

# CORPORATE GOVERNANCE AND IPO UNDERPRICING

Lalit Bhalla\*, Akshay Bhatia\*\*, Vijay Kaushal\*\*\*

**Abstract** *Corporate Governance influence the companies to manage their organization in such a way to achieve the long term strategic goals to satisfy the shareholders, creditors, employees, customers, suppliers, and complying with the legal and monitoring requirements, apart from meeting environmental and local community needs. Corporate Governance is administered to provide the maximum benefits to the stakeholders.*

*The evaluation on the basis of its listing and its returns, describes the customary valuation of such IPO. There is always an impact of the edifice of the management on the pricing of IPOs, the status of directors also affect its pricing structure. It also depends upon the policies, norms and legislative structure of the management.*

*This is a pragmatic study that examines the pricing of IPOs and the initial performance of such IPOs in Indian capital market. It also describes the impact of corporate governance on pricing of Initial Public Offers, and also outlines the relationship between corporate governance and underpricing of IPOs.*

**Keywords:** *Corporate Governance, IPO, Underpricing.*

## INTRODUCTION

Indian capital market is one of the oldest capital markets of Asia. Even the IPOs have their existence from the historical era but IPO market in India has been developing since the transformation of Indian economic structure after the economic reforms in the form of liberalization of the Indian economy. IPO has become one of the most preferred methods of raising funds for various new companies and existing companies. The IPO market in India is growing as a large number of companies are issuing equity shares in the capital market. Since 1990 reforms, the Indian IPO market went through a dynamic phase of policy changes, reforms and streamlining.

Among these reforms and transforms, one of the most significant developments was the substitution of Controller of Capital Issues (CCI) by a free pricing mechanism. CCI had the regulatory control on all capital issues in Indian market. CCI was the authority which actually cleared the issue price set as the offer price of such issue. The CCI's formula was used to compute the fair price of equity in the light of accounting information. This resulted into extreme underpricing & heavy over subscription in maximum of the cases. This step assisted the Indian IPO market to move to the free pricing. The free pricing mechanism allowed the companies to raise funds from the capital market at competitive price. It actually makes the companies independent to evaluate the

issue and to price it accordingly for the market which makes the issue more attractive and beneficial to investors as well as the companies.

In 1992, Securities & Exchange Board of India (SEBI) was established to regulate the capital market and to provide a governed environment for the Indian capital market. SEBI was given the authority of monitoring and regulating the activities of the companies, bankers, lead managers to the issue, stockbrokers and other mediators to the stock market. The newly created regulatory agency governing financial markets, the Securities and Exchanges Board of India (SEBI), then took up the role of inspection of potential and facts for public offerings with an eye to ensuring truthful information disclosure in the prospectus.

With the abolition of the CCI, firms were then free to price issues as they perceived. The number of public issues taking place per month has gone up sharply in the period following the abolition of the CCI, and the role of debt in financing projects has diminished. However, the post-CCI period is also characterized by extremely high levels of underpricing by world standards.

In India, the primary market is unique by world standards in many ways as it has been shaped by an unusual history of regulation, the institutional details of how IPOs take place are singular, the sheer size and scope of the primary market is enormous and the large scale direct participation in the primary market by millions of retail investors is unlike that

\*Assistant Professor, Management Department, Lovely professional University, Punjab

\*\*Student, MBA(Honours), Department of Management, Lovely Professional University, Punjab

\*\*\*Professor, ICDEOL, Department of Commerce and Management, HP University, Shimla

in any other country in the world. The Indian IPO market experienced different conditions in different phases. The market got a real boom in early 90s whereas it was halted by the Asian crisis as well during the late 90s. Many scams in Indian capital market also affected the echelon of IPOs.

The recent global slowdown also impacted the Indian IPO market as many of the firms delayed their issues to protect their IPO to expose to a high risk of failure due to hesitant investors. Even many of the Institutions were dragging their money back from the capital market which resulted into an awful era of capital market in India.

Corporate governance has emerged as an important field of research and concern for finance discipline as well as management of the markets from last decade. It has become a central issue in developing countries for the effect of financial crisis in developed global market in 2008. Corporate governance influence the companies to manage their organization in such a way to achieve the long term strategic goals to satisfy the shareholders, creditors, employees, customers, suppliers, and complying with the legal and monitoring requirements, apart from meeting environmental and local community needs. We can also say that corporate governance is administered to provide the maximum benefits to the stakeholders.

