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A General Study on IPO in India

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***Abstract* - Initial public offering (IPO) is the process by which a firm sells its equity shares to the public for the first time. One of the challenges for the investors is to evaluate the pricing of the IPOs because IPO firms do not have historical price information. Various theories have been developed by the researchers from time to time explaining why the offering price of IPOs is set well below the first day trading price.**

In today's fast moving and dynamic world, short-term investors face difficulty while choosing which avenue to invest in. The article is about the general study done on the IPO in India. How does it work in India? What is the process to be followed in IPO? It also contains the information like the objectives of the IPO, advantages and limitations of the IPO and also the factors which influences the functioning of the IPO in India.

***Index Terms* – Floor price, issue price, red herring prospectus, listing date, over subscription, under subscription, lot size, book building process, underwriter.**

INTRODUCTION

IPO stands for Initial Public Offering; it is an offering of share from a company which is new to the share market and trading for the first time. This is done by offering those shares to public, which were held by the promoters or the private investors prior to the IPO. It is also defined as a first sale of stock to the public by a private company. Generally, they are offered by new, small scale or medium sized firms which are looking for raising of funds to grow and expand their business. In the case when other investors or promoter held the shares the stake holding comes down to extent their shares are offered to the public. Hence, the IPO is also referred as "public offering" or "flotation".

Here the IPO shares are freely traded in the market which is also known as "free float". Even though the IPO offers many benefits, there are few significant costs involved such as banking fees, accounting fees and legal expenses and have to fulfil the basic requirements to disclose the important and sensitive information. So, normally the IPOs are offered to public by disclosing the details of the proposed offering to the potential purchasers in the form of lengthy document called as "prospectus". Mostly the companies have to the Undertake the IPO with the assistance of investment banks for acting as an underwriter.

These underwriters render their services such as correctly assessing the value of share i.e., share price and establishing a public market for shares i.e., Initial sale. In few cases the alternatives like Dutch auction method have also been explored and applied for several IPOs. IPO trend in India came into existence in the eighties, when a large number of companies, organization came out with public issues, which triggered a growth in the primary market. An entire industry of agents, retail investors, brokers, and merchant bankers, grew in the primary issues market. Thus, the term IPO came into existence in India.

In early modern days, the Dutch were the first financial innovators who started and helped in laying the foundation for the modern financial system. The very first modern IPO in history was took place and started in the year 1602 when the Dutch East India company offered their company shares to the public with the aim of raising funds. Thus, we can say that the Dutch East India company is the first company in the history which publicly traded company, which officially issued the bonds, share of stock and listed on the official stock exchange. In India there are two stock exchanges which are mostly used by the companies to list their shares namely NSE (National Stock Exchange) and BSE (Bombay Stock Exchange).

WHAT IS IPO?

As we all know the IPO are normally issued by the new, small or medium sized firms they don't have to disclose much information about their company as there are few shareholders and investors. The actual participants of the company before the IPO are angel investors and founders. In the process of issuing the

IPO the private company has to sell at least a portion of their business to the public and traded on a stock exchange, this is the reason why IPO is said to be as "going public".

WHY GO PUBLIC?

What would the main reason for a company to go public? So for any new start-ups, small scale or medium sized firms go public for mainly two reasons one is to raise capital from various financial avenues and the other is when a company wants to expand their business. Beside these two reasons the other factors which includes for a company to go public is:

- The very first factor is liquidity, when a company is in need of liquid cash it can be possible when they will trade in the open market
- Convenience in IPO were going public makes it possible to implements few benefits such as employee stock ownership plans, which helps to attract the top talent of the industry
- As long as a company has a high demand in the market due to its quality service and customer satisfaction, a public company can always issue more stocks

WHAT ARE THE FACTORS TO BE INCLUDED BEFORE APPLYING FOR AN IPO?

- Reasonable risk: Risk aspects engaged in the execution of the plan
- Mining data: The historical record of the firm providing the IPO promoters, reliability, and their past records
- Growth: Products offered by the company and their potential going forward

PROCESS OF IPO

1. Underwriting: The underwriting is a process where a middleman helps in raising the money from debt or equity. Since, IPO is done through the process of underwriting, the underwriters plays a vital role between company and public. A deal is negotiated between these two parties
2. Filing with SEBI: After the negotiation of the deal between both the parties, next process will be filing with SEBI. Once the deal gets agreed by the parties, the registration statement has to be filled with SEBI. The statement consists of the company information such as financial statements, management background and legal problems. Later the SEBI goes through the investigation process and approves for it
3. Red herring: It is a prospectus which consists most of the information pertaining to the company's operation. Red herring is a preliminary prospectus filled with Securities and Exchange Commission (SEC) by the company.

