

# **PUBLIC RESPONSE TO INITIAL PUBLIC OFFERING (IPO) IN NEPAL**

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# **TRIBHUVAN UNIVERSITY**

## ***CENTRAL DEPARTMENT OF MANAGEMENT***

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### ***RECOMMENDATION***

This is to certify that the thesis

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has been prepared as approved by this Department in the prescribed format of  
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### *VIVA-VOCE SHEET*

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and found the thesis to be the original work of the student written according to  
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## DECLARATION

I hereby, declare that the work reported in this thesis entitled “**Public Response to Initial Public Offering (IPO) in Nepal**” submitted to Central Department of Management, University Campus, T.U., Kirtipur is my original piece of work done in the form of partial fulfillment of the requirement for the Master’s Degree in Business studies under the supervision and guidance of Prof. Dr. Radhe Shyam Pradhan, Central Department of Management.

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## **ABBREVIATIONS**

A.D.	:	Anno Domini
BSE	:	Bombay Stock Exchange
CFO	:	Chief financial Officers
CIT	:	Citizen Investment Trust
FY	:	Fiscal Year
GDP	:	Gross Domestic Product
IPO	:	Initial Public Offering
LSE	:	London Stock Exchange
Ltd.	:	Limited
NCML	:	NIDC Capital Market Ltd.
NEPSE	:	Nepal Stock Exchange
NFCL	:	National Finance Company Ltd.
NIDC	:	Nepal Industrial Development Corporation
NMB	:	Nepal Merchant Bank Ltd.
NYSE	:	New York Stock Exchange
SEBON	:	Security Exchange Board of Nepal
SEC	:	Security Exchange Centre

# CHAPTER I

## INTRODUCTION

### 1.1 Background of the Study

Initial Public Offering (IPO), referred to simply as a “public offering” is when a company issues common stock or shares to the public for the first time. They are often issued by smaller, younger companies seeking capital to expand, but can also be done by large privately-owned companies looking to become publicly traded. Basically initial public offering (IPO) occurs when a security is sold to the general public for the first time, with the expectation that a liquid market will develop. An IPO can be of any debt or equity security. Most companies start out by raising equity capital for a small number of investors, with no liquid market existing if these investors wish to sell their stock. If a company prospers and needs additional equity capital, at some point the firm generally finds it desirable to "go public" selling stock to a large number of diversified investors. Once the stock is publicly traded, this enhanced liquidity allows the company to raise capital on more favorable terms than if it had to compensate investors for the lack of liquidity associated with a privately held company. Existing shareholders can sell their shares in open-market transactions. With these benefits, however, come costs. In particular, there are certain ongoing costs associated with the need to supply information on a regular basis to investors and regulators for publicly traded firms. Furthermore, there are substantial one-time costs associated with initial public offering that can be categorized as direct and indirect costs. The direct costs include the legal, auditing, and underwriting fees. The indirect costs are the management time and effort devoted to conducting the offering, and the dilution associated with selling shares at an offering price that is, on average, below the price prevailing in the market shortly after the IPO. These direct and indirect costs affect the cost of capital for firms going public.

Capital market plays a vital role in the developing nation's economy. The proceeds from sale of securities in the secondary markets do not go to the organizational issuer instead to the initial owners (sellers) of the securities. This is the first issue market that attracts

investors to invest in the shares of the issue companies. The secondary market comprises the organized security exchanges and a specialist facilitates the transaction. The primary share market is the market for new issue of securities. The success of the capital market depends on primary market and this ultimately provides a basis for multiple transactions in secondary market. It is the media through which new financial assets are issued or generated. After securities have been purchased from the primary market, they can be traded in the secondary market. The major of all capital market transaction occur in the secondary markets.

In the context of Nepal, Nepal Stock Exchange Limited (NEPSE) is only the secondary market in Nepal. The Security Exchange Centre issued 62 companies' shares from the year of its inception to 1999 A.D. Among these 23 companies were undersubscribed including Nepal Med. Ltd., Nirmod Pharmaceuticals Ltd, Harisiddhi Brick and Tile Ltd., Himgiri Textile Ltd, Banswari Leather and Shoes Factory Ltd., Nepal Awasthi Bikash Bhatta Company Ltd., and Yeti Finance Co. Ltd etc. Although the secondary market was non-functional and public were not fully aware of on the working of the capital market. The public response to the new issue of shares of selected companies like bank and finance companies were overwhelming.

Nepal Stock Exchange Limited is a non profit organization. It operates under Security Exchange Act 1983. The basic objective of the Nepal Stock Exchange Limited is to impart free marketability and liquidity to the government bonds and corporate securities by facilitating transactions in its trading floor through market intermediaries, such as brokers and market makers. Government of Nepal, Nepal Rastra Bank, Nepal Industrial Development Corporation and its members are the shareholders of NEPSE. Members of NEPSE are permitted to act as intermediaries in buying and selling of government bonds and listed corporate securities. It has 23 member brokers and two market makers. It has also given membership to eleven sales and issue manager (financé companies) and two dealers: NMB Bank and Nepal Financial and Saving Co. Ltd.

Capital market is gaining business attention since last few years. The NEPSE index, which shows the stock price trend of all the listed securities in the stock market, has been increasing in the recent fiscal years. Hence, the general investors are very keen to make investment in the securities of the companies, through both primary and secondary markets. In primary market, the investment is made through public issues of ordinary shares, preference shares, debentures and right shares as well as mutual fund and unit's scheme.

Keeping these views into the consideration the study focuses on the response towards public offering by investors. It is also based on the dealing process of primary market. It also focuses on what investors want in IPO before they invest their sector performance, knowledge, ultimate goal for investment, sources of information etc.

## **1.2 Statement of the Problem**

The problem towards which this study is directed is to identify the public responses towards the IPO of financial as well as non-financial sector in Nepalese market, how is primary market growing in Nepal, how are the issue managers performing in IPO, generally what an investor expects from his or her investment, etc. Still more than half of Nepalese Citizens are under the line of literacy. And among the literate ones, there is lack of proper knowledge about the practice of stocks. They do not know what the securities mean at all. How can we expect them to invest in the securities? And even among the aware people there is still lack of confidence level. They do not want to take risk. In developing country like Nepal, IPO is still a new phenomenon. There exist various types of obstacles in IPO. In this respect, there is the tendency, limitation of ownership and control of the enterprises within the close circle. On the other hand, there were no financial or other incentives for the firms to the public. Further more the existing strong barriers of socio-economics infrastructure and historical reasons made the successful flotation difficult. Dealing in public issues of the primary market securities is subject to the directives and regulatory framework of the concerned

governing bodies. Hence, the study is primarily deals with the process of managing the process of the public issues by the issue managers. Besides, Investment in the primary market instrument has gaining the interest of the general and corporate investors. Most of the public offerings have been successfully made since the investors have considerable concern and willingness for investment in these securities (SEBON, Annual Report) There is not any provision to present citizenship at the time of submitting their share application form. So, single investor can apply hundred of applications, showing dummy names. As a result they can capture large number of shares. When single investor captures large number of share, he can influence the company management and stock price also. The study is meant to know the perception and perfection of the general investors regarding the investment in the securities through primary Market. The focus of the study is on the status of the general investor, the volume and portfolio of their investment and the decisive factors they consider while opting companies for investment. But the study is also equally concentrated on investment in the manufacturing and processing companies in the non-financial sector. The study aimed at those factors which could be decisive from the investors view whether to invest or not in particular company. Hence, study was felt required to find out why there has been such variation in the responses by the public. The causes for this response must be analyzed so that new companies who would like to issue new shares can benefit from the conclusion drawn from this research. Besides these, there are other factors, which slow down the pace of stock market growth in Nepal. They are:

- Unfavorable macroeconomic conditions,
- Political instability,
- Unconfident investors,
- Weak tax system and slow privatization process,
- Lack of institutional investors,
- Lack of trained and qualified manpower,
- Insufficient knowledge of investors about the security market.

But among these which is/are the main factor to define the market are still questions to be answered. Keeping these views into the consideration this study focuses on the following research questions:

- What are the process of IPO in Nepal?
- What is the situation of primary market issues in Nepal?
- What are the problems of IPO in Nepalese market?
- How the Nepalese investors show their responses to the primary market issues?
- What are the pace of stock market growth in Nepal?
- What is the systematic mechanism of IPO in Nepal?
- What are the sectoral growth of IPO?

### **1.3 Objective of the Study**

The major objective of the study is to focus on the public response to the initial offerings or primary issues of shares in Nepal. The specific objectives are:

- To analyze the current situation of primary market issues
- To examine the sectoral growth of primary market
- To find out the investor response to initial public offering
- To evaluate the performance of the Investment Bankers (Issue managers) in the process of IPO.

### **1.4 Limitations of the Study**

The study is carried out for the partial fulfillment of Master in Business Studies programme of Tribhuvan University. It focuses to analyze certain aspects of primary share market in Nepal Studies and references are limited in the perspective of Nepalese capital market. The other limitations are:

- The study, lack of the sufficient time resources are the major limitations of the study since the study has been conducted for fulfilling the partial requirement of MBS course of T.U Nepal.

- This study has analyzed and evaluated the data from limited sources and data.
- This study is mostly based on secondary data. So, the accuracy of research depends upon the reliability of data.
- Only a few companies from financial and non- financial sector are considered for the study.
- The study heavily focuses on the initial public offering and current legal aspects associated their in.
- The study has not covered recent changes because of limitation of data
- Variations of data in itself are also found when comparing with different sources.
- The information regarding the same questionnaire is different from different sources.
- Due to the difficulties of availability of the data, only ordinary and simple techniques have been used for the analysis.

### **1.5 Organization of the Study**

This study will be organized in 5 chapter. The first chapter contains the introductory part of the study, this chapter describes the general back ground of the study, statement of the problem, objective of the study, significance of the study, limitation of the study and organization of the study. The second chapter is devoted to theoretical analysis and brief review of related and pertinent literature available. It includes a discussion on the conceptual framework and review of the major studies. similarly the third chapter includes the research methodology employed in the study. This deals with the nature and sources of data, list of the selected companies, the model of analysis, meaning and definition of statistical tools. However the fourth chapter deals with the presentation and analysis of both primary and secondary data by using mathematical and nonmathematical tools and it deals with major finding of the study. finally the fifth chapter incorporates summary, conclusion, and major finding of the study. The bibliography and annexes are incorporated at the end of the study.

## **CHAPTER–II**

### **REVIEW OF LITERATURE**

Actually review of literature means that the study of relevant topic in the related field of researcher reviewing related research studies and findings such that all past studies, their conclusion and deficiencies may be known and further research can be done. Literature review is basically a "stock taking" of available literature survey, thus, provides us with the knowledge of the status of their field of research .therefore, this chapter has its own importance in the study (Kothar i, 1990:10)

This chapter includes the review of previous studies, article and conceptual framework for the related studies. To present the real framework of the study, mere analysis is not enough and review of some related materials should be dealt with to give research a clear vision. Knowledge of past study provides foundations to the present study .This chapter are mainly divided into two parts like conceptual framework and review of related studies.

#### **2.1 conceptual Frameworks**

##### **2.1.1 Financial Market**

Market in which long-term well as short loan is provided is called financial market. It provides forum in which supplier of funds and user of funds transactions in short term debt instruments or marketable securities take place in the money market .Long-term securities (like bonds and stocks) are traded in the capital market .Capital market further can be divided into primary market and secondary market. All securities, whether in the money or capital market are initially issued in the primary market? This is the only market I which the company or government is directly involved in the transaction and receive direct benefit from the resale of securities. Once the securities began to trade among individuals, business, government or, financial institutions, savers and investors, they become part of the secondary market.

The primary market is where new securities are sold and the secondary market can be viewed as a “used” or "preened" securities market. In short, we can divide financial market into money market and capital market .And these markets can be further divided into primary and secondary market.

### **2.1.2 Money Market**

Money market is the market for the short term securities like treasury bills, government bonds, certificates of deposits banker s acceptances and commercial paper or promissory notes. It includes both primary and secondary market activities. The money market exists because certain individuals, business, governments and financial institutions have temporarily idle funds that they wish to place in some kind of liquid assets or short term interest earnings instrument like this other individuals ,business, governments and financial institutions are in need of seasonal or temporary financing. Thus, the money market provides the platform for the supplier (who have idle funds for some period) and demand makers of short term liquid funds. In theory, we found money market different from the capital. In practice, however in most countries with efficient financial markets, where money and capital market is combined, the merchant banks are active in both. This is because negotiable money market instrument for all practical purpose is simply a short term capital market instrument. Therefore, the techniques and facilities needed to operate money market are almost same as those needed to operate the capital market.

### **2.1.3 Capital Market**

The capital market is defined as a place where finance is raised by companies for meeting their requirement of funds for new projects, modernization and expansion programmes, long-term working capital needs and for various other purposes. The capital market mobilizes savings of individuals as investment in shares, debentures, Units of mutual funds and other like financial instruments, which are ultimately deployed for productive purposes in various sectors of the economy. (Weston and Bringham, 1998:256)

A place where long term lending and borrowing takes place is known as capital market. The capital market is the market for long-term loans and equity capital. Companies and the government can raise funds for long-term investments via the capital market. The capital market includes the stock market, the bond market, and the primary market. Securities trading on organized capital markets are monitored by the government; new issues are approved by authorities of financial supervision and monitored by participating banks. Capital market refers to the links between lenders and borrowers of funds, arranging of funds-transfer process to seek each other's benefit.

Capital market consists of the various suppliers and users of long term finance. It is differentiated from the money market which embraces short-term finance. The capital market serves as a link between suppliers and users of finance. It is a mechanism for the mobilization of public savings and channeling them in productive investment. In this way, an important constituent of the capital market is the securities market. It has a wide term embracing the buyers and the sellers of securities and all those agencies and institutions which assists the sale and release of corporate securities. (Weston and Brigham, 1998:257)

For the purpose of easiness the capital market can be divided into two parts, these are:

### **2.1.3.1 Non-securities Market**

Non-securities market is a market where financial needs (often borrower demanders) are fulfilled for longer period of time without issuance of any securities like shares bonds and debenture. Financial transactions such as banks, business houses, saving institutions and individuals come under this non-securities market.

### **2.1.3.2 Securities Market**

The security market is known as the market where all types of securities are traded. Security market is a broad term embracing a number of markets in which securities bought and sold. Securities markets goes about the business of placing any order to buy or sell, how the order is executed, the process of setting

the payment and transfer costs, and one hopes the payment of federal personal income taxes on the profit from the transaction. Security market sets a price for the securities it trades and makes it easy for people to trade them. Securities market facilitates the sale and resale of transferable securities. The securities market can be defined as the mechanism for bringing together buyer and seller of financial assets to facilitate trading. Securities market is classified into two the market in new securities are sold is called primary and the market in which exiting securities are resold is called the secondary market. Secondary market is created by themselves actually buying and selling dealers set price at which they themselves are ready to buy and sell (bid and ask price respectively). Broker and dealer come together in organized market or in stock exchange (Gitman, 1992:457) the securities market may also be divided into two parts

#### **2.1.3.2.1 Primary Market**

The term “Primary Market” is used to denote the market for original sale of securities by issuer to the Public. The primary market is the place where corporations and Government Issue new securities at first time to generate the money for real investment. All the securities, whether it is for short term or long term, are initially issued in the primary market. This is the only market in which the company or government bodies are involved in the transaction and receives direct benefits from issue that is the company actually receives the proceeds from the sale of securities ( Bhattarai, 2005: 7). The primary market itself can be subdivided into seasoned and unseasoned issues. A seasoned new issue refers to the offering of an additional amount of already existing securities, whereas an unseasoned new issue involves the initial offering of a security to the public. In primary market the principal sources of funds is the domestic savings of individual and business, other supplies include foreign investors and governments. The ultimate supplies of funds are those sectors with a surplus of current incomes over expenditures (savings) and these funds flow to ultimate users, economic use securities to finance a surplus of expenditure over their current incomes.

Basic Characteristics of primary market are:-

- Market for new long term chapter.
- The securities are sold for the first time
- The securities are issued by the company directly to investors,
- Used by the companies for the purpose of setting up new business or for expanding or modernizing the existing business.
- Facilitates capital formation in the economy.
- The transactions are less in primary market.
- Buying security in primary market is less risky.

