A STUDY ON ISSUE OF SHARES THROUGH INITIAL PUBLIC OFFER (IPO) IN INDIA AND ITS CHALLENGES

CS Prashant Prahladbhai Patel[1]
Assistant Professor, V. T. Poddar Commerce College, Surat
Affiliated to Veer Narmad South Gujarat University, Surat, Gujarat, India
prashantp1086@yahoo.com,

CS Shweta Prahladbhai Patel[2]
Assistant Professor, J. Z. Shah Arts and H. P. Desai Commerce College, Surat
Affiliated to Veer Narmad South Gujarat University, Surat, Gujarat, India
shwetappatel09@yahoo.in

I. ABSTRACT

Initial Public Offer (IPO) plays a role of new blood in the nerves of existing companies as the companies try to raise funds for their approaching ventures through IPO. The study has conducted to analyse challenges and factors affecting the offerings which come out in the primary markets. There are always risks and rewards for the companies which may depend upon certain factors and uniqueness of the companies. In primary market two companies of same sector may get different response of IPO even if they have offered in same time horizon and in same external environment. This main objective was achieved by studying the important factors affecting IPO. The paper concluded that many variables affect the success of companies offering securities to public such as IPO Issue Size and Price Band, Reputation of Key Managerial Personnel, Goodwill of the Companies, Age of the Companies, corporate governance, level of debt or equity, company market share, etc. The study also covers the issues of delay or failure of IPO like Listing Procedure and Documentation, The study also provides the major factors affecting the issuance of shares through IPO such as global meltdown, amendments in the rules and regulations of government policies and acts, volatility of market, Management Related Issues, Substantial Investment in IPO, etc.

Key Words: Initial Public Offer, Factors affecting IPO, Failure of IPO, Issues and Challenges.

II. INTRODUCTION

India is a promising market when it comes to commodity, currency, equity or derivatives. This means that in the coming decade, exchanges engaged in these asset classes will only see higher growth as more and more investors take to investing. Beginning of 2017 has proved to be yet another good year for IPOs as some of the well-known names like Shankara Building Products, D-Mart's parent company, Avenue Supermarts, Hudco, Bombay Stock Exchange (BSE) and Music Broadcast have given remarkable returns to investors on the day of the listing. Among the other companies coming to tap the primary market this year includes India's premier stock exchange; National Stock Exchange, IRCTC Limited, Go Air, Barbeque Nation Hospitality Limited, etc.

III. INITIAL PUBLIC OFFERING

An IPO, or Initial Public Offering, is an invitation to the public to subscribe to a company's share capital. When these needs are large, companies need to approach investors to finance their future fund requirements. In return, investors can expect a share of the company's future profits through dividends, and capital growth through stock price appreciation. The company management is responsible for running the business well, with healthy revenue and profit growth. In turn, this induces more investors to participate in that business by buying the company's shares in the stock market (secondary market). The result: share price appreciation. When investors are highly confident of both the prospects of the company's business and its management's ability to deliver on that potential, the scope for future share price appreciation tends to get factored into the price of the newly-issued shares as soon as they are listed on the stock exchange.

Advantages of Public Issue

- Money non-refundable except in the case of winding up or buy back of shares.
- No financial burden i.e. no fixed rate of interest payable. However, in order to service the equity, dividend may be paid.
- Enhance shareholders' value if the Company performs well.
- Greater Transferability.
- Trading & Listing of securities at stock exchanges.
- Better liquidity of securities.
- Helps building reputation of promoters, Company & its products/services, provided the Company performs well.

Applicable Laws

- Provisions of the Companies Act, 2013.
- Securities Contracts (Regulations) Act, 1956.
- SEBI rules & regulations
- Compliance of Listing Obligations and Disclosure Regulations with the concerned stock exchanges after the listing of securities.
- RBI regulations in case of foreign/NRI equity participation.

Obligations and Public Issue Procedure of the Company:

Pre-Issue Obligations (i.e. before the opening of issue)

- Board Resolution for approving the draft prospectus and related resolutions.
- Shareholders' Resolution pursuant to the Companies Act, 2013.
- Filing form MGT- 14 with ROC for passing special resolution for issuing of shares as above.
- Appointment of intermediaries and entering into MOU with them.
- Due diligence by a merchant banker.
- Submission of all required papers / documents with merchant bankers.
- Preparation of draft prospectus in consultation with merchant banker and submitting the same with SEBI along with the fees & other requirements and submitting the same with stock exchanges as per guidelines.
- Receipt of queries from SEBI / stock exchanges, if any and make changes in prospectus, if required.
- Reply to SEBI/stock exchanges in connection with changes in prospectus.
- Obtaining in-principle approval from stock exchanges.
- File final prospectus with SEBI/Stock Exchanges/ ROC.
- Statutory Advertisements.
- Submission of 1% security deposit with the Regional Stock Exchanges.
- Depositing Promoters' Contribution in the issue in a separate Bank Account.

