
EXAMINING THE PERFORMANCE OF INITIAL PUBLIC OFFERINGS: A STUDY OF INDIAN HOSPITALITY AND TOURISM INDUSTRY

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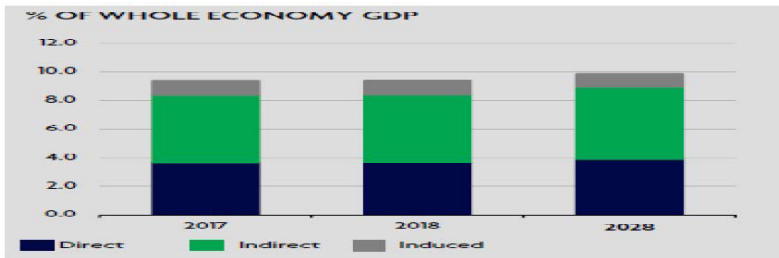
Abstract

Present study is an attempt to examine the listing day market performance of public issues floated by hospitality and tourism firms in India. During the sample period of 15 years (from January 2004 to March 2018) the average initial day Market Adjusted Excess Return (MAER) was found to be 18.8%. Further, the average return of travel support services segment was observed to be highest within the sector. The findings of the study are consistent with Chen and Chen, (2010).

Keywords: *Hospitality and Tourism Industry, Initial Public Offerings (IPOs), Underpricing*

Introduction

Since the Globalization, Privatization and Liberalization in 1991, there has been rapid growth of the Indian Economy. In the last two decades, various regulatory and political changes have fuelled the share of few sectors in the development of the economy. Tourism and hospitality is one among those few sectors, which have proactively contributed in the rising Gross Domestic Product (GDP).



Source: World Travel & Tourism Council's (WTTC) Economic Impact 2018 India

Tourism industry in India accounts for US\$ 234 billion (9.4 percent of the GDP) in 2017, forecasted to rise by 7.5 percent in 2018 and it is expected to grow at US\$ 492.2 billion (9.9 percent of the GDP) in 2028¹. According to India Brand Equity Foundation (IBEF), tourism industry is the 3rd largest foreign exchange earner for the country in 2016. During January – November, 2017 India's Foreign Exchange Earnings (FEEs) from tourism increased 20.4 percent year-on-year to US\$ 24.655 billion. Moreover, according to World Travel & Tourism Council's (WTTC's) Economic Impact 2018, hospitality and tourism industry in 2017 contributed to 8 percent of the total employment (41,622,500 jobs), which is expected to rise by 3.1 percent in 2018 (42,898,000 jobs) and further by 2 percent p.a. (52,279,000 jobs) till 2028 (8.4 percent of total).

In addition, hospitality and tourism industry also helps in regional and economic development of the country. According to WTTC's report, in the year 2017, a total of US\$ 41.6 billion (6.3 percent of total investment) was made in Hospitality and Tourism industry. It is further expected to rise by 6.7 percent in 2018 and additionally rise by 6.7 percent p.a. over the next ten years to US\$ 85.2 billion in 2028. Following the development of the tourism and hospitality industry and rising need of the required funds the Indian financial market has witnessed increased number of IPOs in this industry. During the last few years, 20 IPOs have been floated in this industry in India.

Initial Public Offering (IPO) underpricing is a well elaborated phenomenon across the financial markets of the world². Beatty and Ritter, (1986) cited ex-ante uncertainty, Rock, (1986) observed info asymmetry,

Allen and Faulhaber (1989) suggested signaling hypothesis, Welch (1992) observed informational cascades, Carter and Manaster (1990) and Megginson and Weiss (1991) highlighted certification hypothesis and Ibbotson and Jaffe (1975) and Ritter (1984) observed hot and cold issue periods, as varied reasons for IPO underpricing. The empirical literature on Indian markets observes underpricing in the range of 20 percent to 30 percent, which is at par with the developed countries of the world³.