The existence of Underpricing in Indian capital market has already been supported by many researchers. Ghosh S. (2004) also described the existence of Underpricing of IPOs in Indian capital market by taking 1842 companies that got listed on the Bombay Stock Exchange (BSE) between the periods from 1993 to 2001.

Predicting the movement of share on the initial days of trading is not unproblematic because there is often little chronological data with which to analyze the company. Also, most IPOs are of companies going through a transitory growth period, which are subject to additional uncertainty regarding their future values. The evaluation on the basis of its listing and its future period returns, describes the customary valuation of such IPO. The study also distinguishes the structures of IPOs in India in which the management expects a huge listing returns from such IPO and it affects the pricing of such IPOs in the hands of the company which results into overpricing. There is always an impact of the edifice of the management on the pricing of IPOs, the status of directors also affect its pricing structure. It also depends upon the policies, norms and legislative structure of the management.

The underpricing of IPO is one of the most widely studied experiential phenomenons in the financial literature. Underpricing is defined as the proportionate difference between the offering price and the price at which the shares consequently trade in the secondary market. Underwriters take many factors into consideration when pricing an IPO, and attempt to reach an offering price that is low enough

to stimulate interest in the stock, but high enough to raise an adequate amount of capital for the company. The process of formatting an optimal price usually involves the underwriters arranging share purchase commitments from leading institutional investors.

To the best of the researchers' knowledge this is probably the first study in the context of underpricing of IPOs & corporate governance in India. A large number of studies have been published regarding underpricing of IPOs and on the role of corporate governance in emerging markets. This study is aimed at examining the pricing of IPOs in Indian capital market. It also describes the impact of corporate governance on pricing of Initial Public Offers and outlines the relationship between underpricing of IPOs & Corporate Governance.

## REVIEW OF LITERATURE

Review of literature constitutes an important section in any research study, which provides a critical overview of various dimensions of any subject, which have been explored over different time frames and it helps us to identify the gaps in the literature, which motivates for further research in the area so that such gaps in literature can be plugged. The following discussion is an attempt to provide an overview regarding different dimensions of an IPO that have been critically examined on the basis of short run performance in the market and to substantiate the relationship of corporate governance with any Initial Public Offer.

Literature review has been organized in two parts. Part A reviews different studies that examined the short run price performance of IPO stocks or related to under pricing of IPOs and Part B converses the studies performed to examine the impact of corporate governance on the company's functioning and policy formulation. After such categorized study of such components, it would be unproblematic to comprehend the essentials of the major components of the study, by which a significant relationship can be established.

### Underpricing of IPOs

Habib and Ljungqvist (2001) generalize the notion that issuers have an incentive to reduce underpricing, and model their optimal behavior. They argue that if issuers can take costly actions that reduce underpricing, they will do so up to the point where the marginal cost of reducing underpricing further just equals the marginal benefit. This marginal benefit is not measured by underpricing itself, but by the reduction in the issuer's wealth loss that underpricing implies.

Loughran and Ritter (2004) also provided some facts that banks have strategically underprice the IPOs, in an effort to

enrich themselves or their investment clients. Another fact in the study is that the top banks have lowered their criteria for selecting IPOs to underwrite, resulting in a higher average risk profile for their IPOs which certainly require making them heavily underpriced.

Ritter et al (2006) found that the underpricing of IPOs in Denmark is only 5 percent for a period of 14 years beginning from 1984, while in China for a period of 10 years from 1990, the underpricing was found to be more than 250 percent.

Engelen (2007) presented an empirical study on a country level, the impact of investor protection on the growth of capital market & the long run expansion. They found that Countries where investor protection is strong, gives an advantage to the companies in comparison to the countries where investor protection is not so strong in terms of cost to the public.

Tian & Megginson (2007) suggested that investment risks in China's primary markets are greater than in other new issues markets and these risks partly explains the extreme levels of Chinese IPO underpricing. However, the principal cause of this underpricing is government regulation. The supply restricting measures traditionally adopted by the Chinese regulatory authorities turn IPO shares into hot commodities, which are fiercely bid for, and this leads to corruption and a reallocation of wealth from firms and investors to politically connected individuals and groups.

Coakley, Hadass & Wood (2009) analyzed the nature and factors of short run underpricing for such IPOs which have been issued during 1985-2003 on London Stock Exchange, counted to be 591. They also state the significant difference between the 1998-2000 bubble year and rest of the taken samples. They also state that the venture capitalist and reputable underwriters played a significant role for the rest of the samples except the bubble years. The combination of venture capitalist and prestigious underwriters was highly associated with the highest underpricing witnessed during 1998-2000.