Post-Issue Obligations (i.e. After the Closure of issue)

- Collection of Application forms and processing the same at the Registrar & Share Transfer Agent in consultation with Merchant Banker.
- Separate Account (Escrow A/c) be opened for the applications received from Public.
- Submitting post issue monitoring report with SEBI from Merchant Banker.
- Basis of allotment in consultation with regional stock exchange.
- Post issue advertisement.
- Dispatch of share certificates/refund orders.
- File form PAS-3, PAS-4 & PAS-5 for return of allotment with ROC.
- Entering in to Listing Obligations and Disclosure Regulations.
- Obtaining permission from Stock Exchanges for listing of securities.
- Commencement of trading of securities.
- Redressal of Investors Grievances.
- Application to SEBI/Stock Exchanges for refund of security deposit.

IV. LITERATURE REVIEWS

Iqbal Thonse Hawaldar1, K.R. Naveen Kumar and T. Mallikarjunappa (2018, Financial Economics, Hawaldar et al., Cogent Economics & Finance) studied, “Pricing and performance of IPOs: Evidence from Indian stock market”, and they analysed that IPOs in India are under-priced based on their performance on the first trading day. Authors advised that the retail investors while investing in IPO shares should consider the fundamentals and prospects of IPO companies rather than the prevailing market sentiments. Otherwise, they will incur loss due to the underperformance of IPOs in the long run.

Dr. H. N. Shivaprasad and Mr. Kallanagouda studied, “IPO Performance and IPO Grading in Indian Markets: An Empirical Study (2008-2012)”, they analysed that IPO grading has an important significance while considering investment alternative and it is found that IPOs which have good fundamentals generated good gains at the time of listing and also good market gain over a period of time in the secondary market where as IPOs with poor fundamentals performed very are poorly in generating return and their prices were also more volatile.

Chauhan Ajay Kumar and Kavidayal B.D (2010) in their paper "Significance of IPO grading in Indian stock market: Empirical evidence" analysed the application of IPO grading on long-term returns liquidity, under-pricing, the P/E ratio and volatility of the companies.

Deb and Marisetty (2010) in their paper "Information content of IPO grading" argue that objective, independent and exogenous certifying mechanism like IPO Grading provides a better opportunity to test the well-established certification hypothesis, especially in the context of emerging markets. Using a sample of 163 Indian IPOs they tested the efficacy of IPO grading.

V. OBJECTIVES

- To identify major factors affecting issue of shares through IPO.
- To know the obstacles faced by Indian Companies in making Initial Public Offer.

VI. RESEARCH METHODOLOGY

The study is based on secondary data which has been collected from various reports published by Bombay Stock Exchange, National Stock Exchange, Securities and Exchange Board of India, Reserve Bank of India, etc. and from the information disseminated by the companies on their own websites. Apart from that various journals, newspapers, Reference Books and other material has been used to get the correct essence of financial data.

VII. CHALLENGES OF INITIAL PUBLIC OFFER IN INDIA

Initial Public Offering is the major component of any corporate world. To start a company, you not only need good financial assistance, you also need proper resources like quality manpower, skilled managers, and the experienced management. People in India have got the misconception that IPO implementation is like a walk in the park. Not quite, IPO is the challenging aspect of any corporate world, because it can decide about the rise and fall of an enterprise in India.

1. Wide Ranging Documentations and Reporting: To be honest, the amount of documentation required for setting up an IPO is too much. This requires a sweet combination of tactical and practical documentations. Any mistake in filing documents required, not matching the expectation laid by Securities and Exchange Board of India (SEBI), can affect company.
2. Management Related Issues: Simply by appointing the directors, managers, CEO, Vice president to the top position, does not resolve issues. Various issues like takeovers, ousters, infighting will definitely come up. As the owner of the company, you will need to resolve these issues with iron hand.
3. New responsibilities and restrictions for the management: The IPO process, as well as the on-going responsibilities that arise from the new public status, require substantial amounts of the executives' time that otherwise might have been spent on the operational business. The directors and executives of a public company also face certain restrictions, for example related to dealings with the company

shares and disclosures of the market-sensitive information. Hence the activities of the directors and top management of public companies are more regulated and require additional attention.