#### **2.1.3.2.2 Secondary Market**

Secondary market involves the purchase and sale of securities which are already issued to the general public and traded in the stock exchange. Secondary market is created by brokers, dealers and market makers. Brokers bring buyer and seller together with themselves actually buying or selling, dealer's set price at which themselves are ready to buy and sell (bid and ask price respectively). Brokerage and dealer come together organized market or in stock exchange (Gitman, 1992: 457). Nepal Stock Exchange

(NEPSE), New York Stock Exchange (NYSE) and Bombay Stock Exchange (BSE) are the example of organized stock exchange (secondary market). The secondary market is a very important element of the securities market. The existence of an organized secondary market can provide this level of confidence to holder of securities so that they can purchase securities in the primary market readily convert these securities to cash whenever they wish to do so. The benefit of secondary market is that it increases the investment opportunities. Person who may not have been able to acquire securities on the primary market have been able to acquire securities on the secondary market.

## **2.2 Public Offerings**

It is the raising of long-term funds for governments or corporation from a fund sufficient public group in the primary market. The most important aspect of public offerings is its role as the single most effective means by which government and corporate entities can obtain long-term (debt or equity) on a permanent basis. It not only permits them to broaden their sources of finance beyond the banking system but also the banking system is usually a short-term or medium-term floating rate lender. The securities market is often the only means of obtaining large sums of fixed rate, long-term funds.

### **2.2.1 Advantages of an IPO**

As discussed above, the primary reasons for conducting an IPO are to raise money and to create liquidity for investors. There are also important incidental benefits to going public. Objective benefits include:

- (i) Obtaining a readily ascertainable market value for the company's stock,
- (ii) The ability to make acquisitions through the payment of securities rather than cash,
- (iii) Greater access to financing through commercial lending,
- (iv) Greater access to the financial markets for follow-up offerings, and
- (v) Heightened name recognition and prestige among customers and suppliers.

Less objective benefits are the sense of success and accomplishment that accompanies a successful IPO and becoming a publicly traded company.

### **2.2.2 Disadvantages of an IPO**

The major disadvantage to becoming a publicly traded company may be compliance with the act reporting requirements. While registering under the act is quite simple, the periodic and event -based reporting obligations under the act require a significant amount of time and expense. In addition, the act obligations will compel disclosure of information that the issuer, its directors, management and controlling stockholders

might otherwise want to keep to themselves. Financial and business information, executive compensation, transactions between the company and its directors, management and major stockholders, and certain employee benefits must all be disclosed in reports filed with the SEC, mailed to the stockholders, and made available to the public upon request. Directors and officers, as well as major stockholders, also must file reports with the SEC disclosing most transactions in the company's securities. Also, the failure to accurately make such reports may result in civil or criminal penalties.

The direct financial costs, including legal, accounting and printing fees, of conducting an IPO and of being a publicly traded company are substantial, as are the indirect costs of the time required to be spent on these matters by management.

Also, the management and governance of a publicly traded company is more difficult and less flexible. The solicitation of stockholder votes on any matter is strictly regulated under the act, and rules of the exchange on which the securities are listed require certain matters to be approved by stockholder vote even if not otherwise required by state law. Additionally, because of pressure to raise the price of the company's stock, management may feel persuaded to adopt policies aimed at achieving short-term results rather than long-term goals.

### **2.2.3 Timing of an Initial Public Offering**

Obviously, not all companies that would like to go public are in a position to do so. Factors relevant to a company's ability to successfully close an IPO include (I) its past financial performance, its financial projections for the future, and its ability to generate consistent increases in revenues and earnings, all of which are crucial for a public company to survive in the market place,

- (ii) the experience and depth of the company's management team,
- (iii) a solid product position in the market with growth potential,
- (iv) a focused mission set forth in a well written business plan to present to prospective underwriters, and
- (v) attorneys, accountants and public relations firms experienced in working with

the SEC. Especially in the case of technology-based companies, the determining factor in the success of an IPO may ultimately be the receptivity of the stock market to new issuances in a Company's particular industry at the time that the IPO is undertaken.

The company will have to satisfy the underwriters that all of the above criteria are met, and even then the underwriter may insist on changes to the company's capital structure as a condition to its engagement. For example, the underwriters might require the company to affect a reverse stock split prior to the closing of the IPO in order to price the shares being offered in a typical IPO price range. If the underwriters do not feel that the company is offering a sufficient number of shares to ensure an acceptable "float" of publicly traded shares, they might require that certain stockholders participate in the offering by selling some of their own shares (a "secondary offering"). The underwriters might also insist on fundamental changes in the company's means of conducting its business as a condition to its engagement, such as the cessation of insider transactions and perceived conflicts of interest and the appointment of outside directors. Companies which are not willing to make such changes may not be able to attract an underwriter willing to manage the IPO.

If the issuer belongs to a certain industry that is particularly attractive to investors at the time of the proposed IPO, it will have more leverage in choosing and negotiating with an underwriter. Conversely, if market conditions are unfavorable at the time of the offering, the issuer will have less flexibility in how the deal is structured and may have to postpone the IPO altogether.

#### **2.2.4 Primary Market Instrument**

After the establishment of Securities Board of Nepal in 1993, the following instruments have been used by the Nepalese corporate bodies to raise capital from primary market.

##### **2.2.4.1 Common Equity/Stock Offering**

Common equity represents the ownership position in a company. The holders of common stocks, called shareholders or stockholders are the legal owners of the company. They are entitled for dividends for the capital contributed by

shareholders by purchasing common shares. The capital represented by common stock is called share capital. Equities convey ownership of the corporation and are basically valued in line with expected future earnings. To date they have been relatively little affected by financial innovation (Gautam & Thapa, 2006:17). Many companies have only one class of stock, often called common stock or ordinary shares. This class of stock carries residual ownership of the company, entitling the holder to unlimited interest in the earnings and assets of company after limited claims are paid. Dividends paid on stocks are usually unstable because they tend to vary with earnings and also less than earnings. The market price of common stock is often subject to wide fluctuations, because it depends largely upon investors expectations of future earnings. Following are the most significant feature of equity shares.

### **1. Risk**

Equity shareholders run the risk of receiving nothing if earnings are insufficient to cover all obligations (Srivastava, 1995:337).

### **2. Control**

Every equity shareholder has the right to vote on every resolution placed before the company and his voting right on a pool is in proportion to this share of paid-up capital of the company (Srivastava, 1995:338).

### **3. Rights**

The equity shareholders have the right of Voting, to transfer shares in the proceeds upon the liquidation of company, share in the profits when distributed as dividends etc.

### **4. Pre-emptive Right**

The Company is under legal compulsion to offer new issues to the equity stockholders before placing them in the market for subscription. Such a right of equity stockholders to purchase newly issued equity stock is termed as preemptive right or right offering.

## **5. Maturity**

There is no stated maturity at which capital must be returned to the equity shareholders. So, equity shares provided permanent capital to the company.

### **2.2.4 .2 Preference Shares**

Preferred stock is a fixed income security and it is also the alternative sources of long term funds for the company. Preferred stock is similar to bonds in same respects and to common stocks in other ways preferred stock represents equity of a corporation but it has different from common stock because it has preferences over common stock in payment of dividends and in the assets of the corporation in the event of liquidation (Ross, Jaffe and Westerfield, 1993:402).

The preferred stock, though not a popular with investors as bonds and common stock, offers unique features that make it attractive under certain circumstances. First, it is hybrid security because it has characteristics of two types of securities: debt and common stock. Second, it is essentially a fixed income security. Preferred stock investors typically receive fixed dividends (Cheney & Moses, 1992: 404-405). Preferred stock has a number of features, major features includes: It has priority of claim over common stockholders with regards to income. They are paid dividend at a fixed rate specified in the agreement. Preferred stockholder claims on assets are superior to equity Stockholder during the time of liquidation of company. Normally preferred stockholder do not have direct right to participate in the management through voting from directors and other matters. Unlike common stockholder, preferred stock always has a Par value. At their option preferred stockholders may be allowed ( if mentioned in the

Corporation s charter ) to switch over to equity stock. A call provision gives the issuing corporation the right to call in the preferred stock for redemption. Today, however most new preferred stock has a sinking fund and thus an effective maturity date.

The different type of preference share:-

- Cumulative preferred stocks.
- Non-cumulative preferred stocks.
- Redeemable preferred stocks.
- Non-redeemable preferred stocks.
- Convertible preferred stocks.

### **2.2.4.3 Bonds/Debenture**

Debenture as a debt security is the alternative sources of long-term fund for the company and given different names in different countries. In the United Kingdom, Nepal and India the term „debenture“ is popular, but in the US the term „bond“ is common (Srivastava, 1995:342). A debenture is an unsecured corporate debt, whereas a bond is secured by a mortgage on the corporate property. A debenture is an acknowledgement of a debt under the sale of a company and containing a contract for the repayment of the principal sum at a specified date and for the payment of interest at a fixed rate percentage (Srivastava, 1995:343). A bond is a type of fixed-income security by a borrowing entity in which the amount to be paid to the investor is specified in the investment contract or indenture. Debentures have some important features such as interest rate, maturity date, redemption, indenture, security, converted ability, yield and claims on assets & incomes (Pandey, 1994:820). In short, debenture is a formal evidence of debt and termed as the senior securities of a company. Certain distinguishing features of debentures are as follows: The debenture or bond has fixed maturity date. That means, the principal amount of bond must be repaid at the time of maturity. Debenture holder has priority on claim to income over preferred stockholder and common stockholder. Bondholders also have priority over stockholder in respect of their claims on assets. Debenture holders do not have controlling power through the vote for the election of directors but indirectly influence managerial decision through protective covenants in indenture.

The different types of debenture are:-

- Secured debenture.
- Unsecured debenture.
- Redeemable debenture.
- Perpetual debenture.
- Convertible debenture.

#### **2.2.4.4 Options**

An option is probably the most popular derivative security in the world of investment. It is a contract between two people wherein one person grants the other person the right, but not obligation, to buy or sell a specified asset at a pre-determined price on or before a set expiration date. It is derivative security because it derives its value from an underlying security (Security for which the option has been written) such as a stock, a bond etc. In the securities industry, options are marketable security and can be bought and sold in the stock exchanges. So the option owner has the right to sell the option and any other investors can invest on it. An option buyer pays an option writer a premium for granting the option. After options have been created, they can be traded at determined premiums (or Prices) that fluctuate continuously (Gautam & Thapa, 2006: 7-1). Option is not in exercise up to now in Nepal. The option is divided into two types i.e. Put and Call Option. Option to sell certain shares at predetermined price within or a certain later date called Put Option where as an option to buy certain share at a predetermined price with in or on certain future date is called call option (Bhattarai, 2006: 291). Option has certain features which are given below.

##### **1. Exercising Date**

The fixed price stated in the option contract at which the underlying asset may be purchased or sold is the exercise price. it is also called strike price and denoted by E.

## **2. Expiration Date**

The option has a certain maturity period. The option expires after its maturity period and the maturity date is the expiration date.

## **3. Exercising an Option**

The act of buying or selling the underlying asset through an option contract is called exercising an option.

### **2.2.4 Initial Public Offering (IPO) Manual**

Initial Public Offerings (IPO) manual is the detail procedure of handling Initial Public Offerings of the companies seeking “going public” for the first time. This manual outlines all the activities and steps that have to be observed by all issuing companies and issue managers in respect to Initial Public Offerings (IPO). This manual has been prepared with a view to present a detailed, descriptive and step-by-step action sequences in the Initial Public Offerings, relevant to all the companies offering shares to the general public. But, it is subject to periodic amendments and supplements. The Public Offering is not an easy task. There are many organizations involves during this periods. They are:

#### **2.2.4.1 Issuing Company**

Issuing company is the company raising funds from the general public through the process of public offering. The purpose of public offerings is for the collection of funds from general public, a fund sufficient group, by the company as per its requirement of business expansion. The company seeking for public offerings could be a completely new company (initial public offerings), a new company set by the existing company (initial public offerings) or by existing listed company (successive public offerings).

As per the Company Act, only public companies are liable to go for public offerings. The Act specifically states that private companies are not allowed to sell their shares and debentures in the free market. For public company issuing debentures, the reasons for such issue, project to be financed and its estimated budget along with the

information about secured or naked nature of the debenture, needs to be approved from the governing bodies.

NRB has made mandatory that financial institutions must go for common stock public offerings within specified time of operation commencement. NRB has also set forth different minimum percentage of equity holding to be offered to the public shareholders. For commercial banks, minimum shares to be held by public is 30%; for finance companies, it is 40% ; for development bank it is minimum 30% and maximum of 50%. In the case of foreign participation, their equity holding would be arranged from the percentage allocated for the public. For finance companies, in the event of foreign participation, the minimum percentage to be allocated to the general public is 25% of paid-up capital.

For other public companies such compliance to go into public offerings of equity holding are absent. For such companies, going into public signifies the need of funds for the company rather than the obligation.

The provisions and conditions of Securities Registration and Issue Act, 2051 has set the guidelines that before going into public offerings, issuing company should take into consideration that (SEBON Annual Report, 2007:23)

**a) If the issuing company is industrial institutions**

- The institution has bought the land or made other provisions in which necessary infrastructure like factory; office buildings, godowns etc. are already build in or made necessary arrangements for it.
- Necessary technology has been selected for which spare parts of machineries needed have been bought. If not, LC has been opened to buy the necessary technologies.
- Estimated budget has been proposed for the project to be implemented and for which if loans are required, such agreements are already made.
- In the absence of long-term loan agreement, issue securities are under written.
- Necessary approvals according to the existing Acts have been taken.

**b) If the issuing company is financial institutions**

- According to the nature of the business, required infrastructures are installed.
- Approval has been taken under the Company Act 2063.
- For commencing other activities, authority and approval from governing bodies based on existing Acts has been taken.

**2.2.4.2 Merchant Bankers**

Merchant bankers are intermediaries in which they work as mediators in the fund mobilization from the general public to the business groups. The funds are raised from the hypothetical market that comprises widely spread fund surplus groups, mainly the general public and the concentrated fund deficient groups, mainly the business groups. Funds are raised under different tool names that have long-term and short-term maturing period. According to such maturity period of the tools traded, market is identified as capital market for long-term and money market for short-term tools to be traded.

The role of merchant bankers in this market is to help create and expand securities underwriting, the secondary market for securities and money market. They also provide additional services in advising corporations and managing investment portfolio for the needing groups.

The concept of merchant banking differs from other commercial and development banks in respect that they do not require large funds to be invested as a principle. Their sources of income are basically the service charge they charge to their clients for playing intermediary role in the fund mobilization and their advisory role. Typically, the activities of domestically oriented investment banks can be grouped under:

- Securities underwriting
- The secondary market for securities
- The money market
- Corporate advisory services
- Investment portfolio management services, and also

- Venture capital Leasing / hire purchase
- Other services (insurance, real estate etc.)

The role of merchant banking in managing the public offerings comes under the heading of securities underwriting. The working process of which would be described comprehensively later.

For the working of merchant banking function in Nepal, Nepal Rastra Bank (NRB) has set forth the working guidelines. Guidelines have identified working of merchant banking into two sets of functions. The first set is the non fund-based functions and the second set is fund- based functions.

Fund-based activities identified for the merchant banking are:

- Bridging finance
- Underwriting
- Project finance
- Venture capital
- Acquisition and merger

Non fund-based activities identified for the merchant Banking are:

- Share issue management
- Mutual fund
- Portfolio management
- Corporate counselling
- Project counselling
- Debenture trusteeship
- Arranging international finance
- Investment advisor
- Advising corporate mergers

NRB has set the directives as for non fund-based activities of merchant banking, for underwriting and for bridging finance it is not necessary to take separate approval from

NRB. But, for other fund-based activities of merchant banking, it is necessary to take separate approval from NRB for different activities to be undertaken.

In Nepal, there are 7 merchant banks already established. They are providing issue manager, lead underwriter, register, transfer of shares etc. services to other institutions.

#### **2.2.4.3 Securities Board**

Securities board has been formed under the Securities Exchange Act, 2040 Clause 3. This legislation has required for the creation of an independent Statutory Board to be an apex authority for securities market, thus resulting into the formation of Securities Board.

The need of legislative body is for maintaining healthy and orderly development of the securities markets and to ensure adequate investor protection. Establishment of Securities Exchange Board (SEB) is necessary to promote markets that ensure:

- **Fairness:** The markets must promote integrity in dealings, high standards of conduct and good business practice.
- **Efficiency:** The markets should with professionals and be well informed, offering high standards of service at reasonable cost.
- **Confidence:** The market must inspire confidence in both investors and issuers to actively participate in and rely more on the securities markets.
- **Flexibility:** The markets should be resilient, innovative and be continuously responsive to the needs of all market participants.

