Short run performance of Initial Public offerings: An analysis of IT and Automotive Industry

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Abstract:

Primary market plays a significant role in the development of any economy. Primary market is a place where the company issue shares for the first time to the public. Primary market provides a platform to companies to raise the money for their expansion and to investor to invest their money in stock market. Generally, investors are scared to invest in stock market because of uncertainty regarding the future performance of companies. Investors have to analyze the underpriced and overpriced securities before investing in capital market. This study made an attempt to analyze the initial listing and short run performance of Initial public offerings from IT and Automotive Industry during 1st January 2018 to 31st December 2018. The result found that the IT industry have shown negative returns except in 1month, 2month,3month and Automotive Industry have shown positive return and performed better than the market adjusted excess return.

Key Words: *Initial Public offerings, Capital market, listing, underpriced, overpriced.*

Introduction:

Financial system is a collection of financial markets, financial institutions, laws, regulations and techniques through which financial instruments are traded, interest rates are determined and financial services are produced and delivered around the world. Financial markets play a significant role in the development of economy in general and that of corporate sector in particular. It helps in allocation of scare financial and economic resources. It directs the resources in productive sectors by transferring them from savers to borrowers. Financial market gives impulsion to the savings of the people. Thus, it increases overall investment activities in the country. Financial market is classified as Primary and Secondary market. The primary market is where the company publicly sells new stocks for the first time in the market. Generally in many cases the shares are issued for the first time through prospectus is called Initial Public Offerings. Secondary market is a market where the issued shares are traded in the stock exchange. From investor's point of view, it is essential to analyze the securities (underpriced or overpriced securities) before taking the investment decisions. The objective of the study is to analyze the initial listing and short run performance of Initial public offerings in Indian Capital Market.

Literature Review

Ravichandran (2014) has documented his thesis by analyzing 322 Initial Public offerings based on characteristics such as year wise, offer price, issue size, sector wise, ownership pattern and subscription ratio during 2006-2013 in Sensex and Nifty as well. The researcher has analyzed the initial listing and after market performance of Initial public offerings based on character wise by calculating the market adjusted excess returns with and without initial returns. And also examined the factors determining the listing day performance of Initial Public offerings by using regression in Indian Capital Market in both Sensex and Nifty as well. At the end of the note concluded that the market adjusted excess returns in majority of the cases outer performed compared to market indices. The results explained elaborately on character wise. Sajal Das (2013) analyzed the initial listing performance of initial public offerings by calculating initial returns and also analyzed the short run and ling run performance of Initial public offerings in mega (issue size more than 100 crores) and minor (issue size less than 100 crores) issues during boom and recession period during 2000-2009 by considering 40 Initial Public offerings and found that the 92.5% of IPOs are underpriced. Finally concluded that the performance of IPOs in long run have shown negative returns in mega and minor issues except positive return in first year by mega issues. Mani Jindal (2015) has examined the short and long run performance of Initial public offerings by calculating the market return, market adjusted excess return, standard deviation, beta, Sharpe ratios, treynor ratio and Jensen ratio by considering 108 IPOs during 1999-2014 in national stock exchange. The study found that the short run and long run performance of initial public offerings have shown negative returns. Author has used factor analysis to evaluate the respondent's answers through questionnaire in order to know the investors behavior towards the investment decision in Initial public offerings and found that the investors are irrational towards the investment decisions in Initial public offerings. Seshadev Sahoo and Prabina Rajib (2010) has carried his research to analyze the short run and long run performance of Initial public offerings by using market adjusted abnormal return, wealth relatives and buy and hold returns by considering 92 Initial public offerings during 2002-2006 and found that on an average 46.55% initial public offerings are underpriced. Author analyzed the various factors such as offer size, post issue promoter holding leverage ratio, ex ante uncertainty, subscription rate, and age of the firm influencing the performance of initial public offerings.

Objective

- To analyze the initial listing performance of IPOs in India Capital Market.
- To analyze the short run Performance of IPOs by calculating return Weekly, one month, two month, three month , six months and yearly.

Research Methodology

- **Data Sources:** The secondary data is used for the study such as research publications, journals, thesis, Closing prices of companies are collected from the Bombay Stock Exchange and money control.
- **Sample Size:** The Initial Public offerings are offered during 1st January 2018 to 31st December 2018 is considered for the study. The IT and Automotive Industry are chosen for chosen.
- **Statistical tools Used:** Mean, Standard deviation.
- Methodology

a) Mean: Mean is also known as arithmetic average and is the most commonly used tool to measure the central tendency. It is calculated by the sum of all the given numbers divided by the number of observations.

$$\bar{x} = \Sigma x_i) / n.$$

Where,

$\bar{x}$ = Mean

x_i = the values of the independent variable

n = number of observations

b) **Standard Deviation:** Standard deviation was introduced by Karl Pearson in 1893 widely used tool to measure of dispersion of a set of data from its mean. It measures the absolute variability of a distribution. The formula to calculate the Standard deviation is given by

$$\sigma = \sqrt{\frac{\Sigma (x-\bar{x})^2}{n}}$$

Where,

σ = Standard deviation

$\bar{x}$ = Mean

x = the values of the independent variable

c) **Calculation of Raw Return :** Raw return or Initial Return of each Initial Public offering is calculated by taking the difference between the closing price on the first day of listing and the offer price divided by the offer price

$$RR = (P_1/ P_0) – 1 \ldots\ldots\ldots\ldots\ldots\ldots\ldots\ldots\ldots\ldots\ldots\ldots(1)$$

Where,

RR = Raw Return or Initial return

P_1 = Closing Price on the first day of trading in the stock exchange

P_0 = Offer price

d) **Calculation of Market Return:** Market Return or Index return is calculated based on the Sensex index return is calculated by the difference between the closing value on the first day of Market return and the closing value of the market index on the offer day.

$$MR = (Rm_1/Rm_0) - 1 \ldots\ldots\ldots\ldots\ldots\ldots\ldots\ldots\ldots\ldots\ldots\ldots\ldots .. (2)$$

Where,

MR = Market Return or Index Return

Rm_1 = Closing value on the first day of market return (Sensex)

Rm_0 = Closing value of the market index on the offer day

e) **Calculation of Market Adjusted Excess Return :** Market Adjusted Excess Return refers to the difference between the Raw return and the Market or Index Return.