RESEARCH QUESTIONNAIRE

1. Will you be ready to own the stock if the prices fall by 40-50%?
2. What percentage of your portfolio would be allocated to IPO investment and what would be your risk tolerance?
3. Are you planning to invest in IPO to 'flip' it (short term strategy) or have plans for staying long term?

OBJECTIVES

1. Repayment of borrowings
2. For general corporate purpose
3. Growth and expansion of the business
4. Accommodation of the working capital

REVIEW OF LITERATURE

Beatty and Ritter (1986)	Balanced under-pricing is ensured by underwriters, for they have reputational capital at stake. IPO managed by highly reputable underwriters, therefore, are less likely to be heavily under-priced.
Titam and Trueman (1986)	Firms with good prospects choose to bring their IPO into market through high-quality auditors and under writers to signal their true value. IPO quality is increasing function of quality of auditor and under writers.
Carter and Manaster (1990)	IPO associated with well-established under writers exhibit lower initial returns.
Barry et al. (1990)	Results show that number of VCs, Size of their ownership and span of board service are negatively correlated with level of under-pricing and therefore presence of VC lead to lower initial return.
Megginson and Weiss (1991)	In an industry and size wise comparison of VC backed and non -VC backed IPO revealed that VC backed IPOs are less under-priced.

Paul A. Gompers (1996)	IPOs of companies backed by less experienced and younger VC firms are more under-priced than those of backed by established VC firms.
Carter, Dark and Singh (1998)	IPO managed by reputed under writer's experience less short-run under-pricing and better long-run performance.
Dewenter, Novaes and Pettwar (2001)	Results support significantly higher under-pricing of Japanese keiretsu group firms IPO than those of independent Japanese firms.
Lee and Wahal (2004)	Over sample study period of 20 years, results show that venture capital backed IPO are more under-priced and hence exhibit greater first day return than IPO without venture capital funding.
Prasad, vozikis and aritff (2006)	Found the existence of higher under-pricing in Malaysia when compared to developing nations. They also concluded that there exists a positive relationship between first day under-pricing and government regulatory intervention.
Goergen, Khurshed and Renneboog (2009)	Euro new markets are heavily under-priced and there is significant difference in under-pricing of German and France Euro new market where the former is more under-priced than latter.
Marisetty and Subrahmanyam (2010)	IPOs that are affiliated to business group, foreign business group and government-affiliated firm experience greater under-pricing than independent firms.
Deb and Marisetty (2010)	IPO grades significantly relies on such firm characteristics as size, business group affiliated and board independence. Large companies affiliated to business group having good number of independent directors on board receive higher grade.
Poornima, Haaji and Deepha (2016)	Observed IPOs can be considered as both long-term investment tool and speculative tool.

RESEARCH METHODOLOGY

Source of study

1. The given information is gathered from web sites, magazines and through newspaper.
2. Books related to Financial Management.
3. Web sites were used as the vital information source.

Advantages

1. One of the main advantages of IPO is having a stronger capital base.
2. It is also beneficial for the business in increasing the other financing prospects.
3. The issuing of IPO or going public for any private company will ultimately increases the company's reputation as well as personal prestige.

LIMITATIONS

1. Time consuming as it is one of the lengthy processes to go public.
2. Filing of an IPO is one of the costly and expensive for any investor as it includes legal fees, accounting fees and printing costs.
3. IPO process is very complex in nature as it requires a lot of members to be included in the process like portfolio managers, brokers, investors, shareholder.

FINDINGS

1. The study is about how the company processes with the capital which has been raised from the public.
2. They have to manage the funding of the capital within their business.

CONCLUSIONS

The IPO is a process where the main aim of the company is to raise the money from the public for the growth and expanding their business. The extra money or excess money from those public borrowings will be used for the development and growth of the business. When the company goes public from private is the process which is said to be as "Public Offering" or "Initial Public Offering" or "Flotation".

The company has to prepare a invitation for the public before issuing the IPO. The invitation which is sent to the public for investing in their company will be in the form of a lengthy document called as "Prospectus". This particular document consists of all the required information and details of the company which includes financial statements, working capital and so on.

Before issuing the IPO in the stock exchange the company has to make a relationship with a middle person who are professional in this field such as tax consultants, risk managers, chartered accountants, etc. They have to negotiate and agree upon a deal between both of them.

Once the deal is agreed by the parties then they are required to fulfil few official formalities to list their company in the stock exchange. After the formalities are performed the SEBI will go through the investigation and approves the company to sell their shares to public.

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