#### **Role of Securities Board in Issue of Securities**

In its approach to manage public issues of securities, the Board will bear in mind

- a. Protection of rights and interests of the investor, especially,

The right to adequate, true and fair information

- The need for liquidity Prompt, fair and equitable allotment
- Easy and efficient service in allotments and transfers

**b.** The need to encourage corporate entities to tap the securities markets for their diverse resources needs.

The Board would Endeavour to evolve market and institutional structure, a set of instruments and methods of public offerings to cater the above objectives.

The legislative provisions relating to public issues of securities may be classified under:

**a.** Capital control, governing issue of securities and the terms of their issues:

- To regulate terms of issues of securities from the viewpoint of investor protection, issuers needs and overall development of the securities market; and
- To promote sound capital structure of companies.

**b.** Prospectus provisions, governing the disclosure of information at the time of issue of any security;

**c.** Obligations of regular disclosure of financial and other information on entities making public issues;

**d.** Listing requirements governing traded securities;

**e.** Provisions governing allotment and transfer of securities:

- Ensuring fair and equitable allotment; and
- Promoting speedier and more efficient service in matters of allotment and transfer.

#### **2.2.4.3.1 Offices of the Registrar of Companies (ROC)**

Registrar of Companies (ROC) is the governing body for any institution registered under Company Act. In its governing role, it observes and regulates any company going into public examining whether the process of “going public” is in accordance with the rules and regulations set forth by the existing Company Act or not.

As per the Company Act 2063, public companies need to publish their prospectus before issuing securities to the public. Before publishing prospectus, one copy of the prospectus needs to be submitted to ROC. In this process, ROC approves the prospectus to be published. While approving the prospectus, ROC makes sure that important information is not missed out and unnecessary information is not mentioned. In the presence of such changes, ROC sends it back to the company for necessary changes. Upon satisfactory changes ROC grants approval to issuing company to issue the prospectus. Apart from approving the prospectus to be published by the issuing company before going into public, ROC does not play other major role. (Shrestha,2006:42)

#### **2.2.4.4 Stock Exchange Market**

Stock exchange has been defined as any body of individuals, whether incorporated or not, constituted for the purpose of assisting, regulating or controlling the business of buying and selling of or dealing in securities. The stock exchange therefore is the most important institution in the secondary market. In the primary market, it comes into play during primary share allotment, during issuing share in premium and when Securities Board asks Securities Exchange Market for its opinion.

Securities Exchange Act 2063 has stated that for the operation of the stock exchange market, approval needs to be taken from the Securities Exchange Board. Any registered institution except private companies willing to do or allow others to do security transaction should get approval for securities exchange market from the securities board.

After the issue of securities to the public, the Act requires that companies be listed in the Security Exchange Market before the floated shares can be traded in the market. Nepal Stock Exchange Limited (NEPSE) is the only stock exchange market in the country.

#### **2.2.4.5 Financial Institutions**

They are financial intermediaries like commercial banks, finance companies (merchant bankers), and development banks and cooperatives institutions. These institutions are established under the Company Act and Nepal Rastra Bank Directives. These financial

institutions perform the role of intermediaries in the securities issue as per the authority received from the Securities Exchange Board. Financial Institutions are involved in securities issue process as:

- Issue managers
- Underwriters

#### **2.2.4.6 Issue Manager**

Issue manager in the primary market carry out all the function related to public issuance of securities on behalf of the issuing company. Presently there are 9 issue managers in the market. Which are:

**Table 2.1**  
**Name of Issue Manager of Nepal**

S. No.	Name of Issue Manager
1	Ace Development Bank Limited
2	Citizen Investment Trust
3	NIDC Capital Markets Limited
4	Nepal Finance Limited
5	National Finance Company Limited
6	NMB Bank Limited
7	Nepal Sri Lanka Merchant Bank Limited
8	Nepal Share Markets and Finance Limited
9	Civil Capital Market Limited.
10	United Finance Limited
11	Elite Capital Limited
12	Nepal Housing and Merchant Finance Limited
13	Vibor Bikash Bank Limited
14	Development Credit Bank Limited
15	Tinau Bikash Bank Limited
16	Investment Management Merchant Banker Limited
17	Beed Investment Limited
18	Growmore Merchant Banker Ltd

*Sources: [www.sebonp.com](http://www.sebonp.com)*

#### **2.2.4.7 Underwriters**

Generally all commercial banks, finance companies and other financial institution can provide underwriting services and providing such services accordingly. But the public issue getting underwritten has become Herculean task. Almost banks, finance companies and financial institutions reluctant to underwrite the public issue of shares because they feel underwriting are risky business. This type of reluctant has been strengthened more by some development cases. On the other hands, these exit some anomaly in underwriting concept between New Company Act and securities exchange regulation. Company Act defines issue manager as underwriters a well. Secondly no acts and regulations clearly spells about the qualification to be an under writer that who can underwrite the public issue and who can not or whether banks finance companies and financial institution other that member of Nepal Stock Exchange can provide the underwriting ser vices that there is always deficient fund/resources to meet the demand of underwriting. Thirdly, because of the insufficient resources and despite of the reluctance of commercial banks (who have enormous resources), issue manager are somehow managing the consortium of underwriting. (Shrestha, 2006:59)

#### **2.2.4.8 Nepal Rastra Bank (NRB)**

Nepal Rastra Bank is the central banking authority in Nepal. It is the governing authority in setting guidelines to all the financial institution regarding its area of operation. But, in the case of public offerings, its involvement is very minimal. Its role in the issue process is only to grant financial institutions approval to be involved with different role in the issue process. Also for different fund based activities of merchant banking, approval needs to be taken from Nepal Rastra Bank.

### **2.3 Terms Involved in the Process of Initial Public Offerings of Common Stocks**

#### **2.3.1 Initial Public Offering (IPO)**

It is a process by which an institution raises desired capital through issuing of securities (common stock, preferred stock, bond, commercial paper and debentures) in the capital or money market for the first time.

For the purpose of public offerings, Company Act has specified that the public issue process of any public company should be managed through the institution receiving authority from SEB. Internationally, financial institutions with the merchant banking operations, manage the overall issue process of any public limited company. Such institution managing the overall process of the public offerings is termed as an issue manager.

### **2.3.2 Issue Manager**

Issue manager is the institution solely holding the responsibility of managing the public offerings of any issuing company. Securities Exchange Act, 2040 clause 18, has defined issue managers as institutions holding license from the Security Board to manage public offering process. The format of application letter and required information to be provided while registering for issue manager are given in the appendix.

### **2.3.3 Lead Manager**

In the event of more than one issue managers managing the issue of securities of any company, the term lead manager is used to identify the individual issue manager s. The existing Act and the Directives have not clearly identified the maximum number of lead managers managing securities issue of any company at the same time.

### **2.3.4 Underwriting**

Underwriting is an agreement between the issuing company and a financial institution like bank, merchant banker, broker or other person, providing for their taking up the shares or debentures to the extent specified in the agreement between them, if it is not subscribed by the public. The underwriting agreements ensure that the public issued is fully subscribed. The commission paid to the underwriters as consideration for the underwriting arrangement is known as underwriting commission.

### **2.3.5 Lead Underwriter**

Lead Underwriter is the one that arranges the whole underwriting process for the issuing company with the help of other sub-underwriters. The issuing companies and intermediaries should note that underwriting is a serious contractual arrangement having financial implications on the issuer and the underwriter. The business of underwriting, therefore, presupposes inherent financial strength on the part of the underwriters. In the process of identifying underwriters, therefore, issue manager must satisfy himself about the net worth of the underwriters and their outstanding commitments and disclose.

In the event that the issued shares are not fully subscribed by general public, the distribution of unsold share to the underwriters would be held on the pro- rata basis based on the number of shares committed by them to underwrite.

### **2.3.6 Underwriters or Sub-underwriters**

They are the smaller institution agreeing to underwrite fewer number shares. Underwriters and sub-underwriters work under the management of the lead underwriter. Their financial responsibility remains within the total amount of shares agreed by them to undertake.

### **2.3.7 Banker to the Issue**

Banker to the issue is normally a commercial bank, which provides the custodian service to the issuing company and keeps the subscription money. Banker to the issue may or may not receive applications from the investor s, issue acknowledgements for the same, and enter the application details in application schedules. It also involves in the process by realizing the proceeds of the cheques/draft and issue final certificates to the issue manager for the number of applications and amount collected. Issuing company in consultation with the issue managers makes the appointment of banker to the issue.

The banker to the issue generally comprises the consortium of bankers providing working capital finance to the company, the banks providing underwriting assistance for the issue, the bank associated with the issue managers and other banks which are regularly and efficiently handling public issue work.

### **2.3.8 Collection Centers**

Collection Centers are normally financial institutions such as banks, finance companies, brokerage houses etc. Collection centres receive applications from the investors, issue acknowledgements for the same, and enter the application details in application schedules. They also realize the proceeds of the cheques/drafts and issue final certificates to the issue manager for the number of applications and amount collected. The appointment of collection centres is made in consultation with the issue managers.

### **2.3.9 Prospectus**

The prospectus is defined as, “any document described or issued as a prospectus and includes any notice, circular advertisement or other document inviting deposits from the public or inviting offers from the public for the subscription or purchase of shares in, or debentures of, a body corporate.”

The Company Act 2063 has made mandatory that any public institution going into public offerings must issue the prospectus before issuing the securities to the public. According to the Act, before publishing for the public, the prospectus signed by the board of directors should be sent to and get approval from the Office of Registrar of the Companies and Securities Board. The requirement is made to make sure that the information provided to the public is as per requirement and is not manipulated to mislead the public. The prospectus published for the public should state in the publication the approval from the Office of Registrar of the Companies.

The Company Act 2063 has stated that matters referred in the prospectus are the liability and responsibility of company publishing it. Board of Directors signing the documents is answerable to the matters stated in the prospectus. In the event that,

company has knowingly published false statement in the prospectus and believing on which if securities has been purchased and loss incurred, such loss coverage would be the personal liability of the directors signing the prospectus.

In short, prospectus is a legal document containing important features of Article of Association, Memorandum of Association, and important decision taken by the board of the company affecting the future of the company and important conditions to be obeyed by the general applicants. The main purpose of the publishing prospectus is to inform public about the company and the issue. (Shrestha, 2006:62)

### **2.3.10 Budget for the Issue**

Budget for the issue is a tentative figure of expenses that is estimated to incur in the process of public offerings. The budget is to be born fully by the issuing company, if not, according to the understanding reached between issuing company and the issue manager.

### **2.3.11 Application Form**

It is a form provided to general public to apply for the issued securities by a company. The application for ms needs to be filled both in English and Nepali. It contains information about the company, issue of shares, and space for applicants to fill in for the buyers detail information.

Application form is the legal document that the investor provides to the company stating the number of shares of a company he/she is willing to accept. The applicants submitting the application for ms would imply that he/she has accepted the terms and conditions stated in the application form with the full knowledge about the matters refer red in the prospectus. Attached with the application form a photocopy of citizenship is collected as a proof to applicant's acceptance to terms and condition and a remedy to possible discrepancies in identification. In case of minor applicants, citizen certificate of parents or guardian is to be attached.

### **2.3.12 Bridge Financing**

It is a short term lending provided to the issuing company till the date of share allotment, backed by the collection from public issue. The company is to make the payment after receiving allocated shares money from public offerings. Normally financial institutions provide bridge loans to companies against their underwriting commitments. The said loans are adjusted against allotment of shares/debentures. The bridge finance is issued when Companies require meeting their immediate requirement of funds. If there is a substantial lead-time between making a public issue and commencement of commercial production. If issues is to be deferred to the most opportune time.

### **2.3.13 Memorandum of Understanding**

In the process of issuing securities to the public, besides issuing company, different intermediaries are involved. Memorandum of Understanding is the legal agreement made between issuing company and different intermediaries. This agreement states the terms and condition in respect to the function and authority of the involved parties.

Different MOU to be signed in the process of issue offerings are:

- MOU between issuing company and the issue manager/lead managers:  
This is required as the Company Act requires securities issue process of any public company is to be done through the registered issue manager. This legal agreement between issuing company and issue manager specifies terms and condition, responsibilities and the authorities of involved party.
- MOU between issue managers and the underwriters.
- MOU between issue manager and the bankers to the issue.
- MOU between issue manager and the collection centres.

### **2.3.14 Issue Commission**

It is the commission charged by the issue manager to the issuing company for the service it has provided. Issue commission is paid for issue management process. The responsibility of issue manager in the issue process, for which issue commission is to be charged as demarcated in the agreement itself. The commissions are normally set as per the negotiation.

### **2.3.15 Underwriting Commission**

Underwriting commission is the amount charged by the underwriters for underwriting the securities issued. The commissions are normally determined as per the negotiation.

### **2.3.16 Collection Charges**

Collection charges are the amount charged by the collection centres for collecting the application forms and other documentation process. The collection charges are also charged on percentage of the amount collected. The percentage charged also depends upon the negotiation between issue manager on behalf of issuing company and the collection centres.

### **2.3.17 Refund Charges**

Refund charges are the amount charged by the collection centres for refunding the oversubscribed money to the general investors. The refund charges are charged on percentage of the total amount refunded. The percentage charged depends upon the negotiation between issue manager on behalf of issuing company and the collection centres.

### **2.3.18 Fix Charges to the Collection Centres – Finance Companies**

It is a fix charged given to the collection centres like finance companies for making required preparation for collecting application from the investors and conducting other required activities. The fix charge amount provided to the collection centres is also based on the negotiation.

### **2.3.19 Pre Issue and Post Issue**

Pre-issue in the issue process is defined from the point of approach by the issue manager to the prospective issuing company to the point of allotment of securities and refund of oversubscribed money to the investors. This segregation has been made on the basis of Company Act, as it requires that the process of securities issue, allotment of securities, collection of subscription needs to be done through institutions approved to carry out issue management.

### **2.4 Report on Public Issue Approval**

A total of 64 public limited companies raised funds amounting to Rs.10, 668.2 million by issuing securities in the fiscal year 2007/08. In the fiscal year 2006/07, a total of 34 public limited companies have raised funds amounting to Rs.2, 295.5 million.

In the last fiscal year, total listed companies in Nepal Stock Exchange Ltd. were 135 which reached to be 150 in the fiscal year 2007/08. In the fiscal year 2007/08, the turnover increased by 172.98 percent to be Rs.22, 820.8 millions compared to turnover of Rs.8, 360.1 million in the fiscal year 2006/07.

In the fiscal year 2007/08, the market capitalization of the listed companies increased by 96.59 percent to be Rs.3,66,247.5 million as compared to market capitalization of Rs.18,630.13 million in the fiscal year 2006/07. In the Fiscal year 2007/08 the preliminary estimate of the contribution of market capitalization to the GDP is 44.62 percent.

### **2.5 Course of Action during IPO**

#### **2.5.1 Preparing the Registration Statement**

Immediately following, and in some cases preceding, the kick-off meeting, the company and its counsel will begin work drafting the registration statement. In a public offering, both the content and form of an issuer's registration statement must strictly comply with SEC rules. In most IPOs, the issuer is required to file its registration statement on Form S-1. In fact, Form S-1 is not a "form" which a company fills out, but

rather a list of items of information which the company must include in the registration statement. Each of these items references a rule in SEC Regulation S-K (or Regulation S-X in the case of financial information) which provides in detail the amount and format of the information to be provided.

A registration statement on Form S-1 consists of two parts, which will be bound together in a single book and filed with the SEC as a public document. Part I is the information that must be included in the prospectus, the actual offering document to be distributed to potential investors after the filing of the registration statement. Part II, which is filed with the SEC and made publicly available but is not required to be distributed to offerees, contains supplemental information, including, as exhibits, the underwriting agreement, the company's charter and by-laws, and all contracts to which the company is a party that could materially influence a potential investor's decision as to whether to purchase the securities being offered. The company can seek to redact from such contracts those limited provisions which it feels contain confidential business information by blacking them out of the filing and submitting separately to the SEC an application for confidential treatment which explains how the company could be harmed by disclosure of such information. Part II also contains the signature page to the registration statement, to be signed by the company's principal executive, financial and accounting officers as well as by at least a majority of its directors.

The prospectus serves two important roles. First, it is a selling document intended to present investment in the company as an exciting opportunity. As such, it should be well written and visually pleasing. The underwriters generally have strict guidelines as to form and style, which they will communicate to the financial printer. The underwriters will occasionally prohibit the distribution of a prospectus if they find it deviates from such guidelines, so it is important to ensure that the printer has received and reviewed the managing underwriter's instructions.

Second, the prospectus is a disclosure document which must make complete and accurate disclosure of all material information about the company and the offering to protect the company from claims by investors. As such, the company's and

underwriter's counsel will spend considerable time ensuring that the prospectus sets forth in proper order and format all such information, both through continuous review of the SEC rules as well as through an ongoing business, legal and accounting due diligence investigation of the company.