Deb & Marisetty (2010) discussed that in the year 2007, Indian capital market regulator-SEBI, introduced a unique certification mechanism for IPOs whereby all IPOs have to undergo mandatory quality grading by independent rating agencies. In this paper they argue that such objective, independent and exogenous certifying mechanism provides a better opportunity to test the well established certification hypothesis, especially in the context of emerging markets with institutional voids. They mentioned that grading decreases *IPO* underpricing and positively influence demand of retail investors using a sample of 163 Indian companies. Grading reduces secondary market risk and improves liquidity.

## Corporate Governance & Under-Pricing of IPO

Jenson (1986) described that at the company level, good corporate governance assures the optimal use of firm's capital. It also mentioned that the top management with free cash flows invested in over diversification, which often resulted into organizational inefficiencies. This problem is more likely to happen when there are weak corporate governance mechanisms.

Byrd and Hickman (1992) found that the abnormal bidder returns on the date of takeover bid announcements are significantly higher when the board's decision is likely to have been made by independent directors instead of related directors. This also suggests that the market believes that independent/outside directors dominated boards are more likely to act in the best interest of the shareholders.

Pandya (1992) examined that SEBI's efforts in the direction of investors' protection as a regulatory and development body of capital market are varied and unlimited. The measures taken by SEBI mainly taps measures for apportion efficiency in the primary market where IPOs exist, with fair degree of transparency, reforms in the secondary market for making it transparent and visible which would provide the primary market a strong base for its effective trading, and mainly the focus is onto the protection of the investing public.

Cremens & Nair (2005) have verified that the effective corporate governance relies on both internal and external mechanisms and that they are strong complements. Corporate governance of a firm can't be judged by its external edifice, it also have many of the internal facts, policies and structures which make a firm stand to the corporate governance ratings.

Committee on Corporate Governance, SEBI (2003) stated the mandatory suggestions focus on strengthening the responsibilities of audit committees, improving the quality of financial disclosures, including those related to related party dealings and proceeds from initial public offerings; requiring corporate executive boards to assess and disclose business risks in the annual reports of companies; introducing responsibilities on boards to adopt formal codes of conduct; the position of nominee directors; and stock holder approval and improved disclosures relating to compensation paid to non-executive directors.<sup>11</sup> The Committee believes that these recommendations represent certain standards of 'good' governance into specific requirements, since certain corporate responsibilities are too important to be left to lose concepts of fiduciary responsibility.

Yeh & Shu (2004) scrutinized that the negotiation of the offering price is strictly dictated by the soundness of corporate

<sup>11</sup> [www.sebi.gov.in/commreport/corpgov.pdf](http://www.sebi.gov.in/commreport/corpgov.pdf) (viewed on 14/11/2010)(viewed on 14/11/2010)

governance structure of the IPO firm. Their empirical results from 218 Taiwanese IPO firms for a decade are generally consistent with the positive incentive effect and negative entrenchment effect. They judge that the outcome is the result of repetitive negotiations that involve different interest parties, namely the controlling shareholder of issuing firm, underwriter, and outside investors. Corporate governance variables serve the nexus that integrates the underlying hypotheses in illustration of the willingness and motivation of the controlling shareholder, the acceptance and allowance of the underwriter, and the informativeness of the provided accounting data.

Ljungqvist (2005) found that institutional structure affects the underpricing of IPOs in different nations. A new dimension was brought forward by this study that underpricing is less in case of companies in developed markets as compared to the companies in less developed markets.

Hazem, Charles & David (2006) describes that after controlling other influences, an increase in overall capital market governance in a country is linked to a decrease in the cost of equity, an increase in market liquidity, and an increase in pricing efficiency. Specifically, improved security laws are associated with decreased cost of capital, higher trading volume, greater market depth, lower price synchronicity, and reduced IPO underpricing. These results hold for the overall CMG index, and are directionally consistent for each of the three individual CMG components, are cost of capital (both realized and implied), market liquidity (i.e., trading volume and market depth) and pricing efficiency (i.e., stock price synchronicity and IPO underpricing).

Bedard & Coulombe (2007) contributed to the debate surrounding the effectiveness of governance practices by examining IPO firms' decision to voluntarily create an audit committee, and the effect of governance characteristics on the quality of disclosure as measured by management forecast errors and on the cost of capital as measured by IPO underpricing. Their results seem to indicate that the creation of an audit committee is more likely when the board of directors is larger, a higher proportion of its members are independent and it is not chaired by the firm's CEO. Governance characteristics do not seem to affect the quality of financial information issued by IPO firms.