As cited above, a strand of literature has highlighted various theories related to IPO underpricing but none of those have attempted to examine the presence of IPO underpricing in the phenomenally growing Tourism and Hospitality industry in India. The present study is an attempt to plug this gap.

The study will be organized in five sections. In section I, introduction to the problem under study is discussed, section II reviews the related literature, in section III the details of database and research methodology are discussed, in the fourth section findings are discussed and in the section V the conclusion of the study is presented.

Review of Literature

Plethora of literature is available on examining the performance of IPOs but the literature on the subject is scarce. Jang and Park (2011) examined 113 empirical studies on hospitality and observed only 2 percent of the total were dedicated to IPOs.

Atkinson and LeBruto (1995) observed underpricing of 30.63 percent in IPOs of US hospitality industry. Canina (1996) in a sample of US hospitality IPOs issued from 1979 to 1994 found 16.32 percent average underpricing. Further, Canina (1996) in the same study observed IPOs return to be outperforming S&P 500 returns after 1 year from the issue. Later, Canina and Gibson, (2003) observed 137 hospitality sector IPOs issued from 1981 to 2001 in US and found 16.5 percent average underpricing. Wang (2007) examined 22 IPOs of Chinese hospitality and tourism firms issued from 1993 to 2006 and found initial returns in a range of 56.1 percent for airlines to 334 percent for a catering firm. Similarly, Chen and Chen (2010) observed average underpricing of 150 percent in 25 tourism IPOs issued from 1993 to 2006 in China. Further, Chen and Chen (2010) also observed the issues underpriced

even after 1 year from listing. However, Borghesi et al. (2015) using a sample of US hospitality IPOs issued from 1996 to 2012 suggested underperformance relative to the market for at least the first three years from listing date.

In a nutshell, there is a strand of literature examining the performance of IPOs in developed markets, however, to the best of our knowledge no study has yet been attempted in India. Hence, this study will be an attempt to plug the literature gap.

Database and Research Methodology

Since the Globalization, Privatization and Liberalization in 1991, Indian Economy has witnessed a radical change. Moving with the wave of industrial growth the financial market has also soared to the new highs. However, hospitality and tourism industry have outnumbered the growth of all other industries in the economy. Moreover, Initiatives taken by government are fuelling the growth of this industry. Following the pace of the industry and rising need of the funds the number of IPOs by hospitality and tourism industry in India has increased since the large public issue by Jet airways in 2005. Since then 20 IPOs has been issued by different hospitality and tourism firms in India till March 31, 2018. Therefore, there is a strong need to empirically study the market performance of the hospitality and tourism industry in India.

The segment classification was adopted from the Indian Brand Equity Foundation, Ministry of Tourism. The data used in this study have been compiled from the Securities Exchange Board of India (SEBI) website. The listing day price related information was collected from the official website of Bombay Stock Exchange (BSE). The detail of 20 IPOs is given in the Table 1 below.

Data Analysis and Interpretation

IPO underpricing is measured by Market Adjusted Excess Returns (MAER). The MAER of an IPO has been defined as the excess of Initial Returns (IR) of the stock over the Market Return (MR) between the issue closure and the listing day. In order to calculate the market return BSE Sensex as the proxy for the market return have been used.

Name of the Sector	Issue Size (Rs. In Crores)	Percentage of total	No of issues	Percentage of total	Underpricing (RAW Return)	MAER (%)
Airlines	2327.37	24.73	3	15	-4.39	-2.91
Hotels	464.30	4.93	3	15	16.87	15.45
Restaurants	1654.81	17.58	3	15	15.82	19.23
Travel Support Services	610.38	6.48	1	5	28.90	28.33
Amusement Parks	181.25	1.92	1	5	26.08	25.56
Medical Tourism	4169.84	44.32	9	45	25.85	25.39
Total	9407.98	100	20	100		

Source: Author's Calculations

$$\text{MAER} = \text{IR} - \text{MR}$$

Where, IR = Initial return of a stock:

$$\text{IR} = \frac{(\text{Closing Price of the stock on the listing day} - \text{Offer Price})}{\text{Offer Price}}$$

MR = Market return:

$$\text{MR} = \frac{(\text{Sensex on the listing day} - \text{Sensex on the issue closure day})}{\text{Sensex on the issue closure day}}$$

The descriptive statistics of all variables are discussed in Table 2 below.