The prospectus is generally organized as follows:

- The Prospectus Summary, which contains a short description of the company, its business, the offering and summary financial data.
- Risk Factors, which identify and describe risks associated with an investment in the company.
- Use of Proceeds, which discusses what the funds will be used for.
- Selected Financial Data, which presents selected income statement and balance sheet data.
- Management's Discussion and Analysis of Financial Condition and Results of Operation, in which management discusses material line items in the Selected Financial Data section and why certain changes have occurred over the years reported. Management should also fully disclose known trends or uncertainties that could materially affect future financial conditions.
- Business, which provides an overview of the company's business and is broken down into subheadings such as "Industry", "Products", "Marketing and Distribution", "Research and Development", "Manufacturing", "Competition", "Intellectual Property Matters", "Litigation", "Human Resources", "Facilities", etc. This section is the central part of the prospectus. It is generally the first section to be drafted and is continuously reworked and revised until filing and again, through amendments, until the registration statement is declared effective.
- Management, which lists the company's directors and executive officers and then sets forth in detail compensation paid to its chief executive officer and its four other most highly compensated executives.

- Certain transactions, which sets forth transactions, including the private placement of securities, involving the company and its officers, directors and controlling stockholders.
- Principal Stockholders, which sets forth the equity holdings of the company's controlling stockholders, directors and executive officers.
- Description of Capital Stock, which describes the relative preferences and privileges of the different classes of the company's capital stock upon completion of the IPO. If the company has adopted the anti-takeover measures referenced above, they will be disclosed in this section.
- Shares eligible for future sale, which discloses the number of shares, held by existing shareholders, which will be eligible for resale after the IPO pursuant to SEC Rules, and the timing of such eligibility. This provision will also disclose any registration rights that the existing shareholders may be contractually entitled to. Under writing, this describes the terms of the underwriting agreement.
- Additional Information, which explains that the prospectus is only part of the registration statement and how to obtain from the SEC.
- Financial Statements, which provide two years of audited balance sheet data and three years of audited income statement, cash flow, and stockholders' equity data, and unedited data for any subsequent interim period and the comparable period of the prior year.

The working group will continuously meet to revise the prospectus at drafting sessions which generally take place at the offices of company counsel. Once the group feels that the prospectus is close to being final, company counsel will send it to the financial printer on computer disk, where it will be professionally type- set. Prior to filing, the working group will meet, possibly several times, at the printer for final revisions.

### **2.5.2 Liabilities and Due Diligence**

Each participant involved in the preparation of the registration statement can be held personally liable for any material misstatements or omissions in the prospectus. The liability can be severe, including complete restitution of the proceeds from the offering to the investors. While the company is held strictly liable for such misstatements or omissions, the underwriters and individual company directors and officers may raise a "due diligence defence". That is, if the participants can prove that they made a thorough review of every relevant aspect of the company and still could not have known of the inaccuracy, they will not be held liable. Consequently, a considerable amount of time is spent by each member of the working group, but particularly by company counsel and underwriters' counsel, interviewing company management, requesting production of all corporate documents and material contracts, and reviewing and determining which of these documents are material and need to be disclosed. This process continues up until the final amendment to the registration statement is filed.

### **2.5.3 The Registration Process**

Once the working group has completed the registration statement and compiled all of the exhibits, company counsel will instruct the financial printer to deliver the appropriate number of copies to the SEC. The filing occurs upon receipt of the registration statement by the SEC. At the same time that the registration statement is filed, company counsel will also file the request for confidential treatment.

The registration statement will be assigned to a branch of the SEC's Division of Corporation Finance upon receipt, where two examiners will be appointed to review it, one to focus on financial information and the other on non-financial information. Usually within 30 to 35 days, the SEC will send a letter to the company containing its comments to the registration statement, the so-called "comment letter". Generally, each of the comments must be addressed through amendment of the registration statement or the provision of a written explanation as to why an amendment is not necessary. Company counsel generally calls the examiner to discuss the comments before responding. Once each of the comments have either been addressed or waived, the

amended registration statement is filed with a cover letter explaining the revisions with cross references to the comment letter. Quite often, the SEC will send a follow up comment letter stating which of the initial comments it feels have not yet been properly resolved and, less frequently, containing additional comments.

Usually, prior to receiving comments from the SEC, the preliminary prospectus is printed in quantity for distribution by the underwriters. Occasionally, the quantity printing is delayed either for new financial results to be included or to receive initial SEC comments.

#### **2.5.4 The "Red Herring" and the "Road Show"**

As discussed above, after filing the registration statement, the company and its underwriters may make oral offers, other than by use of mass media. Written offers may only be made through the use of the preliminary prospectus, which is often referred to as the "red herring", because it contains on its cover a legend printed in red stating that offers to buy may not be accepted nor sales made prior to the effectiveness of the registration statement.

The company will generally launch its marketing campaign with a press release which is limited in content pursuant to SEC permits the use of press releases which briefly describe the offering and the company, name the underwriters and indicate where prospectuses may be obtained.

After the press release, the company and lead underwriters travel to major cities to present the company and its business to potential investors and members of the underwriting syndicate. These presentations are referred to as the "road show" or the "dog and pony show". The company's management may also schedule face to face interviews with potential large investors at this time.

#### **2.5.5 The Underwriting Agreement**

Prior to filing the registration statement, the managing underwriter will present the company with its form of underwriting agreement. The underwriting agreement sets forth the relationship and the legal obligations between the company, the

underwriters and the selling stockholders (if any), such as (i) the obligation of the underwriters to buy the shares at a specified discount, (ii) the obligation of the company to reimburse the underwriter for certain expenses, (iii) representations and warranties of the company, (iv) covenants of the company, (v) conditions to closing, (vi) indemnification provisions covering liability for material misstatements or omissions in the registration statement and (vii) occurrences which will allow the underwriter to back out of the deal prior to closing, such as wars, stock market crashes or, in some agreements, major adverse effects to the company's business. As discussed above, the underwriting agreement is not signed until after SEC clearance and the completion of the "road show."

The underwriting agreement will generally grant the underwriter an option to purchase an additional number of shares (usually 15% of what is being offered) in order to satisfy sales of shares by the underwriter in excess of the number of shares being offered, which are referred to as "over-allotments" or the "green shoe." Over-allotments are good for the after-market of the company's stock as they create increased demand for the shares. The underwriter is generally allowed to exercise this option until thirty days after the closing.

When the final underwriting agreement is signed, it will provide the date of the closing of the sale of the shares to the underwriters, which is generally three days after the agreement, is executed.

#### **2.5.6 Request for Acceleration**

At least two days before trading commences, the company and the underwriters must provide the SEC with acceleration requests, asking the SEC to accelerate the effective date.

#### **2.5.7 Pricing and Effectiveness**

Promptly after the road show is concluded and the registration statement declared effective by the SEC (usually the same day), but prior to signing the underwriting agreement, the company and the underwriters will meet to negotiate the price of the

shares. The company will be represented by a pricing committee, which will have been appointed by the board of directors, and certain members of the underwriting syndicate may participate as well. As discussed above, the underwriters and the company will have generally agreed to a range of prices as early as the kick-off meeting, so the final price should not come as a surprise to anyone. Generally, the underwriters will push for a lower price than the company's pricing committee, as they will want a good reception and a strong immediate after-market for the shares. Except for when the market is particularly favorable, the underwriters generally prevail in this negotiation.

The night after the pricing, members of the working group will then visit the printer once again to add the pricing information to the final prospectus. The final prospectus is then filed with the SEC and printed in quantity for distribution by the underwriters to the purchasers.

### **2.5.8 Closing**

As soon as the final prospectus has been disseminated, orders for the shares are accepted by the underwriters. Trading begins on the morning following effectiveness of the registration statement in anticipation of the closing. The closing is the date on which payment is made for the shares. The SEC requires the settlement of the IPO within three business days of the pricing.

A variety of closing deliveries are required under the underwriting agreement, including counsel opinions and accountant comfort letters. The day before the closing, company counsel and underwriter's counsel will generally meet for a "pre-closing", where they will review the closing documents.

The closing generally occurs in the morning by conference call between company counsel, underwriter's counsel and the company's new transfer agent. The company counsel will confirm that it has received a check or wire transfer from the underwriters for the offering price less discount and that it considers all of the conditions to closing to have been met. Underwriters' counsel will confirm that it too considers all of the conditions to closing to have been met. The transfer agent will then

declare the IPO closed and release the stock certificates per the instructions of the underwriters. If the underwriters have elected to exercise the green shoe options, the over-allotment shares will be included at this closing; otherwise, they will be purchased at a subsequent closing.

## **2.6 Review of Related Studies**

This section of the study draws excerpts from International articles, Nepalese journal articles along with Masters Degree Thesis. International journals have been accessed through the different websites and newspapers. Similarly, Nepalese journals and Masters Degree thesis have been accessed from Library of Tribhuvan University Central Library and SEBON Library.

Large number of research work has been carried out elucidating different aspects of IPO's throughout the globe. However, only those works, which were accessible and considered relevant to this study have been included and excerpted below:

Paul ,(1960) carried out a study of international capital market which the American economic review has pleaded that the development of world capital market appears to be reaching the state where they can make significantly greater contribution to world economic growth and trade. More importantly, the groundwork has been laid for the healthy development and future growth of international capital markets. Barring the intervention of war or other major disturbances, world capital market give promise of being able to play and increasingly important, through no predominant role in the movement of capital internationally.

Lowry and Schuvert (2002), carried out a study on, IPO Market Cycles: Bubbles or Sequential Learning? The study emphasized that both IPO volume and average initial returns are highly correlated. Furthermore, companies tend to go public following periods of high initial returns. The study revealed that there exist significant positive relation between average initial returns and subsequent IPO volumes. They concluded with the result, which showed that the dynamic behavior of initial returns and IPO issued is a complicated function of many

factors. There are significant biases in IPO offer prices and arise from underwriters not fully incorporating all avoidable information when they set offer prices. These biases affect both the serial correlation in initial returns and the lead-lag relation between initial returns and IPO volumes. They also found that the serial correlation in initial returns is predominantly driven by information learned during the registration periods of recent IPOs but only partially incorporated into the registration periods of recent IPOs but only partially incorporated into the offer price. Furthermore, they found that information learned during the registration period that is positively related to further IPO volumes. Investment bankers learning processes throughout this registration period causes monthly aggregate initial returns to be autocorrelated and to be positively related to future levels of IPO activity.

Baru and Fawcett (2006), carried out a study on Initial Public Offerings; An Analysis of Theory and Practice. The study intended to extend the IPO literature by analyzing unique data from surveys of Chief Financial Officers (CFOs) to compare CFO perspectives to prevailing academic theory. Specifically, they examined the following seven issues; motivations for going public, timing of the IPOs, underwriter selection underpricing, signaling IPO process issues and the decision to stay private. In this regard, they surveyed three subsamples of firms, namely those that successfully completed an IPO, those that began the process but chose to withdraw the issue and those that are large enough to go public, but have not attempted an IPO. They surveyed 330 CFOs and their survey process followed Dillman's (1978) total design method, which is a standard for conducting academic surveys. Their findings are summarized as: The most important motivation for going public is to create public shares for use in future acquisitions. Insiders are opportunistic especially at VC-backed firms. They seek to go public at a time that portends a high stock price. The underwriter selection process is driven by a very small set of selection criteria namely underwriter reputation and IPO process expertise. CFOs attribute most underpricing to market uncertainty and the need to reward investors for taking the risk of IPO. The most important positive

signal is past historical earnings, this may promote window dressing. CFOs strongly prefer firm – commitment underwriting. Companies remain private to preserve decision-making control ownership.

Simha, (1960) carried out a study on capital market in his book the Capital Market in India has observed that capital is an extremely fascinating subject and efficient capital market is an indispensable prerequisite to economic development. In fact, even as regards the resources for the public sector, the capital market has a rather important role to play.

### **2.6.1 Review of Nepali studies**

Shrestha, (2002) has analyzed why the share market is inactive and what are the main causes for inactiveness and what measures should be done etc are carefully defined. Similarly, how the securities frauds and manipulation have occurred and to what extent they can be overcome would be highlighted here to draw adequate feedback to the regulating and controlling authorities to devise suitable laws to prevent such frauds and minimize manipulation in share price. The Performance of Nepalese IPO.

Dahal, (2007) in his article published in the Sebon journal, the paper assesses the performance of Nepalese IPOs and relates them to potential factors. The study finds that the Nepalese IPOs are heavily oversubscribed and provide the investors with the market adjusted excess rate of return leading to the conclusion that Nepalese IPOs are under priced too.

The leading business journals like "The Boss" magazine, "The New Business Age" and "Aaja Ko Abhiyan" have been used during the study. The different writer's different views, the primary market scenario i.e., current scenario has been discussed among the group members during the research. The websites have been used instead of journal of different organizations. Like for the knowledge of government securities, NRB website, for other information SEBON website and different world leading management websites have been used.

Prior this, quite a few research has been carried out by various scholars covering

different aspects of capital market. Yet there is dearth of research study in the area of IPO. However, few research studies that are considered relevant and accessible during study period have been excerpted below:

Adhikari (2005), has conducted a research on Under Pricing in Nepal. The basic objective of the study was to analyze the under Pricing of IPOs in the context of Nepal. Beside the study also examined the trends of Public offering market and process of going public in Nepal. For purpose of study data of the periods of 4 years from 1999/00 to 2003/04 were used. The researcher concluded that under -pricing does not occur among Nepalese firms. The researcher also added that the result is not consistent with theory and different finding of empirical studies conducted in different countries. IPO s market in Nepal does not enjoy any right to set the price of their issue. The price setting process is totally controlled by the regulatory body. Because of this reasons, Nepalese merchant banker could not play any role to influence the offer price of IPO s.

Mahat (2007) Conducted research on the topic of Future prospect of NEPSE in capital mobilization is able to analyzed situation in Nepal where the industrial sector has very little access to private saving. Also he indicates the availability of industrial securities is nearly absent and the development of financial institutions that link the surplus spending units with the deficit spending ones is in the rudimentary stage.

He further concluded notwithstanding the underdevelopment state of financial institution in the country, growth of invest able funds becoming available recent years. This study also demonstrated the relatively very limited financial contribution of other financial institution to this sector but he does not indicate these factors, which help to uplift the financial contribution to the other sectors like provident fund and NIC etc.

It is acknowledged that a much greater use of resources available in the financial system of the industrial development of the country may not be very smooth and easy. He only specified the growth and potential (measures) of security market, capital market regarding primary and secondary market. It was absent to show the problems

face by the NIDC and other industrial as well as financial sectors. He just shows the preliminary and basic problems of industrial sector but not in broad way. His topic was “future prospects of NEPSE in capital mobilization” but according to the topic the sufficient future prospects/measures are not available in this study but can find thin basic context. There is not indication in the relations of primary and secondary market with economic condition of country in his study. But it is able to give the theoretical version of relationship of capital market with economic growth.

The findings on the term nature of sources and uses of funds and the current ratios of various size and industry groups also do not give any ground for complacency. Some industries were found to have financed a large part of the increase in current assets with the long-term sources of funds, while for others the increase in long-term source was hardly sufficient even to finance the long-term assets formations. He was given high attention to the working capital management in Nepalese industries

Pandey (2008) Conducted research on the topic of Public response to Primary Issue of Shares in Nepal with the objective of: identify the problems of primary share issue market, assess the growth of primary issue market, analyze the pattern of public response to shares & find the reasons of variation. He has summarized the finding as: Public response in primary market is high due to lack of opportunities for investment in other fields. No proper investment analysis is been made. Despite this, public are attracted towards shares than other sectors, basically to increase their value of investment, be it dividend capital gain or bonus shares. It can be seen that public response to primary issues on Banking and Financial sectors is normally higher than that of the manufacturing and services sector. Major causes for poor response in the period 1995-1998 were; interest rates were higher as compared to dividend yield, the public companies were not performing well and people did not know about the importance of investing securities. Now the response is highly positive because people are aware, money flow in the market is higher, people have seen that most companies are distributing dividends, share prices are increasing for most companies and a lack of better alternatives for investment. Now that the average interest rates have gone down, more can be obtained from investment in stock.

Bhattarai (2006), has performed a study on, Public Response to Initial Public Offering in Nepal, with the basic objective of assessing public response to the initial public offering. However, the study also focused on the dealing process and pace of the IPO. The study has used both primary and secondary data. Primary data collected through direct questionnaires provided to the general investor while secondary data were collected from various publications of SEBON, NEPSE and other institutions. The study concluded that most of the general investors in Nepal do not have significant information regarding the primary market but still they are very much interested to invest money in the primary market. It also found that almost each sector was getting good response from public. Specially, financial institutions and insurance companies were becoming more preferable for public than the other non-financial sectors.