Market Adjusted Excess Return = Equ(1) - Equ(2)

Market Adjusted Excess Return = Raw return – Market return

I. Initial listing Performance of Initial Public offerings of IT and Automotive Industry

Table 1.1: Showing Initial listing performance of IPO in IT Industry

2018	RR	MAER
Mean	-4.20	-5.28
SD	9.00	8.51
Min	-17.17	-17.63
Max	3.27	0.36
PR	0.25	0.25
NR	0.50	0.5
ZR	0.25	0.25

Analysis: Table 1.1 showing the initial listing performance of Initial public offerings in IT industry by calculating the raw return and market adjusted excess return. The mean return have shown negative return that indicates overpriced that means the closing prices on the listing day is less than the closing prices on offer day. The standard deviation is slightly high in in raw return compared to market adjusted excess return. The maximum return is slightly high compared to market adjusted excess return.

Table 1.2: Showing Initial listing performance of IPO in Automotive Industry

2018	RR	MAER
Mean	4.44	4.73
SD	8.22	9.12
Min	0.00	-5.05
Max	16.76	17.20

PR	0.60	0.60
NR	0.40	0.40
ZR	0.00	0.00

Analysis: Table 1.2 showing the initial listing performance of five Initial public offerings in automotive industry. It is clears that the mean return is positive in both the raw return and market adjusted excess return. The positive return indicates the closing prices on the listing day are greater than the closing price on offer day that refers to underpriced securities. The standard deviation is slightly less volatile compared to market adjusted excess return.

II. Short runs performance of Initial Public offerings of IT and Automotive Industry

Table 2.1: Short run Performance of Initial Public offering in IT Industry

RR						
2018	**1 Week RR**	**1M**	**2M**	**3M**	**6M**	**1Year**
Mean	-4.61	5.80	1.51	5.65	-10.00	-7.73
SD	4.36	18.25	18.71	22.06	20.03	39.41
Min	-8.76	-15.09	-18.52	-22.31	-39.48	-42.19
Max	0.00	21.94	23.61	27.78	3.89	36.67
PR	0	0.5	0.5	0.5	0.5	0.5
NR	0.75	0.5	0.5	0.5	0.5	0.5
ZR	0.25	0	0	0	0	0
MAER						
2018	**1W**	**1M**	**2M**	**3M**	**6M**	**1Year**
Mean	-0.93	0.00	-1.45	2.49	6.23	7.92
SD	4.44	6.21	8.41	5.97	3.14	9.86
Min	-5.15	-5.79	-9.14	-3.09	3.34	-1.90
Max	3.55	5.74	6.04	7.95	10.51	17.16
PR	0.50	0.50	0.50	0.50	1.00	0.75
NR	0.50	0.50	0.50	0.50	0.00	0.25

Analysis: This table showing the short run performance of Initial public offerings in Information Technology Industry. In the year 2018 four companies of IT industry offered shares through Initial Public offerings in Capital Market. The mean return for 1 week, 6 months, and one year shows negative return that indicates that after 1 week, 6 months and 1 year the closing prices are less than the closing prices on the listing day. Whereas 1 month, 2 month and 3 month have shown positive return that means the 1st, 2nd, 3rd month closing prices are greater than the closing prices on the listing day. On an average the short run performance of Initial public offerings have shown 50% of positive and negative returns.

Table 2.2: Short run Performance of Initial Public offering of Automobile Industry

RR						
2018	**1W**	**1M**	**2M**	**3M**	**6M**	**1 Year**
Mean	5.95	3.54	7.82	19.14	10.06	-6.71
SD	11.64	15.57	13.15	49.75	45.70	17.11
Min	-1.86	-15.22	-10.94	-21.79	-30.74	-18.80
Max	25.94	22.93	24.21	103.33	88.54	5.39
PR	0.40	0.40	0.80	0.60	0.40	0.50
NR	0.60	0.60	0.20	0.40	0.60	0.50
MAER						
2018	**1W**	**1M**	**2M**	**3M**	**6M**	**1 Year**
Mean	0.73	2.91	4.76	2.62	2.88	15.97
SD	1.57	2.66	2.97	5.37	6.87	2.09
Min	-1.28	0.10	0.57	-3.59	-4.22	14.49
Max	2.48	5.78	7.27	8.99	11.00	17.44
PR	0.60	1.00	1.00	0.60	0.60	1.00
NR	0.40	0.00	0.00	0.40	0.40	0.00

Analysis:

Table 2.2 showing the short run performance of Initial public offering of five companies in Automobile Industry in 2018. The above table clearly shows that the mean return for 1 week, 1 month, 2month, 3month, 6month shows the positive return that means the closing prices of respective months are greater than the closing prices on the listing day indicates the short run performance of Initial public offerings are performed better than the market adjusted excess returns.

Conclusion:

This study made an attempt to analyze the initial listing performance and short run performance of Initial public offering for the period of 1 week, 1month, 2month,3month,6 month and 1year of It and Automotive industry. The results found that the short run performance of automotive industry has shown positive return except in one year and IT industry shown positive returns only in 1motn, 2month, 3month respectively. The automotive industry performed better than the IT industry.

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