Variables	Mean	Minimum	Maximum	Std dev.
Raw Return (%)	18.63	-33.04	153.5	39.80
MAER (%)	18.88	-23.12	145.88	38
Listing Delay (days)	16.35	8	22	4.19
Issue Size (Rs. In Crores)	470.39	38	1899.34	452.25
Subscription Ratio	13.22	1.02	73.55	18.94
Age of the Firm (in years)	16.95	3	70.5	13.87

Source: Author's Calculations.

As can be seen from the table above, the degree of underpricing in the sample is widely spread across the range from -33.04 to 153.5 % with the mean underpricing (measured by MAER) 18.8%. The reason of such disparity could be attributed to the fact that issuers in hospitality and tourism industry voluntarily underprice their issue to attract more investors, (Canina and Gibson, 2003). Furthermore, hospitality and tourism being an investment oriented industry relies much on the cheaper sources of finance like IPOs for their growth and expansion. Investment bankers, leveraging their position and informational asymmetry between issuers and investors underprice the issues (Pande and Vaidyanathan, 2007). In addition, Chen and Chen (2010) suggested, investors should not consider IPO underpricing as signal of quality of the firms. As IPO underpricing could be due to market sentiments, prevailing economic conditions and information asymmetry (Boulton, et al., 2010 and Rock, 1986).

Listing delay is also widely spread attributing to the fact that before 2010 the listing period was 22 days which was cut down twice by SEBI in 2010 and 2015 to 12 and 6 days.⁴ The mean issue size of the sample is 470 crore, whereas, the biggest issue size was of Jet airways and smallest was of Lotus Eyecare. The issue size of a company is in direct proportion to the size of assets and operations of the company. The mean subscription ratio of the sample is 13.2%, which is based on the prevailing demand and supply conditions in the industry. Canina et al., (2008) observed a direct relationship of subscription level, size of the issue and IPO underpricing. The average age of the company at the time of IPO in Hospitality industry is 16.95 years. However, in the sample Cox and Kings have an age of 70.5 years whereas, all other companies have the age at IPO of around 20 years.

Conclusion

The present study is an attempt to examine the listing day market performance of public issues by hospitality and tourism firms in India. A sample of 20 hospitality and tourism industry IPOs issued from 2004 to March 2018 are considered and average IPO underpricing is found at 18.8%. However, the IPO underpricing of hospitality and tourism industry reported is much lower than those documented in most previous studies in Asian markets, but is in line with the average return in US market.

The observed IPO underpricing however is not evenly distributed among different hospitality and tourism segments. Evidence suggests that, travel support services segment reported highest average market adjusted underpricing than other segments in hospitality and tourism industry in India. However, in the present study only initial day market performance of the IPOs is considered, therefore, in future research the aftermarket performance of IPOs may be considered. In addition, the future research must also incorporate the reasons of IPO underpricing in hospitality and tourism industry so that a complete understanding of the market performance of this sector can be achieved.

(Endnotes)

¹ World Travel & Tourism Council's (WTTC) Economic Impact 2018 India.

² Loughran T., Ritter J. R., and Rydqvist K. (1994). Initial Public Offerings: International insights. *Pacific-Basin Finance Journal*, 2(2), 165-199. Updated in 2016.

³ Please see Sahoo (2014), Handa and Singh (2014), Krishnamurti and Kumar, (2002), Pande and Vaidyanathan, (2007).

⁴ SEBI in April 2010 announced a reduction in the time between issue closure and listing from 22 days to 12 working days. Later in November 2015, this period was further reduced to 6 days.

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