Bhandari (2009) studied Structure and Efficiency of Securities Market Intermediation Service in Nepal. In Nepalese context very few studies have been done by the individual researcher in this topic. He tried to find out the efficiency of securities market inter mediation service in Nepalese Securities Market. The major finding of his study are, with the elapse of time, there are a lot of changes in structure of intermediaries. The total number of intermediaries is in decreasing trend over his study period and the mixture of market intermediaries are often changing. He considered ten years data for the study. Number of listed companies, traded companies, paid-up capital, market capital and NEPSE index are increasing during his study periods, besides some exception. These indicators show the increasing efficiency in comparison with the earlier year. Similarly, number of permitted brokers during the study periods was decreasing. Some of the brokers hold license only but not submitted financial and transaction reports to NEPSE on time. Other sector of Nepalese economy have not moving except capital market in the later days, there is abnormal development in capital market only. The high proportion of the investor was not satisfied with issue manager/under writing service available. On the other hand, the market makers are not existed from 2002/03 to onwards. The main reason for the failure of the markets

was the inability of the market makers to acquire a sufficient buffer stock of shares initially required by them for market making and introduced very initial stage of the security market. Overall his study's conclusion is that the structure of the securities market is not well defined as lack of adequate mixture of all typical market. Securities markets intermediation service is inefficient. But, interesting things is that amount and volume of share transaction, paid-up capital, market capitalization, and NEPSE index all are in increasing trends. Nepalese Security market is small in quantity and poor in quality as compared to other develop stock market.

## **2.7 Research Gap**

Even though numerous studies have been carried out in different part of the world covering different aspects of securities market, stock trading mechanism and stock pricing behaviors etc. including public response in primary issue of different securities. But there is still lack of research in the field of Initial Public Offering to the stock investment Few studies have analyzed existing state of IPO s in Nepal. However, none of the studies has been able to portray the complete picture of IPO s and their practices in Nepal. This study tries to understand the pace of initial public offering, investor response, procedures, rules, regulations and provisions as well as public awareness about it. This study will be helpful to public companies (new and existing), issue manager, underwriter, investor, government organizations, general public, researcher and other parties related to IPO (Primary issue of different securities).

## **CHAPTER III**

### **RESEARCH METHODOLOGY**

Research methodology describes the methods and process applied in the entire aspect of the study. In other words research methodology is a systematized way to solve the research problem. Research methodology refers to the various sequential steps (along with a rationale, of each step) to be adopted by a researcher in studying a problem with certain object in view. A focus is given to research design, sample selection and size, data collection procedure, data processing, definition of variables, meaning and definition of statistical tools used. This chapter highlights the research methodology used for the study.

#### **3.1 Research Design**

A research design is plan structure and strategy to obtain and strategy to obtain the objectives of the study. The research design used in this study is both descriptive and analytical. The analytical research design is used to access and analyze practices of IPO in use, public response to IPO of commercial banks in the process of IPO and few problems and projects regarding IPO and exploratory design find out necessary suggestions or recommendations for strengthening the capabilities and escaping and efficiency of issuer, underwriters and investors.

The study is based on descriptive and analytical research design. Analytical research design has been used to analyze existing state of IPO in Nepal using long-live model and simple statistical tools.

#### **3.2 Population and Sample**

Number of companies listed in Nepal Stock Exchange (NEPSE) by the end of F/Y 2011/12 has reached 260 and these companies are divided into 8 sectors which include commercial banks, development banks, finance companies, insurance companies, manufacturing and processing companies, trading houses, hotel and others. However, the study it focuses on only those

companies which have gone for IPO during the period of F/Y 2006/07 to F/Y 2011/12. Moreover, only those companies included in 5 sectors: commercial banks, development banks, finance companies, insurance companies and manufacturing and processing companies, have been selected and rest 3 sectors have been excluded as their numbers became small after considering above mentioned time frame of the study. Hence, the population of the study is 259 listed companies representing 5 different sectors in NEPSE. Similarly, even though IPO could be of debt or equity security the study has focused on IPO of common shares only. Also, during analyzing the existing state of IPO's in Nepal, the offers (amount and numbers of issues) from collective schemes like fund and citizen investment trust have not been considered.

As far as sampling is considered, stratified random sampling techniques have been used to ensure that each and every company, representing different sectors had fair chance of being selected. In this study random sampling tables had been used within the sample frame of 25%.

### **3.3 Sources and Nature of Data**

As per nature of the study, the study is based on primary and secondary data as well. The major sources of data used in thus study are:-

- Annual reports of SEBON, to analyze existing state of IPO's Nepal.
- Trading reports of NEPSE to reveal share price information needed during analysis of under-pricing.
- Newspapers especially The Kathmandu Post Daily, The Raising Nepal Daily and Arthik Weekly covering different periods of time to reveal share price information needed during analysis of under-pricing.
- Acts and regulations governing security market and IPO issues that mainly included security act, 2063, security regulation and issue approval guidelines, 2000.

### **3.4 Data Collection Techniques**

Annual reports covering different fiscal years of SEBON were collected its head office at Thapathali. Similarly, trading reports of NEPSE were retrieved from its head office at Durbar Marga. Daily newspaper like The Kathmandu Post and Rising Nepal were access from central library of and weekly newspaper Arthik Abhiyan and business plus were bought myself. Acts and regulatory information's were obtained from law as well as official website of SEBON.

### **3.5 Data Processing**

At first data were extracted from above mentioned sources and recorded in the master sheet. The data were often then entered into the spreadsheet to present them into appropriate tables and figures with aid of computer programmers like Microsoft word. Final, Microsoft excel was run to analyze data revealing existing state of IPO's in Nepal pricing while sophisticated computer program like spas was run to obtain the growth rate of issued amount, average size of issue offered and amount of issue offered from financial and non-financial sector.

### **3.6 Data Analysis Tools**

In the study, different statistical tools and various models have been used to analyze the data and reach the meaningful results, which are described below:

#### **36.1 Multiple Bar-Diagrams and Graphs**

Diagrams and graphs are visual aids which give a bird's eye view of a set of numerical data which show the information in a way that enables us to make comparison between two or more than two sets of data. Diagrams are in different type. Out of these various types of diagram one of the most important from of diagram presentation of data is multiple bar diagrams which is used in cause where multiple characteristics of the same of data have to be presented and compared.

### 3.6.2 Pie-Diagram

A pie-diagram is a widely used aid that is generally used for diagrammatic presentation of the values differing widely in magnitude. In these methods all the given data are converted into 360 degree and all components of the data are presented in terms of angles that total 360 degree for one set of data.

### 3.6.3 Percentage

Percentage is one of the most useful tools for the companies of two qualities or variables. Simply, the word percentage means per hundred. In other, the fraction with 100 as its denominator is known as a percentage and the numerator of these fractions is rate percent.

### 3.6.4 Model for Measuring Growth Rates

Simple arithmetic mean is the values of all the elements in the sample and divides by the number of elements in the sample.

This growth has been used to calculate the growth rates of amount of issues offered, divides size of issues offered and the amount of issue offered from finance and non- finance sector during the study period. As per model,  $(1+g)^n = (1+g)^1 (1+g)^2 (1+g)^3 \dots (1+g)^n$

Where,

n=Number of years

g=Compound growth rate

g1=Annual growth rate of FY 2006/07

g2=Annual growth rate of FY 2007/08

g3=Annual growth rate of FY 2008/09

Compound growth is calculated by using the above formula and finally multiplying the obtained value by 100. Weighted average growth rate gives the growth at a point in time whereas compound growth rate gives the growth rate over the period.

### **3.7 Limitation of the Methodology**

Availability of data is a major concern. NEPSE is the sole authority to release data needed for analysis in this study but has not been able to provide them all. So the major portion of analysis especially stock price information has been based on daily newspapers and subsequently bounded to be influenced by their quality of presentation. The unavailability of data has also forced to limit the time frame of study into FY 2006/07 to FY 2011/12. The study has used stratified random sampling and descriptive and analytical research design, hence is subjected to their inherent biases.

- The study, lack of the sufficient time resources are the major limitations of the study since the study has been conducted for fulfilling the partial requirement of MBS course of T.U Nepal.
- This study has analyzed and evaluated the data from limited sources and data.
- This study is mostly based on secondary data. So, the accuracy of research depends upon the reliability of data.
- Only a few companies from financial and non- financial sector are considered for the study.
- The study heavily focuses on the initial public offering and current legal aspects associated their in.
- The study has not covered recent changes because of limitation of data
- Variations of data in itself are also found when comparing with different sources.
- The information regarding the same questionnaire is different from different sources.
- Due to the difficulties of availability of the data, only ordinary and simple techniques have been used for the analysis.

## **CHAPTER-IV**

### **DATA PRESENTATION & ANALYSIS**

This chapter includes presentation of data and analysis of data reach at a conclusion. The primary data are used to analyze the public awareness, response, expectation, choice for investment etc. The secondary data are used to analyze the public response to the initial public offering per year and, growth of public offering and the behavior of general investors. The collected data are tested through suitable statistical tool. Collected data have been analyzed as in percentage, simple average. The purpose of the analysis is to achieve the objectives set in the chapter one.

#### **4.1 Amount of Public Issues Offered**

Securities Act, 2063 provisional that any company which goes for IPO must get issue approval SEBON prior to make their to public. Since, first year of SEBON's operation: FY 1993/94, it has given issue approval to 260 issues amounting Rs.79,356 million till 2011/12 (SEBON, 2009, Nov 09). As securities regulation also provisioned that the company, which got issue approval, may commit their offer any time within two months from the date of approval (security and issue approval guidelines, 2002), the amount of issue approved and the actual amount issued in fiscal year, may vary. Hence, for better result the study is focused on actual amount issued in the fiscal year rather than the amount approved by the SEBON in fiscal year. Amount of public issues offered during the study period with its growth rates have been in table 4.1.

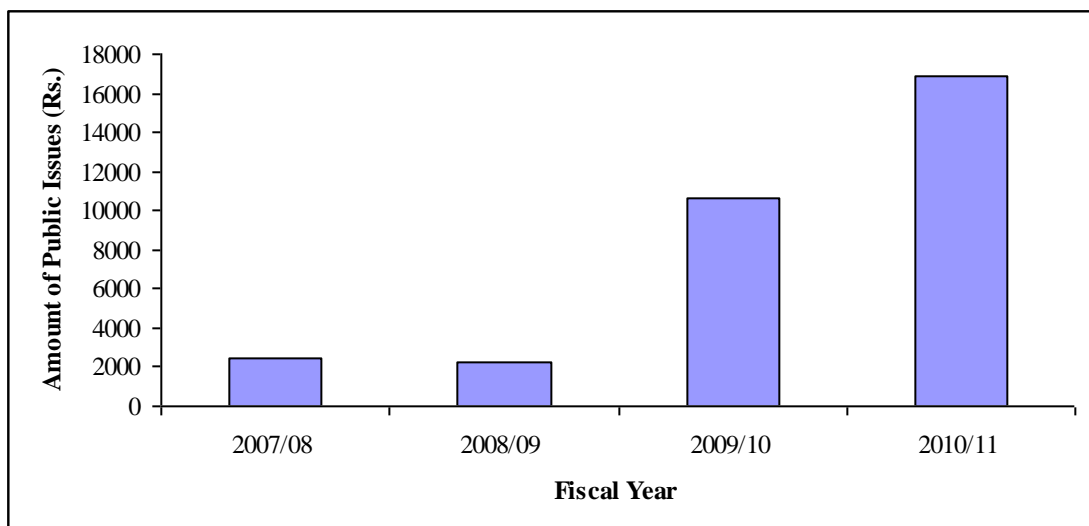
**Table: 4.1**  
**Amount of Public Issues Offered**

<b>FY</b>	<b>Amount of Public Issues (Rs. in Million)</b>	<b>Annual Growth Rate (%)</b>
2007/08	2443.3	50.19
2008/09	2295.6	-6.05
2009/10	10668.2	334.23
2010/11	16828.51	57.74
2011/12	10822.41	35.69

Source: SEBON Report

As shown in table 4.1 and figure 4.1, since first year of SEBON’s operation the amount of public issue has been never been in consistent trend. In the FY 2007/08 issues worth was Rs.2443.30 million were offered to public, Rs.2295.60 million in FY 2008/09. Heavily rises to Rs. 10668.20 in FY 2009/10 and also rises to Rs. 16828.51 in FY 2010/11. But in FY 2011/12 it is drop to Rs. 10822.41. During the study period the highest amount of public issue was Rs. 16828.51 million in the FY 2010/11 while the lowest amount of public issue was Rs. 2295.60 million in the FY 2008/09.

**Figure: 4.1**  
**Amount of Public Issues**



## 4.2 Number of Public Issues Offered

The number of public offering enables to identify the number of offers made by various listed and to be listed companies to the general public in each fiscal year. Table 4.2 revealed the number of issues offered in each fiscal year during the period.

Likewise, the amount of public issue, the number of issues offered in fiscal year also had not shown any consistent trend over the study period. During the entire study period the lowest number of issue offered in a year were 5, on two fiscal year 2007/08 and 2008/09.

The highest number of issues in the fiscal year was in the fiscal year of the study period, FY 2010/11.

**Table: 4.2**  
**Number of Public Issue**

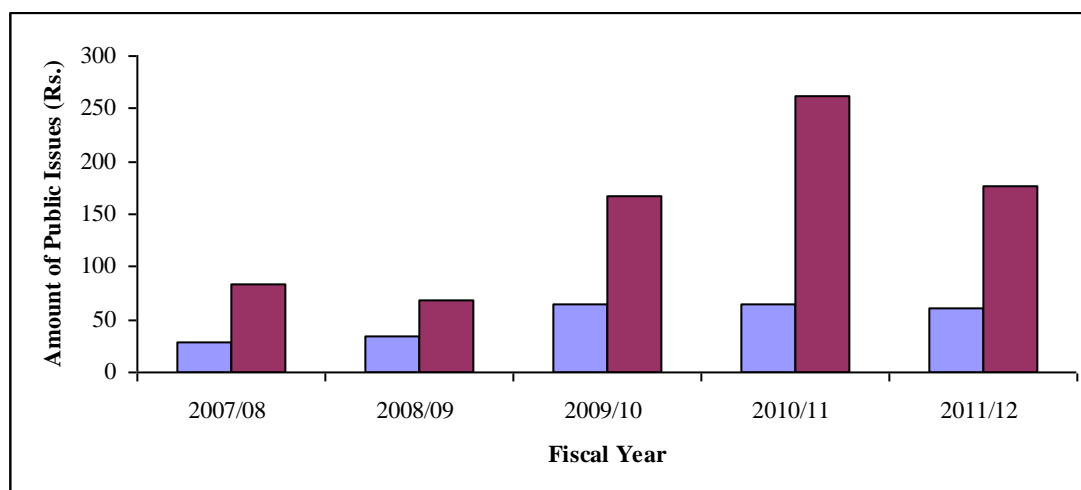
<b>Fiscal Year</b>	<b>Amount (Rs. in millions)</b>	<b>No. of Issue</b>	<b>Average Size (Rs. in million)</b>	<b>Annual Growth Rate (%)</b>
2007/08	2443.3	29	84.25	27.5
2008/09	2295.6	34	67.52	-19.86
2009/10	1668.2	64	166.7	146.89
2010/11	16828.51	64	262.95	57.74
2011/12	10822.41	61	177.42	-35.69

Source: SEBON Report

The table no 4.2 and figure no 4.2 shows that the number of public issues offered and average size of during the study period has been in growing trend till FY 2010/11 but in FY 2011/12 it is decreased. The highest amount of average size is 262.95 in fiscal year 2010/11 and the lowest is Rs 67.52 in 2008/09.

**Figure: 4.2**

**Number of Public Issue and Average Size**



**4.3 Publicly Issued Companies**

As per requirement of NEPSE, issuing companies should list their issues in NEPSE for following such issues to be traded on its trading floor. Since opening of NEPSE in 1993/94, 176 companies have already been listed till the end of 2011/12. The total paid up capital of these companies amounted to Rs. 79,356 million. The most instigating aspect of this total paid up capital is the contribution from financial sector that includes commercial from table 4.3.