4. Substantial Investment in IPO: Companies in India need to plan in advance, before investing in an IPO. Executives, managers and Board of Directors need to invest their time and money in a logical fashion.
5. Interest of Minority Investors Must be Taken: Investors are the heart of any organization small and big in India. Opinions and feedbacks given by the shareholders must be given top priority. Company can achieve its short term operational goals in a systematic manner, at the expense of its vision, when investor's feedback is given importance.
6. Pressure: Various performance pressures are associated with companies in India. All details of the company are shared with people, and hence it is ordinary to experience pressure in sales, operations and financial fields. Tight deadlines are met relating to company operations by sending in the weekly and monthly, quarterly and yearly reports.
7. Extensive public disclosure requirements: It can be an extensive and labour intensive process. It may invite scrutiny, may effectively reduce management flexibility and may disadvantage the company by providing valuable information to competitors, suppliers, customers and business partners.
8. Significant increase in capital and human resource costs.
9. More complex corporate governance structure and regulations: It may demand more time and attention of the management and other top level executives.
10. Stringent eligibility and compliance norms.
11. Risk of takeover bids: Risk of hostile takeover bids, which is increased when the insiders' ownership percentage is decreased by the IPO and large portions of the company's stock can be exchanged in market.
12. To identify what risks and obligations are attached to the Company's Contract and leases.
13. Others Factors such as:
    - Government Stability
    - Implementation of policies
    - Volatility of Stock Markets
    - Global Meltdown
    - Fiscal Policies
    - Financial Literacy
    - Goodwill
    - Due Diligence Procedures
    - FEMA Regulations
    - Listing Obligations and Disclosure Requirements
    - SEBI Regulations
    - SCRA Compliances
    - Corporate Governance Standards
    - Role of Intermediaries
    - Merchant Bankers, Registrar to the issue, Depositories, Underwriters, etc.

VIII. CONCLUSIONS AND RECOMMENDATIONS

Our study shows that there are procedural hurdles in putting up an IPO. As the statutory requirements are highly exhaustive, it is difficult to interpret the requirements in true sense. Thus there for logical and cohesive understanding is highly required. The role played by Merchant Banker can make or break the entire IPO issue. Thus, matching up with the regulatory requirements is the basic hurdle in making an IPO. There are also other factors beyond the control of the issuer in addition to the regulatory environment such as global market situations, the local market sentiment, political environment prevailing in the country, government's outlook towards the industry. It comes to know from this study that among other factors affecting the issue of shares through IPO, there are some major factors affecting the making of an IPO that includes volatility of market, global meltdown, goodwill, merchant bankers, amendments in the statues and government stability which together constitutes a very high percentage in affecting the issuance of shares through Initial Public Offer (IPO). Company should examine each significant factor affecting IPO to get the best returns out of it.

References

(*PROCESSING STATUS OF DRAFT OFFER DOCUMENTS FILED WITH SEBI* . (2017, September 01). Retrieved from Securities and Exchange Board of India: https://www.sebi.gov.in/sebi_data/commondocs/sep-2017/processingdraftsep012017_p.pdf

Live / Forthcoming Issues. (2018). Retrieved from Bombay Stock Exchange: https://www.bseindia.com/markets/PublicIssues/IPOIssues_new.aspx?id=1&Type=p

Adams Michael, B. G. (2008). IPO PRICING PHENOMENA: EVIDENCE OF BEHAVIOURAL BASES. *Journal of Business and Economics Research, Vol no 6*.

Agarwalla, S. K. (n.d.). Mandatory IPO Grading: Does It Help Pricing Efficiency? *IIM Ahmedabad- Research & Publications*, Deccember 2012.

Gemalez, A. a. (2001). SPANISH PUBLIC OFFERING FOR THE PERIOD 1987-1997.

Iqbal Thonse Hawaldar, K. N. (2018). Pricing and performance of IPOs: Evidence from Indian stock market. *Cogent Economics & Finance*.

Kallanagouda, D. H. (n.d.). IPO Performance and IPO Grading in Indian Markets: An Empirical Study (2008-2012).

Marisetty, D. a. (2010). " Information content of IPO grading".

National Stock Exchange India. (n.d.). Retrieved from https://nse-india.com/products/content/equities/ipos/historical_ipo.htm

RBI. (n.d.). *Issue and Pricing of Shares by Private Sector Banks*. Retrieved 2018, from https://rbi.org.in/Scripts/BS_CircularIndexDisplay.aspx?Id=5609

Sabarinathan, G. (Deccember, 2010). Attributes of Companies Making IPOs in India - Some Observations. *IIM Bangalore Research*.