Boulton, Smart & Zutter (2007) suggested that IPO initial returns are greater in countries offering stronger protections to investors. These results hold for various country-level proxies of governance and are both economically and statistically significant. In those nations, that offer lower levels of investor protection, underpricing is less likely to be used as an instrument to limit legal liability or to maintain control because managerial control is implicit due to a general disregard for investor's rights, leading to lower initial returns (on average) in these countries.

Larry (2009) mentioned that the ownership edifice has a bearing on corporate governance, legal units as well as foreign ownership have an influence on long run performance. It also mentioned that the outside directors and the issue stock exchange have no significance influence. Those firms which are having high growth potential and huge base are considered more highly by the market.

Boulton, Smart & Zutter (2010) described that underpricing is a cost that is paid to maintain the control by insiders in countries with legal systems. They reported negative relation between underpricing and post-IPO outside block holdings but a positive association with private control benefits.

Hearn (2010) findings suggest that the establishment of independent audit and remuneration committees to monitor directors and insiders is at best superfluous with their presence actually increasing levels of asymmetric information and underpricing. However the separation of the roles of CEO and Chairman and the founder-entrepreneur ceding control of CEO role are beneficial mechanisms in signaling quality to potential outside investors.

## DATA COLLECTION AND RESEARCH METHODOLOGY

All the Initial Public Offers have been selected to achieve the above written objectives. The sample firms are selected on the basis of the following criteria:

- (i) The data has been taken for two financial years, viz from 1st April, 2008 to 31st March, 2010.
- (ii) The stock listing on Bombay Stock Exchange (BSE) must have the status of an IPO which means that the firm should not have already been listed on any other stock exchange of India for example National Stock Exchange is another stock exchange. If any company is already listed on such exchange, that would be excluded from the study sample.
- (iii) The initial public offering is of common stock,
- (iv) Only those issues will be considered which were issued on the basis of Book-Building process.

For the purpose of collection of data, the official website of Bombay Stock Exchange ([www.bseindia.com](http://www.bseindia.com)) and other data from Capitaline database has been used. In order to make an analysis of such data, descriptive analysis and regression analysis are used. All possible efforts have been made to use different relationships and techniques, which have employed by different researchers in their studies and accepted as most appropriate for the study.

There are 44 companies which have issued their Initial Public Offers in the form of equity stock during the above mentioned period of two years i.e. from 1<sup>st</sup> April, 2008 to 31<sup>st</sup> March, 2010 and listed on Bombay Stock Exchange (BSE).

**Table 1:** Components of Corporate Governance

	COMPONENTS	SCORING	DESCRIPTION
1	Size of Board of Directors	(9 - 12)    (5-8)    (3-4)	Optimum size of Board of Directors leads to effectiveness in decisions. Limit is between 3 to 12 directors in public companies.
		(3)    (2)    (1)	
2	Percentage of Independent Directors in Composition Of Directors	% (50-59/60-69/70-79/80-89/90-99/100)	According to guidelines, 50% of BOD should be Independent Directors.
		(2/4/6/8/10/12)	
3	Chairman of Remuneration Committee	Independent/Regular	Chairman of the committee having the status of independent director weighs more points for corporate governance standards.
		2 / 0	
4	Composition of Remuneration Committee	Independent/Regular	Remuneration committee composed of Independent directors reflects more transparency.
		2 / 0	
5	Chairman of Audit Committee	Independent/Regular	Chairman of the committee having the status of independent director weighs more points for corporate governance standards.
		1 / 0	
6	Composition of Audit Committee	Independent/Regular	Audit committee composed of Independent directors reflects more transparency.
		1 / 0	
7	Chairman of Investor's Grievances Committee	Independent/Regular	Chairman of the committee having the status of independent director weighs more points for corporate governance standards.
		1 / 0	
8	Composition of Investor's Grievances Committee	Independent/Regular	Investor's Grievances committee composed of Independent directors reflects more transparency.
		1 / 0	
9	IPO Grading	"Grade < 3"=0, "=3" =1, "4" =2, "5" =3	Grading range from 1 to 5
			1-Poor fundamentals to 5-Strong Fundamentals
10	Risk Management Policy	Y/N	Risk Identification, minimization, optimization are the part of risk management policy
		1 / 0	

Source: Author's calculation

All these issues were priced on the basis of Book-Building method process.