**Table: 4.3**

**Publicly Issued Company**

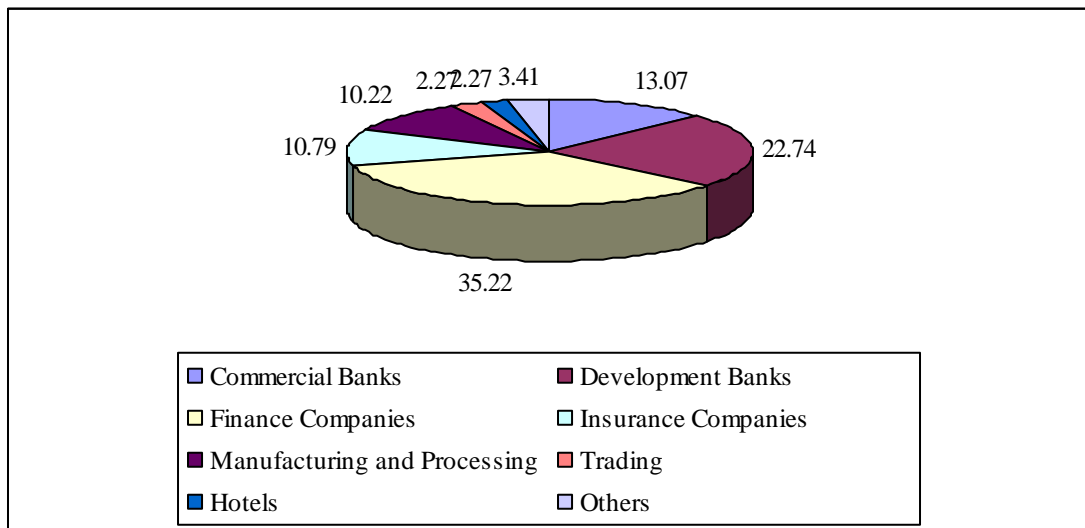
S. No.	Sector	No. of Co.	Percent	Paid up value (Rs.)	Percent
2	Commercial Banks	23	13.07	32900.6	41.46
3	Development Banks	40	22.74	10027.1	12.64
4	Finance Companies	62	35.22	11466.4	14.45
5	Insurance Companies	19	10.79	2432.94	3.07
6	Manufacturing and Processing	18	10.22	2539.74	3.2
7	Trading	4	2.27	82.18	0.1
8	Hotels	4	2.27	1580.71	1.99
9	Others	6	3.41	18327	23.09
	Total	176	100	79356.7	100

Source: SEBON Report

As shown in table 4.3 and figure 4.3 out of 176 listed companies belong to financial sector, which is about 81.82% of the total listed companies in paid-up value perspective commercial banks occupies 41.46%, development banks have 12.64%, finance companies accounts for 14.45% and insurance companies have 3.07% of the total paid-up value. Together as financial sector, they account paid-up value.

On the other manufacturing and processing sector, despite being second (in terms of no. of listed companies) accounts for only 3.20%. Similarly, trading, hotel and others account for 1.99%, 0.10% and 23.09% of the total paid-up value respectively. Together as non-financial sector, they accounts for 18.18% of the total paid-up value.

**Figure: 4.3**  
**Publicly Issued Company**



#### 4.4 Public Issues from Finance and Non-Finance Sector

Listed companies of NEPSE can be divided into finance sector companies and non-finance sector companies. Finance sector mainly includes companies from commercial banks, development banks, finance companies from manufacturing and processing companies, trading companies, hotels and others (SEBON).

Table 4.4 reveals the public from finance and non-finance sector during the study period.

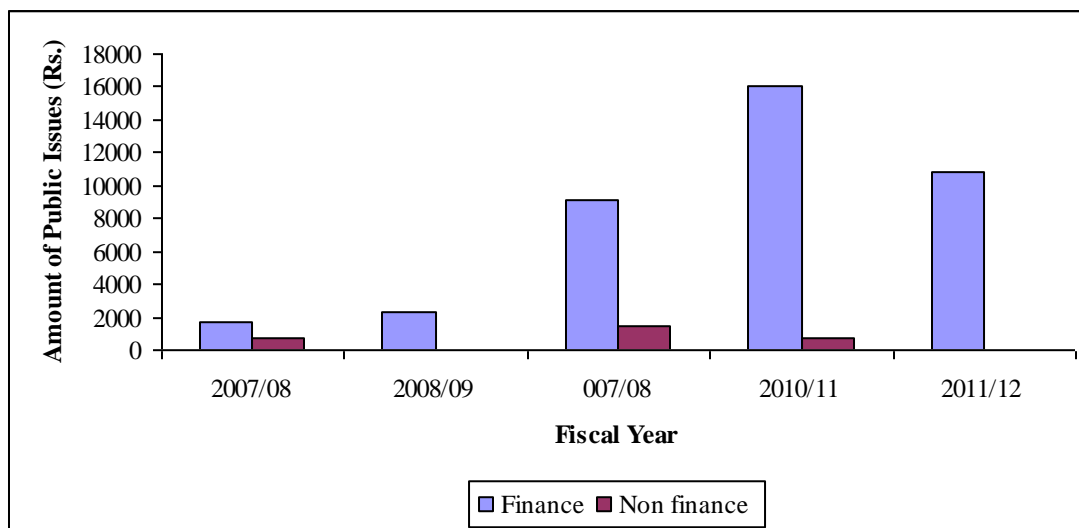
**Table: 4.4**  
**Publicly Issues from Financial and Non-Financial Sector**

Year	Finance Sector			Non-Finance Sector			Total	
	No. of Issues	Amount (Rs. in million)	Annual Growth Rate (%)	No. of Issues	Amount (Rs. in million)	Annual Growth Rate (%)	No. of Issues	Amount (Rs. in million)
2007/08	27	1759.4	18.33	2	683.9	388.50	29	2443.3
2008/09	34	2295.6	30.48	-	-	-100	34	2295.6
007/08	62	9168.20	268.89	1	1500	-	63	10668.2
2010/11	62	16082.07	320.24	2	746.44	-50.24	64	16828.51
2011/12	61	10822.41	-32.71	-	-	-	61	10822.41
Total	246	40127.67	-	5	2930.34	-	251	43058.02

From table no 4.4 and figure no 4.4, it is revealed that total of 251 public issues was made from financial and non-financial sector during the study period. Out of 251 offers, total of 246 (98.01%) offers came from financial sector whereas rest 5 (1.99%) from non-financial sector. It means 98.01% public offers are from financial sector and 1.99% is from non-financial sector. During the study period total of Rs.43,058.02 million issues were issued to public. Out of it Rs.40,127.67 million i.e. 93.19% came from financial sector. Similarly, contribution from non-financial sector amounted Rs.2930.34 million which is 6.81% of the total. These figures clearly show that the financial sector is dominant force of Nepalese IPO market and often calls the shot in the field. This might be the reason why government has promulgated any of rules and regulations bringing more transparency and discipline into the sector.

**Figure: 4.4**

**Public Issues from Finance and Non-Finance Sector**



**4.5 Instrument-Wise Public Issues**

Likewise many other emerging markets Nepalese market also provides limited variety of investment instruments which mainly includes common shares, preference shares, right shares, debenture and few issues from collective investment schemes like mutual fund but in this study the collective investment schemes are not included. Over a period of this time Nepalese stock market has been relying few financial instruments such as common shares, right shares, which cannot be considered good sign regarding overall development of stock market.

As shown in table 4.5 out of 252 offers during the sample period, 85 issues were ordinary shares, which is 33.73% of the total issues offered during the period. Similarly, 154 issues were right shares, which is 61.11% of total issue. Also 12 issues were debenture 4.76%. Hence from number of issue offered perspective, right share was the most preferred instrument for issuing company, followed by ordinary share, debenture and preference share respectively. Similarly, from issued amount perspective right amount, most used instrument with 73.18% of total issued amount , second most used instrument

was ordinary share occupying 14.75% of total amount followed by debentures 11.15% and preference share 0.93% respectively.

**Table: 4.5**  
**Instrument-Wise Public Issues till FY 2011/12**

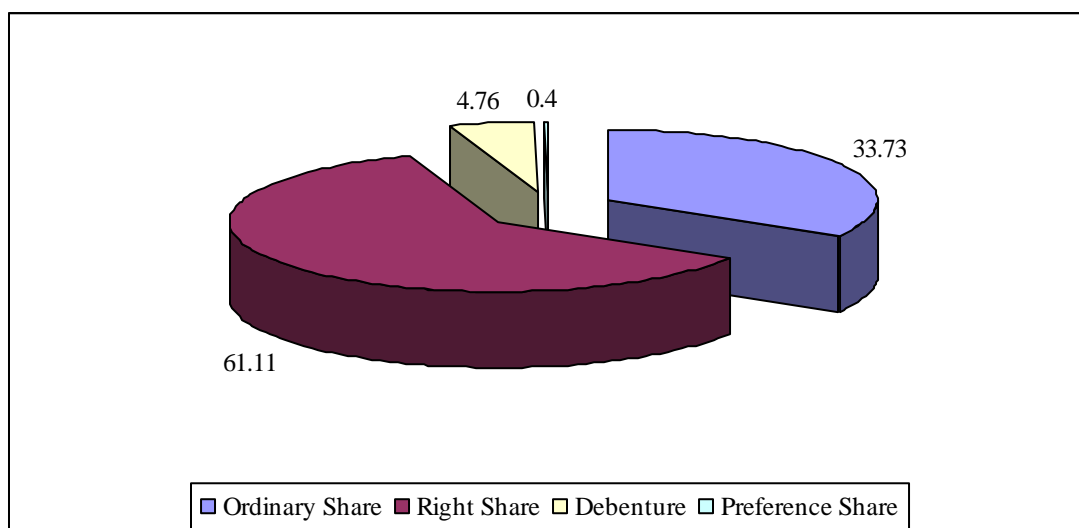
F/Y	Ordinary Share		Right Share		Debenture		Preference Share		Total	
	2007/08	14	456.4	11	1013.5	4	850	-	-	29
		3								3
2008/09	16	290.2	16	1817.2	1	250	1	400	34	2757.5
		5		5						
007/08	16	924.8	42	6093.4	5	295	-	-	63	9968.2
						0				
2010/11	12	1815.	50	14263.	2	750	-	-	64	16828.
		7		19						89
2011/12	28	2649.	33	8173.0	-	-	-	-	61	10822.
		37		4						11
Total	85	63.50	154	31508	12	480	1	400	25	43058
						0			2	
Percentage	33.7	14.75	61.1	73.18	4.7	11.1	0.4	0.93	10	100
	3		1		6	5			0	

Source: SEBON Report

The most striking aspect of the analysis has been the fact that preference share were issued only one and debentures only 12 times. During the entire study period which covered 5 fiscal years. This clearly shows that Nepalese Stock Market is fully dependent on few instruments like ordinary share and right shares. Such fully dependency, on one hand limits the boundary of investment opportunities to the public and on the other hand, limits the overall development prospect of Nepalese Stock Market. At the same time this may also justify the selection of ordinary share as subject of this study.

**Figure: 4.5**

**Instrument-Wise Public Issues till FY 2011/12**



**4.6 Analysis of Annual Turnover**

Annual turnover constitutes an important indicator for measuring the nation's economic activities. It also reflects stock market liquidity as the higher amount of trading of stock market size; the greater is the stock market liquidity. The total amount of securities traded in the FY in the 2011/12 is Rs. 376871.37 million. It was Rs. 21681.14 million in FY 2010/11.

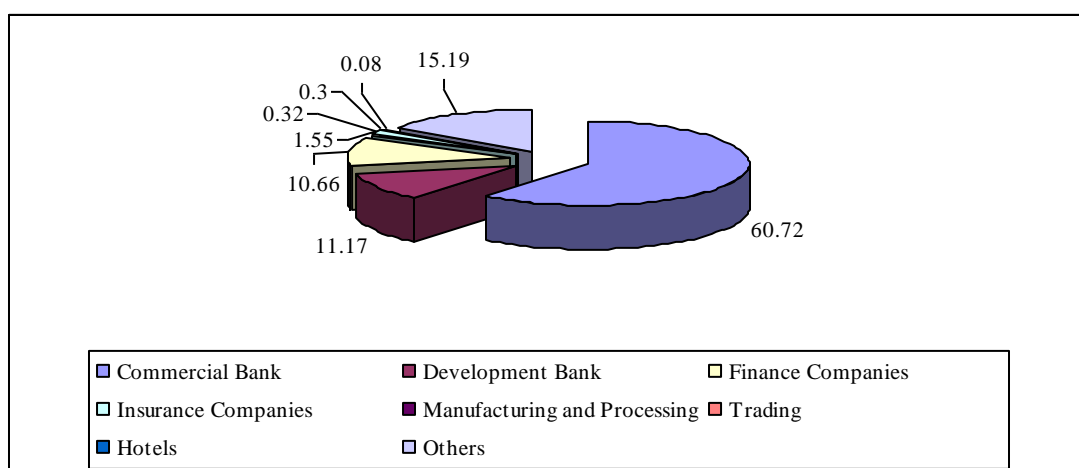
**Table: 4.6**  
**Sector-Wise Annual Turnover**

S.N.	Sector	Amount (Rs. in million)	Percent (%)
1	Commercial Bank	7196.24	60.72
2	Development Bank	1323.53	11.17
3	Finance Companies	1263.94	10.66
4	Insurance Companies	183.47	1.55
5	Manufacturing and Processing	37.74	0.32
6	Trading	35.43	0.30
7	Hotels	10.15	0.08
8	Others	1800.1	15.19
	Total	11851.11	100.00

Source: SEBON Annual Report

As shown in table 4.6 and figure 4.6, among 8 sectors, the contribution from financial sector is about 84.10% that includes commercial banks, development banks, finance companies and insurance companies. On the other hand, contribution from non-financial sector is about 15.89% that includes manufacturing and processing, trading and other companies. These above figure amount of financial sector companies is much higher than that of non-financial sectors.

**Figure: 4.6**  
**Sector-Wise Annual Turnover**



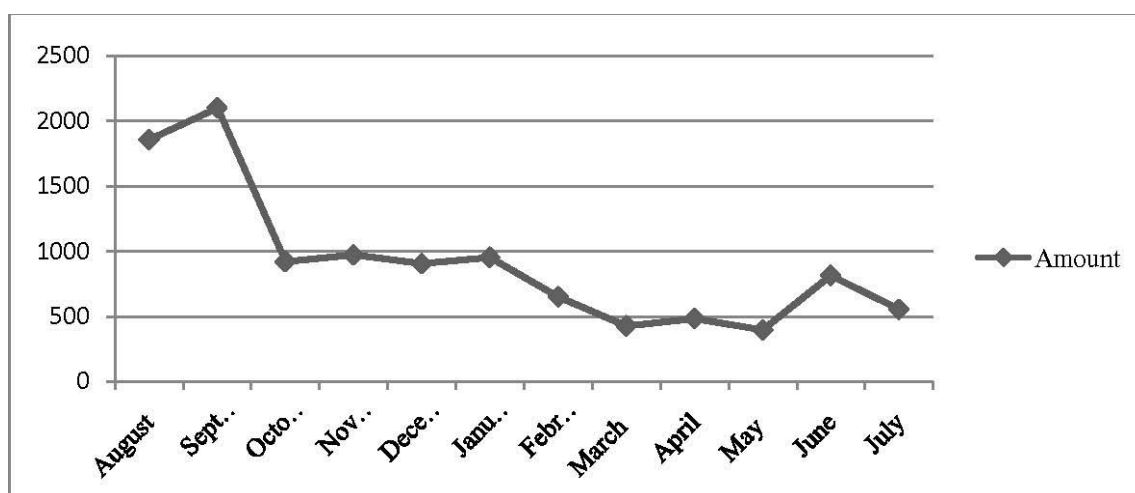
**Table: 4.7**  
**Monthly Turnover 2011/12**

S.N.	Month	Amount (Rs. in million)	Monthly Growth (%)
1	August	1858.81	-
2	September	2101.86	13.08
3	October	922.51	-56.11
4	November	973.49	5.53
5	December	906.79	-6.88
6	January	954.08	5.25
7	February	652.25	-31.64
8	March	428.75	-34.27
9	April	484.93	13.10
10	May	397.9	-17.95
11	June	815.80	0.26
12	July	555.46	-31.91
	Total	11052.33	

Source: SEBON Report

As shown in table 4.7 and figure 4.7, among of 12 month it start from august 2010 to July 2011. The highest turnover is Rs 1858.81 million in august 2010 and the lowest is Rs 397.9 million in May 2011. The highest contribution of monthly growth ratio is 13.10% in April 2011 and the lowest growth rate is -56.11 in October 2010.

