IPOs are very safe, risk free, and make good returns. It was found from the research that returns out of IPOs during the short period is very promising.

Vineet Kohli (2009) in his article “Do Stock Markets Allocate Resources Efficiently? An Examination of Initial Public Offerings”, published in the Economic & Politically Weekly, concluded that high prices of new equity issues are not related to their future operating performance. It was shown that investors neglect the low profitability aspect of new issues and over emphasize their growth performance. The expectation of growth at the time of issue is not met subsequently. These conclusions have some important implications for the design of the financial system. It is often argued that a market-based financial system should be promoted since a bank-based system (especially the one with large presence of public sector banks) does not allocate resources to their profitable use. The large nonperforming assets of public sector banks are often cited as evidence of poor evaluation in the bank-based system. It was seen in this paper that equity markets in India have mainly financed lower profitability firms on the expectation that their earnings will grow in future. However, this expectation has not been realized subsequently as both profitability and growth of issuing firms have fallen in the post-issue period. This suggests that stock markets in India have suffered from excessive optimism and poor evaluation.