Data collection of these companies comprised of the following elements-

- Issue price of each company's equity stock decided on the basis of book- building process,
- Listing Price of each company's equity stock i.e. the open price of the stock in the secondary market/ stock exchange on the very first day of its listing.
- The Final draft of the Prospectus of each issues have been collected which is mandatorily drafted for issue of shares.

The sample for the study is comprised of 44 companies having their Initial Public Offerings in India During 2008 to 2010. The initial selection of IPO securities during this period was obtained from Bombay Stock Exchange (BSE) website. Some samples were expelled from the study due to incomplete information on the official website of the BSE, to comprise the study of reliable facts; relying on any other source of information was not substantiated for the study so the sample companies are limited to 44 issues.

An IPO is 'underpriced' when the offering price at which the firm issues its stock is meaningfully lower than the stock's price at its listing at first day of trading. The amount of underpricing is measured by a stock's 'initial return' which

**Table 2:** Listing Returns of Companies' IPOs

Sr. No	Company	Issue Price	Listing Price	Listing Returns %
1	20 Microns	55.00	50.00	-9.1%
2	Adani Power	100.00	105.00	5.0%
3	Aishwarya Tele.	35.00	50.10	43.1%
4	Alkali Metals	103.00	90.00	-12.6%
5	Anu's Lab.	210.00	260.00	23.8%
6	Aqua Logistics	220.00	219.40	-0.3%
7	Archidply Inds.	74.00	74.55	0.7%
8	ARSS Infra	450.00	640.00	42.2%
9	Birla Cotsyn	14.00	1.23	-91.2%
10	Cox & Kings	330.00	304.10	-7.8%
11	D B Corp	212.00	250.00	17.9%
12	D B Realty	468.00	430.00	-8.1%
13	DQ Entertain.	80.00	135.00	68.8%
14	Edserv Softsys.	60.00	55.00	-8.3%
15	Excel Infoways	85.00	93.05	9.5%
16	First Winner	125.00	125.00	0.0%
17	Godrej Propert.	510.00	510.00	0.0%
18	Gokul Refoils	195.00	203.45	4.3%
19	IL&FS Transport	258.00	287.00	11.2%
20	Indiabulls Power	45.00	44.95	-0.1%
21	Intrasoft Tech.	145.00	140.00	-3.4%
22	Jindal Cotex Ltd	75.00	75.00	0.0%
23	JSW Energy	100.00	102.00	2.0%
24	Jubilant Food.	145.00	161.60	11.4%
25	Kiri Dyes Chem.	150.00	151.00	0.7%
26	KSK Energy Ven.	240.00	220.00	-8.3%
27	Lotus Eye Care	38.00	35.00	-7.9%
28	Man Infra	252.00	335.00	32.9%
29	MBL Infracst	180.00	190.00	5.6%
30	NHPC Ltd	36.00	39.00	8.3%
31	Niraj Cement	190.00	185.00	-2.6%
32	Nu Tek India	192.00	201.10	4.7%
33	Oil India	1050.00	1019.00	-3.0%
34	Persistent Sys	310.00	400.00	29.0%
35	Pipavav Shipyard	58.00	60.05	3.5%
36	Pradip Overseas	110.00	120.00	9.1%
37	Raj Oil Mills	120.00	125.05	4.2%
38	Resurgere Mines	270.00	272.05	0.8%
39	Rishabhdev Techn	33.00	42.00	27.3%
40	Sezal Glass	115.00	110.00	-4.3%
41	Shree Gan.Jew.	260.00	258.85	-0.4%
42	Syncom Health	75.00	88.00	17.3%
43	Texmo Pipes	90.00	101.50	12.8%
44	United Bank (I)	66.00	77.00	16.7%

Source: Author's calculation

**Table 3:** Descriptive Statistics

	Minimum Listing Return	Maximum Listing Return	Average Listing Return	Std. Deviation
PRICING	- 91.21	68.75	5.5759	22.03152

is defined as the percent change between the offering price and the listing price.

The Underpricing of the selected stocks has been calculated by the following formula:

$$\text{LISTING RETURN} = \left\{ \frac{\text{LISTING PRICE} - \text{ISSUE PRICE}}{\text{ISSUE PRICE}} * 100 \right\}$$

For second objective of establishing the relationship between underpricing of IPOs and corporate governance, quantification of corporate governance of the related companies is necessary. Different components have been taken in this study to make the qualitative facts measurable in terms of a common score, by taking significant factors of corporate governance. These components of corporate governance are basically the specifications mentioned by the Ministry of Corporate Affairs<sup>2</sup> and SEBI<sup>3</sup>.