**Figure: 4.7**  
**Monthly Turnover 2011/12**



#### 4.7 Analysis of Market Capitalization

By the end of the FY 2011/12, the percentage contribution of market capitalization on nominal GDP is estimated to be Rs. 31.86%. The market capitalization in the FY 2011/12 is presented below in table 4.8. Table 4.8 Year-wise Market Capitalization

**Table 4.8**  
**Year-wise Market Capitalization**

<b>FY</b>	<b>Amount (RS.)</b>	<b>Annual Growth (%)</b>
2007/08	96763.74	57.68
2008/09	186301.3	92.53
2009/10	366247.5	96.59
2010/11	512939.07	40.05
2011/12	376871.37	-26.53

Source: SEBON Annual Report

As shown in table 4.8, the market capitalization of listed securities at the end of FY 2011/12 is Rs. 376871.37 million which is the second highest amount during the study

period and the highest amount of the whole study is Rs. 512939.07 million in FY 2010/11. The lowest amount is Rs. 96763.74 million in FY 2007/08.

According to the growth rate aspect, the percentage of growth is highest in FY 2009/10 i.e.96.59% and lowest in FY 2010/11 i.e. 40.25%. Also negative growth in FY 2011/12

i.e. 26.53%. The above table shows that the amount market capitalization is in interesting trend.

**Table 4.9**  
**Sectors-wise Market Capitalization**

<b>S.No.</b>	<b>Sector</b>	<b>Amount (Rs. in million)</b>	<b>Percent</b>
1	Commercial Bank	206282.52	54.74
2	Development Bank	27488.87	7.29
3	Finance Companies	29869.59	7.92
4	Insurance Companies	9756.61	2.59
5	Manufacturing and Processing	7592.03	2.01
6	Trading	1617.51	0.43
7	Hotels	5285.58	1.40
8	Others	88978.67	23.61
	Total	376871.37	100

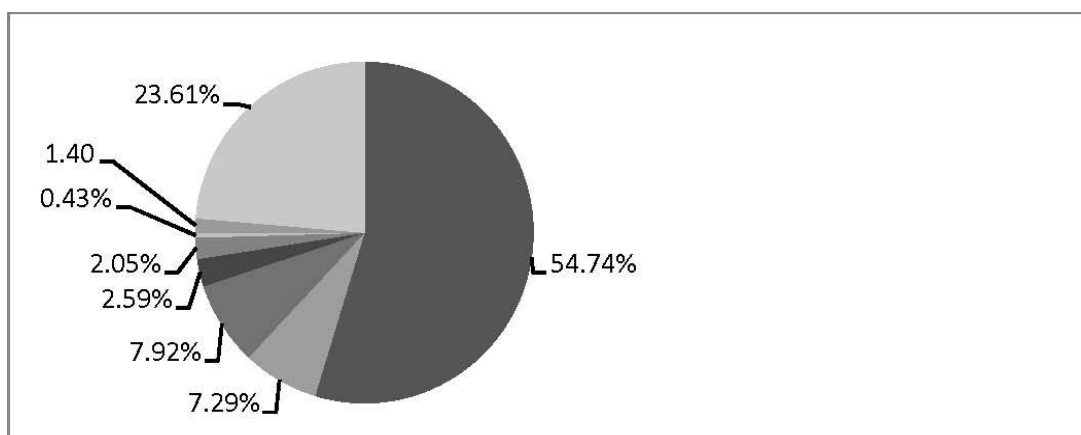
Source: SEBON Annual Report

By analyzing the sector wise market capitalization, banking sector is highest among all sectors. Commercial banks capture 54.74%, development banks 7.29%, finance companies 7.92% and insurance company 2.59%. Similarly, manufacturing and processing 1.40%, trading 0.43%., Hotels 2.01% and others

companies 23.61%. Above figure prove that most of the market capitalization is on the financial sector and rest remains with non-financial and other sector.

**Figure: 4.8**

**Sector wise Market Capitalization**



**Table 4.10**

**Analysis of Annual Turnover and Market Capitalization**

<b>FY</b>	<b>Annual Turnover (Rs. in million)</b>	<b>Market Capitalization (Rs. in million)</b>	<b>% Turnover on Market Capitalization</b>
2007/08	3451.43	96763.74	3.57
2008/09	8360.1	186301.3	4.49
2009/10	22820.8	366247.5	6.23
2010/11	21681.14	512939.07	4.23
2011/12	11851.11	376871.37	3.14

Source: SEBON Annual Report.

Table 4.10 shows that annual turnover and market capitalization. The highest annual turnover is 22820.8 in F/Y 2009/10 and lowest is 3451.43 in 2007/08. The highest market capitalization is 512939.07 in 2010/11 and lowest is 96763.74 in 2007/08.

## 4.8 Primary Data Analysis

One of the most important and logical method to analyze the primary data related to the topic is questionnaire method. 15 copies of questionnaires were distributed to express their views about IPO's in Nepal to senior officials of SEBON, NEPSE general investors, share brokers, professors, lectures and students. The entire questionnaire was collected during the study period. The questionnaire is elated to find out knowledge about IPO, willingness to invest. Source of information and fund used for investing etc.

### 4.8.1 Knowledge about IPO

While getting information about if people had heard about IPO. The question is asked "have you ever heard about IPO" and then most of the people know about it and there are few respondent who don't heard about it.

**Table: 4.11**  
**Knowledge about IPO**

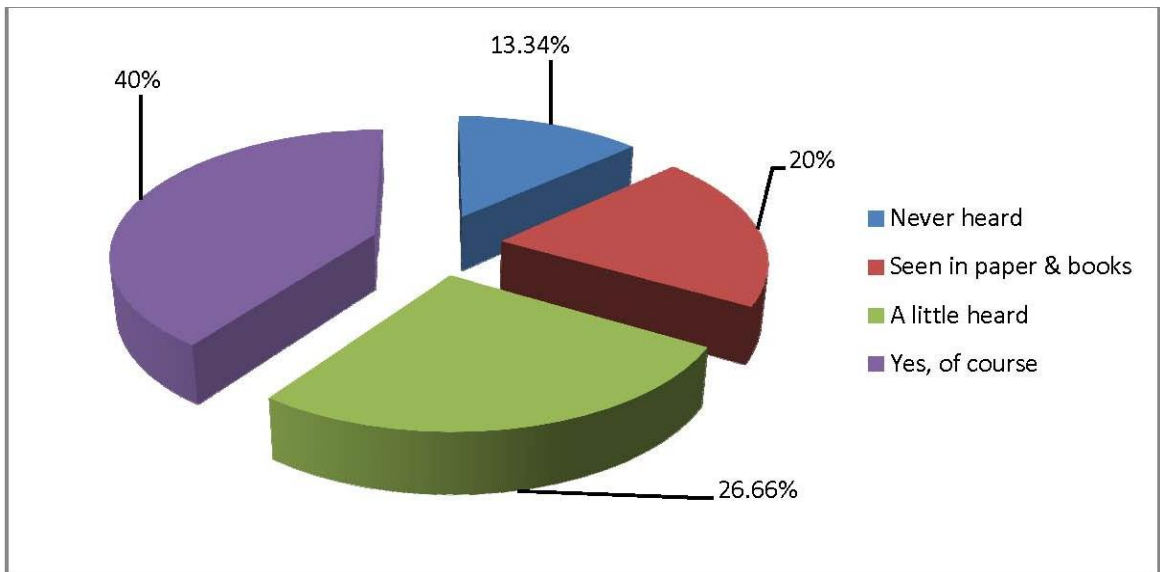
S.No.	Alternative	No. of Response	Percentage (%)
A	Never heard	2	13.34
B	Seen in paper & books	3	20
C	A little heard	4	26.66
D	Yes, of course	6	40
	Total	15	100

Source: Field Survey, 2013

From the table 4.11 and figure 4.9 shows that out of 15 respondents, 13.34 have never heard about IPO, 2 have heard a little bit and rest 4.8.2 Interest (willingness) to invest in IPO

**Figure: 4.9**

**Knowledge about IPO**



**4.8.2 Interest (Willingness) to Invest in IPO**

Only 3 respondents (i.e. 20%) are found to be risk averter, they don't want to take risk all from investing in IPO. 13.34 respondents (40%) stated that there interest to invest respondents (26.66%) stated that they are willing to invest in IPO even the loan if not the cash.

**Table: 4.12**

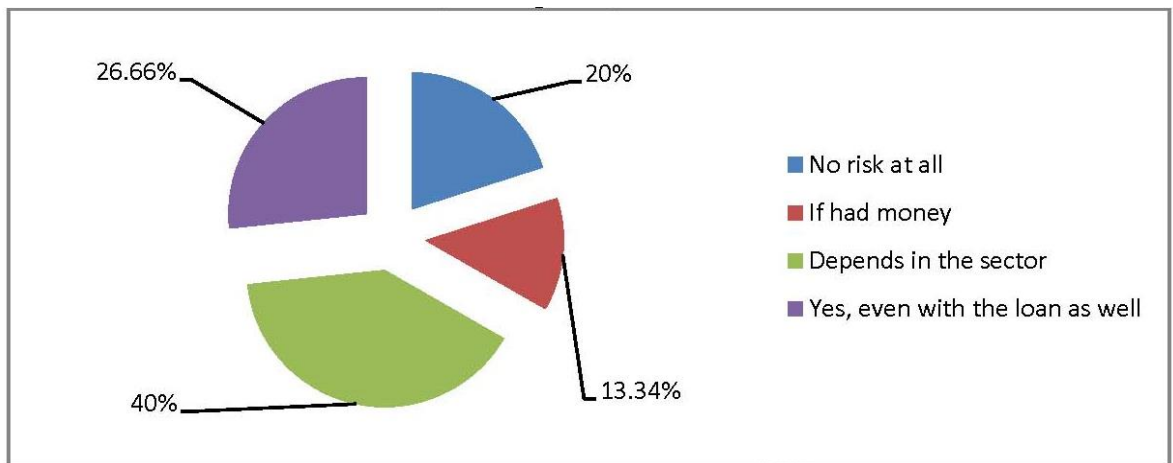
**Interest (willingness) to Invest in IPO**

S. No.	Alternatives	No. of Respondents	Percentage (%)
A	No risk at all	3	20
B	If had m money	2	133.34
C	Depends in the sector	6	40
D	Yes, even with the loan as well	4	266.66

Source: Field Survey, 2013

From the table 4.12 and figure 4.10 it is clear more than 40% people are interest to invest depends upon the sector in IPO even with the loan and the least 20% don't want to take risk, interest of 40% lies on the related sector of IPO. Whole 26.66% want to make only cash investment.

**Figure: 4.10**  
**Interest (willingness) to invest in IPO**



### 4.8.3 Source of Information about IPO

Out of 15 respondents, 40% said that they get information about IPO from Advertisement, 33.34% people said from personal relations or from market. Similarly 20% respondents said that they get information from brokers. There are 6.66% people who find other way of getting information.

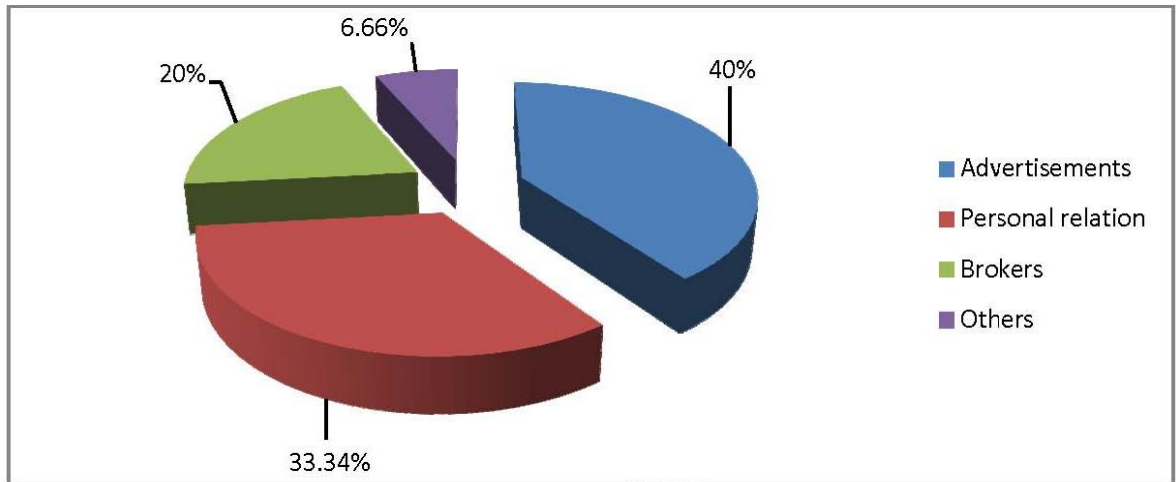
**Table: 4.13**  
**Source of Information about IPO**

S.No.	Alternatives	No. of Respondents	Percentage (%)
A	Advertisements	6	40
B	Personal relation	5	33.34
C	Brokers	3	20
D	Others	1	6.66 6
	Total	15	100 0

Source: Field Survey, 2013

In table no 4.13 and figure no 4.11, the highest ratio is covered by advertisement regarding the response on source of information i.e. 40% and only 20brokers and 33.34% get information from their relatives.

**Figure: 4.11**  
**Source of Information about IPO**



#### 4.8.4 Investors Performance while Investing

While asking about the things that come first in their mind, their preference different from each other. 13.34first, 46.66% people give preference to the sensitive about the brokerage commission wants to know what the market says

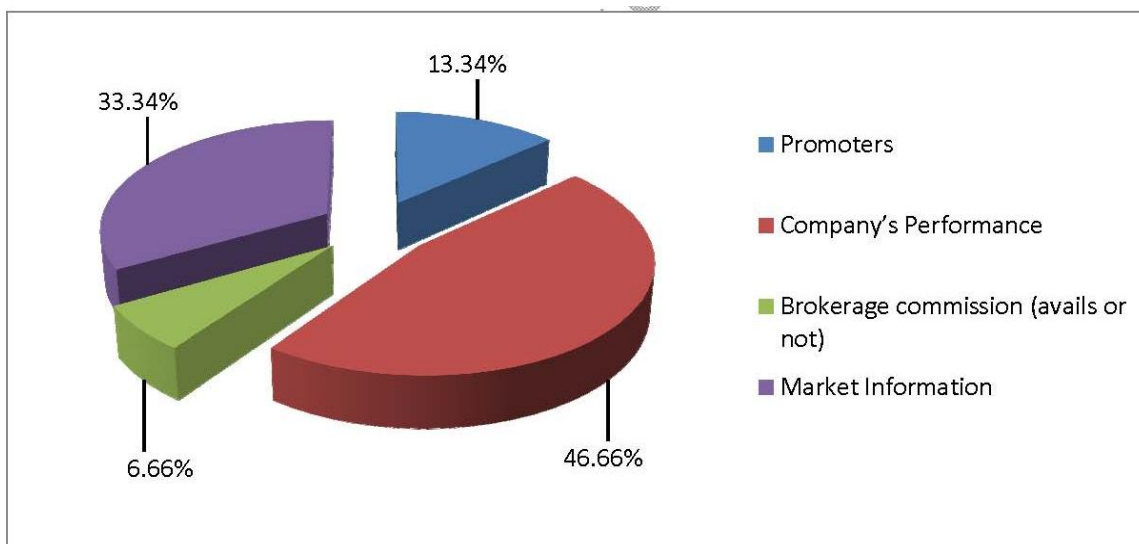
**Table: 4.14**  
**Interest Performance while investing**

S.No.	Alternatives	No. of Respondents	Percentage (%)
A	Promoters	2	13.34
B	Company's Performance	7	46.66
C	Brokerage commission (avails or not)	1	6.66
D	Market Information	5	33.34
	Total	15	100

Source: Field Survey, 2013

The table no. 4.14 and figure 4.12 shows that makes clear that most of the investors 46.66% prefer to know company's performance rather than any other thing before investing and least 6.66% concern about the brokerage commission.

**Figure : 4.12**  
**Interest Performance while Investing**



#### 4.8.5 Number of Companies Invested

Out of 15 respondents 40% said that they have invested in only one company. 33.34% said two to three companies. 113.34% said that have invested in more than three company and 13.34% were found to invest in none of the organization.