Source: Author's Formation

These corporate governance components are used for computing the CG scores. Description regarding each component has also mentioned in the table. Then listing returns have been compared with the Corporate Governance score of the companies with the usage of regression model, the relationship between these factors leads to the completion of the objective of the study.

## UNDERPRICING OF IPO

The collected data has been computed to know the listing returns of the selected sample. Table II describes the listing returns of the companies included in the study. The result comes out to be highly skewed.

During the selected period of two years (2008-09 & 2009-10), some stocks' listing returns are absolutely upto the mark. Table II indicates that the highest listing return is around 69 % or it can be said that the highest underpriced issue was underpriced by 69%. Many of the companies also have negative listing returns. The highest that a stock had lost at its listing was by 91% as shown in Table II. This is also supported by the standard deviation of the listing returns which is much high at 22.03 %.

During this period, the Indian IPO market got underpriced by 5.58 %, like if a person has subscribed 100 shares of Re.

1 each of ABC co. with total investment of Rs. 100, then on listing of that security in stock market it comes out with the return of Rs. 5.58 with total net worth of Rs. 105.58 of his investment. There is a huge variation in listing gains i.e from -91.21% to 68.75% (refer Table III), with a significant standard deviation of 22.03152, exhibiting disparity in listing gains and showing a large uncertainty factor involved in listing.

Even the percentage of underpricing in this period was not much high but still among the sample of IPOs, around two third were underpriced where as only one third got overpriced or gave negative returns on their listing as illustrated in Table IV.

**Table 4:** Proportion of Underpricing & Overpricing

Total No. of Companies	44	100%
Underpricing in companies	29	66%
Overpricing in companies	15	34

In this study one more fact has been verified that the economic conditions of that particular period also have huge impact on the underpricing of IPOs in Indian Market. Table V describes that in year 2008-09, when the global slowdown was affecting each and every economy of the world in one way or the other, the Indian IPO market was also affected badly by giving negative returns on its listing. Whereas in recovery phase, the underpricing was higher than its average for 2 years and for that particular year of 2009-10, the Indian IPO market was underpriced by 11.1%.

**Table 5:** Underpricing in Different Years

Underpricing in 2008-09	-4.1%
Underpricing in 2009-10	11.1%

## CORPORATE GOVERNANCE & UNDERPRICING OF IPOs IN INDIA

The scorecard designed in this study assisted to shed some light on how well the governance mechanism was adopted by the public companies. The quantified data related to the corporate governance of the companies have been shown in Table VI. The level of pricing/ listing returns has also been presented in Table VI with comparison to the Corporate Governance Score of such Indian Companies.

<sup>2</sup> Ministry of Corporate Affairs - Corporate Governance Voluntary Guidelines 2009

<sup>3</sup> Report of the SEBI Committee on Corporate Governance

**Table 6:** Corporate Governance Score & Listing returns

Sr. No	Companies	Corporate Governance Score	Listing Returns %
1	20 Microns	8.00	-9.09%
2	Adani Power	10.00	5.00%
3	Aishwarya Tele.	7.00	43.14%
4	Alkali Metals	8.00	-12.62%
5	Anu's Lab.	7.00	23.81%
6	Aqua Logistics	12.00	-0.27%
7	Archidply Inds.	11.00	0.74%
8	ARSS Infra	9.00	42.22%
9	Birla Cotsyn	8.00	-91.21%
10	Cox & Kings	10.00	-7.85%
11	D B Corp	10.00	17.92%
12	D B Realty	9.00	-8.12%
13	DQ Entertain.	11.00	68.75%
14	Edserv Softsys.	11.00	-8.33%
15	Excel Infoways	11.00	9.47%
16	First Winner	12.00	0.00%
17	Godrej Propert.	13.00	0.00%
18	Gokul Refoils	11.00	4.33%
19	IL&FS Transport	8.00	11.24%
20	Indiabulls Power	10.00	-0.11%
21	Intrasoft Tech.	13.00	-3.45%
22	Jindal Cotex Ltd	12.00	0.00%
23	JSW Energy	10.00	2.00%
24	Jubilant Food.	7.00	11.45%
25	Kiri Dyes Chem.	10.00	0.67%
26	KSK Energy Ven.	10.00	-8.33%
27	Lotus Eye Care	10.00	-7.89%
28	Man Infra	7.00	32.94%
29	MBL Infracst	10.00	5.56%
30	NHPC Ltd	9.00	8.33%
31	Niraj Cement	6.00	-2.63%
32	Nu Tek India	9.00	4.74%
33	Oil India	11.00	-2.95%
34	Persistent Sys	10.00	29.03%
35	Pipavav Shipyard	9.00	3.53%
36	Pradip Overseas	10.00	9.09%
37	Raj Oil Mills	12.00	4.21%
38	Resurgere Mines	6.00	0.76%
39	Rishabhdev Techn	11.00	27.27%
40	Sezal Glass	11.00	-4.35%
41	Shree Gan.Jew.	9.00	-0.44%
42	Syncom Health	10.00	17.33%
43	Texmo Pipes	13.00	12.78%
44	United Bank (I)	7.00	16.67%

Source: Author's Calculation

**Table 7: Anova Results**

R		R Square	Adjusted R Square		Std. Error of the Estimate	
.015a		.000	-.024		22.28984	
a. Predictors: (Constant), Corporate Governance Score						
ANOVA <sup>b</sup>						
Model		Sum of Squares	df	Mean Square	F	Sig.
1	Regression	4.515	1	4.515	.009	.925a
	Residual	20867.161	42	496.837		
	Total	20871.677	43			
a. Predictors: (Constant), Corporate Governance Score						
b. Dependent Variable: Pricing						

Source: Author's Calculation

The data shown in Table VI is used to signify the relationship between these two variables, corporate governance and IPO underpricing. Causal relationship between corporate governance and IPO underpricing, in context of Indian IPO market, is almost non-existent. A cause and effect relationship between IPO pricing as dependent variable and score in corporate governance as independent variable shows insignificant model. F-value at 0.009 with p-value of 0.925 are favoring the rejection of null-hypothesis.  $R^2$ , measure of goodness of fit with 0.000 value reiterating that no causal relation exists between corporate governance and IPO pricing.

Thus to a certain extent it is proved that no matter how good a company is on corporate governance, listing gains are independent of it, which further implies that listing gains happens on factors other than corporate governance in Indian IPO market.

## FINDINGS & CONCLUSION

The overall result of the study shows that in Indian IPO market, the concept of underpricing exists. Even in the unfavorable economic conditions the Indian market reacted negatively upto a certain extent but showed a positive quick growth in the form of underpricing of IPOs in the recovery period of the economy.

The study also signifies the non dependency of Underpricing of IPOs in Indian Capital Market on the Corporate Governance mechanism of the companies. This also indicates that even in many of the developed countries the corporate governance reforms and practices have a positive impact on underpricing of IPO but in India it still requires a long way to find such relationship.

The SEBI Committee on corporate Governance headed by N.R. Narayana Murthy<sup>4</sup> illustrated that in India, the existence

of corporate governance mechanism is still not strong and maximum of investors are not aware about such elements of corporate performance and accountability and it would take a long time to create a strapping base of Corporate Governance as a parameter for company's assessment in India. This fact also support the result of this study that in present scenario corporate governance is not a perceived parameter for a company's performance or worth for investors in India.

There might be other factors on which the underpricing of IPO depends and the investors consider those factors for selecting a stock to subscribe like age of the company, reputation of the company, size of the issue and mainly the sentiments of the market.

These results will form the base for further evolution of the factors which affect edifice of Underpricing of IPOs in Indian capital market and also for insurrection of Corporate Governance in consonance with the rapidly changing economic and industrial environment of the country.

## REFERENCES

- Agrawal, D. (2006). IPO Pricing- Book Building and Efficient Pricing Methodology. Retrieved 2010, November 16 from <http://ssrn.com/abstract=1311749orhttp://dx.doi.org/10.2139/ssrn.1311749>
- Bedard, J. & Coulombe, D. (2007). Corporate Governance, Disclosure Quality and the Underpricing of IPOs. Retrieved 2010, November 18 from [http://neumann.hec.ca/cgj/Textes%20des%20chercheurs/Conf\\_Courteau.pdf](http://neumann.hec.ca/cgj/Textes%20des%20chercheurs/Conf_Courteau.pdf)
- Boulton, T. J., Smart, S. B. & Zutter, C. (2010). IPO Underpricing & International Corporate Governance. *Journal of International Business Studies*, 41(2), pp. 206 - 222.
- Byrd, J. & Hickman, K. (1992). Do Outside Directors monitor managers? Evidence from Tender Offer Bids. *Journal of Financial Economics*, 32(2), pp. 195 - 221.

<sup>4</sup> [www.sebi.gov.in/commreport/corpgov.pdf](http://www.sebi.gov.in/commreport/corpgov.pdf) (viewed on 14/02/2011)

- Coakley, J., Hadass, L. & Wood, A. (2009). UK IPO Underpricing & Venture Capitalists. *The European Journal of Finance*, 15(4), pp. 421 - 435.
- Committee on Corporate Governance, SEBI. (2003). Report of the SEBI Committee on Corporate Governance, 5 - 8. Retrieved 2010, November 14 from [www.sebi.gov.in/commreport/corpgov.pdf](http://www.sebi.gov.in/commreport/corpgov.pdf).
- Cremers, K. J. & Nair, V. B. (2005). Governance Mechanisms and Equity Prices. *Journal of Finance*, 60(6), pp. 2859 - 2894.
- Deb, S. & Marisetty, V. (2010). Information Content of IPO Grading. *Journal of Banking & Finance*, 34(9), pp. 2294 - 2310.
- Daouk, H., Charles Lee, M. C. & David, N. (2006). Capital Market Governance: How do Security Laws Affect Market Performance? *Journal of Corporate Finance*, 12(3), pp. 560 - 593.
- Ekkayokkaya, M. & Pengniti, T. (2012). Governance Reform and IPO Underpricing. *Journal of Corporate Finance*, 18(2), pp. 238 - 253.
- Engelen, P. (2007). Underpricing of IPO & Investor Protection around the World - Country Level Evidence. Paper presented at 24th Annual EALE Conference, Copenhagen, Denmark. Retrieved 2010, November 20 from <http://uk.cbs.dk/content/download/67257/930079/file/Peter-Jan%20Engelen.doc>.
- Ghosh, S. (2004). Revisiting IPO Underpricing in India. Retrieved 2011, October 08 from <http://ssrn.com/abstract=703501> or <http://dx.doi.org/10.2139/ssrn.703501>.
- Habib, M. A. & Ljungqvist, A. (2001). Underpricing and Entrepreneurial Wealth Losses in IPOs. *Review of Financial Studies*, 14(2), pp. 433 - 458.
- Hearn, B. (2010). The Impact of Corporate Governance Measures on the Performance of West African IPO firms. *Emerging Markets Review*, 12(2), pp. 130 - 151.
- Jenson, M. C. (1986). Agency Cost of Free Cash Flow, Corporate Finance and Takeovers. *American Economic Review*, 76(2), pp. 323 - 330.
- La Porta, R., Lopez, F., Shleifer, A. & Vishny, R. (1997). Legal Determinants of External Finance. *Journal of Finance*, 52(3), pp. 1131 - 1150.
- La Porta, R., Lopez, F., Shleifer, A. & Vishny, R. (2002). Investor Protection and Corporate Valuation. *Journal of Finance*, 57(3), pp. 1147 - 1170.
- Larry, L. & Hovey, M. (2009). Corporate Governance, IPO Underpricing and Long-Term Performance of Listed Firms in China. 22nd Australasian Finance and Banking Conference.
- Ljungqvist, A. (2005). IPO Underpricing. *Handbook of Corporate Finance: Empirical Corporate Finance*. B. Espen Eckbo, (ed.). Elsevier (1, Chapter 7, pp. 375-418).
- Loughran, T., & Ritter J.R. (2004). Why Has IPO Underpricing Increased Over Time? *Financial Management*, 33, pp. 5 - 37.
- Ministry of Corporate Affairs. (2009). *Corporate Governance Voluntary Guidelines*, pp. 10 - 19.
- Pandya, V. H. (1992). Securities and Exchange Board of India: Its Role, Powers, Functions & Activities. *Chartered Secretary*, 22(9), pp. 783.
- Ritter, R., Loughran, T. & Rydqvist, K. (2006). Initial Public Offerings: International Insights, Pacific-Basin. *Finance Journal*, 2(2-3), pp. 165 - 199.
- Tian, L. & Megginson, W. (2007). Regulatory Underpricing: Determinants of Chinese Extreme IPO Returns. *Journal of Empirical Finance*, 18(1), pp. 78 - 90.
- Yeh, Y. H. & Shu, P. G. (2004). Corporate Governance and Valuation of IPOs. EFMA 2004 Basel Meetings Paper. Retrieved from <http://dx.doi.org/10.2139/ssrn.496502>.