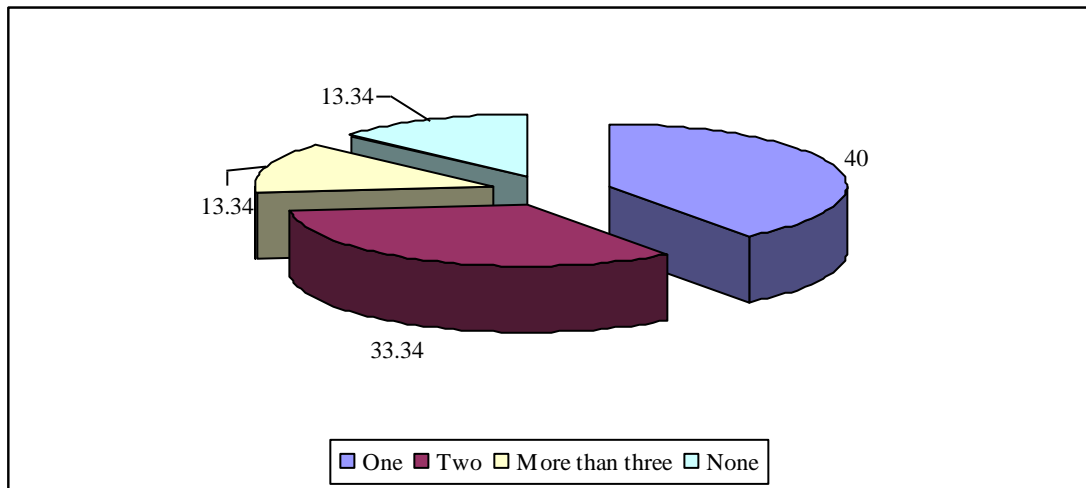
**Table: 4.15**  
**Number of Companies Invested**

S.No.	Alternatives	No. of Respondents	Percentage (%)
A	One	6	40
B	Two	5	33.34
C	More than three	2	13.34
D	None	2	13.34
	Total	15	100

Source: Field Survey, 2013

In table no 4.15 and figure 4.4.13, Being back in share investment in Nepal 13.34% has been found to have invested in more than three companies. Most 40% have invested in only one company and 33.34% have invested in two.

**Figure: 4.13**  
**Number of Companies Invested**



#### 4.8.6 Fund used for the Investment

In the question of fund used in IPO investment, 8 respondents i.e. 53.34% answer personal fund while rest 46.666% answer loan/credit fund.

**Table: 4.16**  
**Fund used for the Investment**

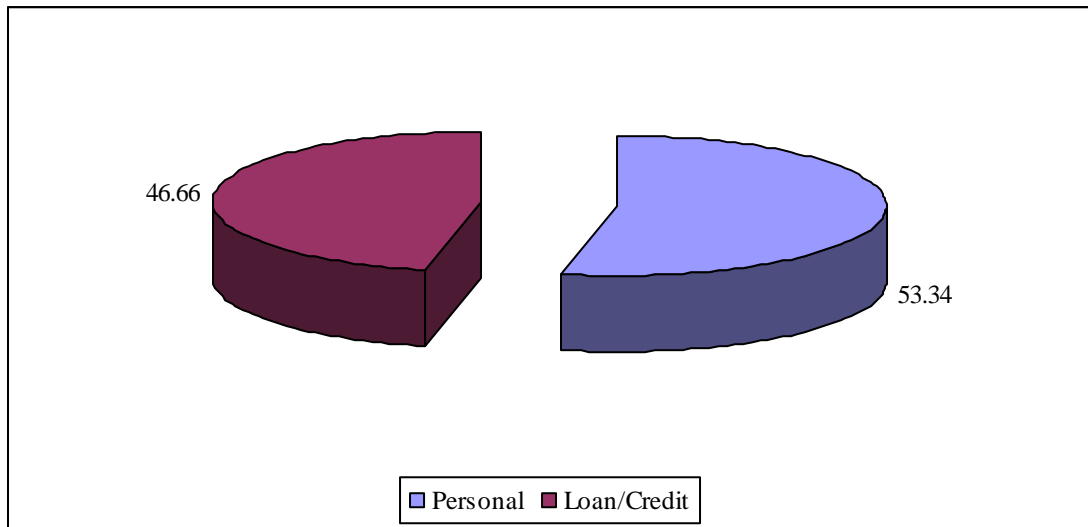
S.No.	Alternatives	No. of Respondents	Percentage (%)
A	Personal	8	53.34
B	Loan//Credit	7	46.66
	Total	15	100

Source: Field Survey, 2013

Here table no. 4.16 and figure 4.14 shows that more than half wants to use their own funds rather than credit. People like to use personal fund rather than loan and credit.

**Figure: 4.14**

**Fund used for the Investment**



**4.8.7 Expectation behind Investment in IPO**

Different people have different expectation behind investing in IPO. For the question regarding these responses were as follows:

**Table: 4.17**

**Expectation behind Investment in IPO**

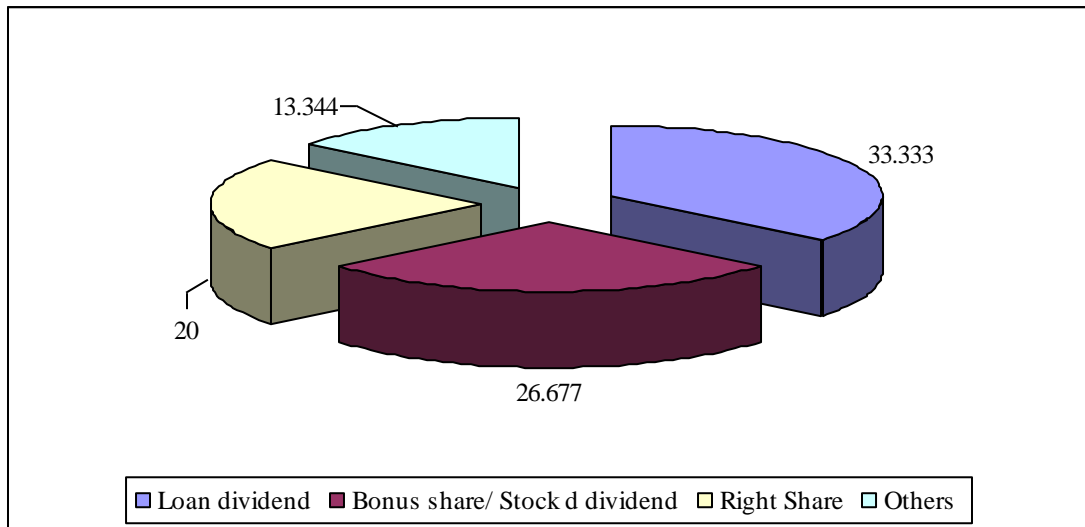
S. No.	Alternatives s	No. of Respondents	Percentage (%)
A	Loan dividend	5	33.333
B	Bonus share/ Stock d dividend	4	26.677
C	Right Share	3	20
D	Others	2	13.344
	Total	15	100 0

Source: Field Survey, 2013

Here, 33.33% expects cash dividend, 26.67% expects bonus share, 20% states to be favor or right share while rest 13.334% seen to be interest in other than these matters. So it shows that the most people are wanted to invest on right share.

**Figure: 4.15**

**Expectation behind Investment in IPO**



**4.8.8 Sector Preference for Investment**

For the question whether to choose financial sector to invest or non-financial sectors 80% choose financial sector and rest 20% choose non-financial sector which have been clearly shown in the below.

**Table: 4.18**

**Sector Preference for Investment**

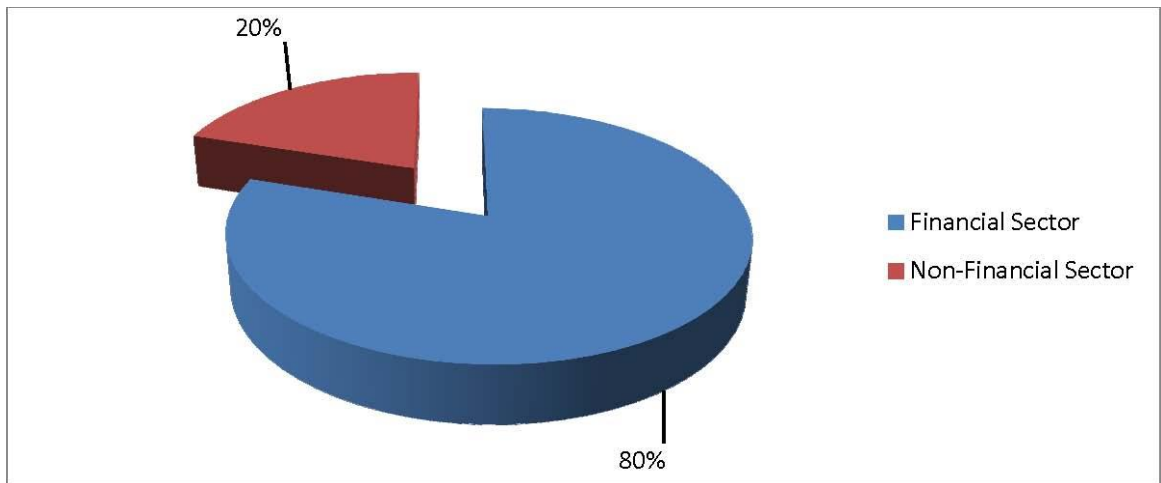
S.No.	Alternatives	No. of Respondents	Percentage (%)
A	Financial Sector	13	80
B	Non-Financial Sector	3	20
	Total	15	100

Source: Field Survey, 2013

In table no 4.18 and figure 44.16, Out of 15 respondents, 80% Preference for Invest to financial sectors and only 20% prefer for non financial sector. Therefore most of the respondent Preference for Invest on financial sectors.

**Figure: 4.16**

**Sector Preference for Investment**



**4.8.9 Preferred Financial Sector**

From among the 15 respondents 46.66 prefer commercial bank, 33.34 prefer development bank, 13.34 prefer finance company and only 6.66 prefer insurance company for investment in financial sector.

**Table 4.19**

**Preferred Financial Sector**

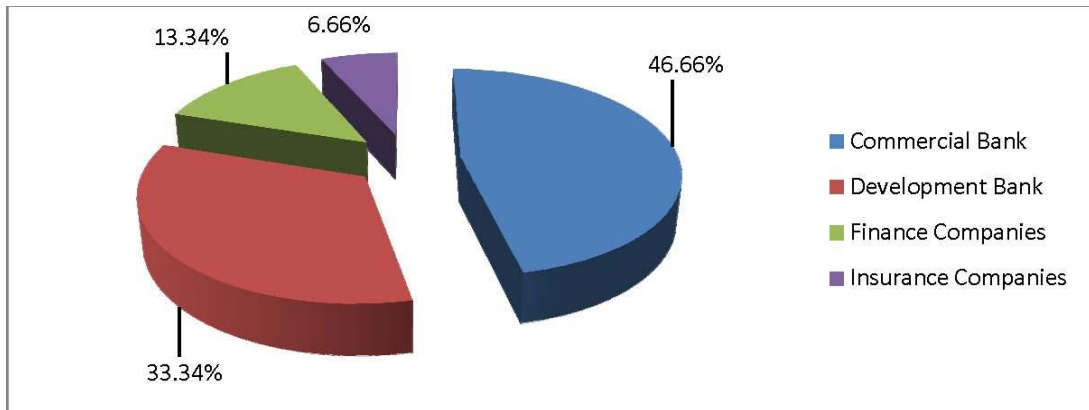
S. No.	Alternatives	No. of Respondents	Percentage (%)
A	Commercial B Bank	7	46.6 66
B	Development B Bank	5	33.3 34
C	Finance Companies	2	13.3 34
D	Insurance Companies	1	6.6 66
	Total	15	1000

Source: Field Survey, 2013

In the table no 4.19 and figure 4.17, out of 15 respondents, 46.66% or most of the investors give preference to commercial bank for IPO investment, 33.34% give to development bank, 13.34% are found to be favor of finance company and remaining 6.66% are in favor of insurance company. Among the investors least are in favor of insurance company.

**Figure: 4.17**

**Preferred Financial Sector**



**4.8.10 Preferred Non-Financial Sector**

From the 15 respondents for the question which non-financial would you prefer to invest the respondents were as follows:

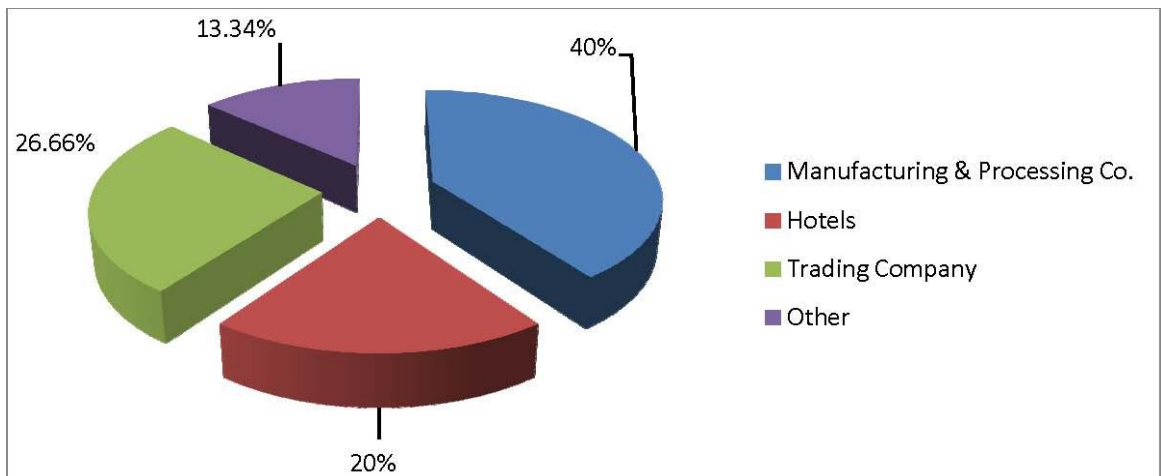
**Table: 4.20**

**Preferred Non-Financial Sector**

S. No.	Alternatives	No. of Respondents	Percentage (%)
A	Manufacturing & Processing Co.	6	40
B	Hotels	3	20
C	Trading Company	4	26.66
D	Other	2	13.34
	Total	15	100

Source: Field Survey, 2013

**Figure: 4.18**  
**Preferred Non-Financial Sector**



**Table 4.21**  
**Ultimately Goal for Investment in IPO**

S. No.	Alternatives	No. of Respondents	Percentage (%)
A	Support for r old-age	3	200
B	Children education	3	200
C	Annual return	5	33.333
D	Other	4	26.666
	Total	15	10 00

Source: Field Survey, 2013

Table 4.20 and figure 4.18 show that for non-financial sector, 40% seems to be interest in manufacturing & processing company, 20% are interested in Hotels while 26.66% interest in trading companies. And the least i.e. 13.34% are interest in other sector.

#### **4.8.11 Ultimate Goal for Investment in IPO**

Different people have different goal for investment 20% have goal of support old age and invest for children education, 33.34% want to invest for fulfilling the goal of getting % have other than goals

**Figure: 4.19**

**Ultimately Goal for Investment in IPO**

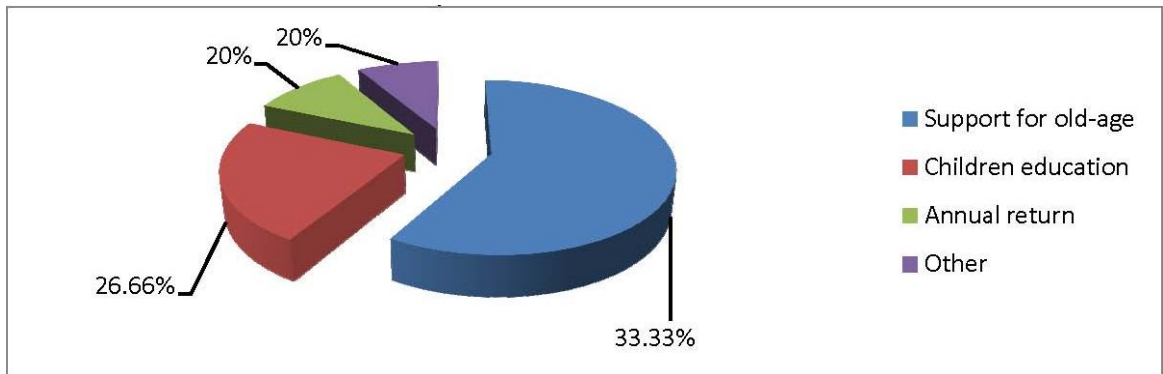


Table 4.21 and figure 4.19 show that most of the people invest for annual return which is 33.33 percent but out of total respondent secondly they invest for supporting for old age and children education which is 20%. And 26.66% of respondents invest for others needs.

**4.8.12 Reason for not Going Public**

All companies do not want to go publicly 26.66% Companies do not want to lose the control by going public, 26.66% think they do not want to share profit, 20% think they do not want to bear the obligation to mass shareholders and remaining 26.66% complex by going public.

**Table 4.22**

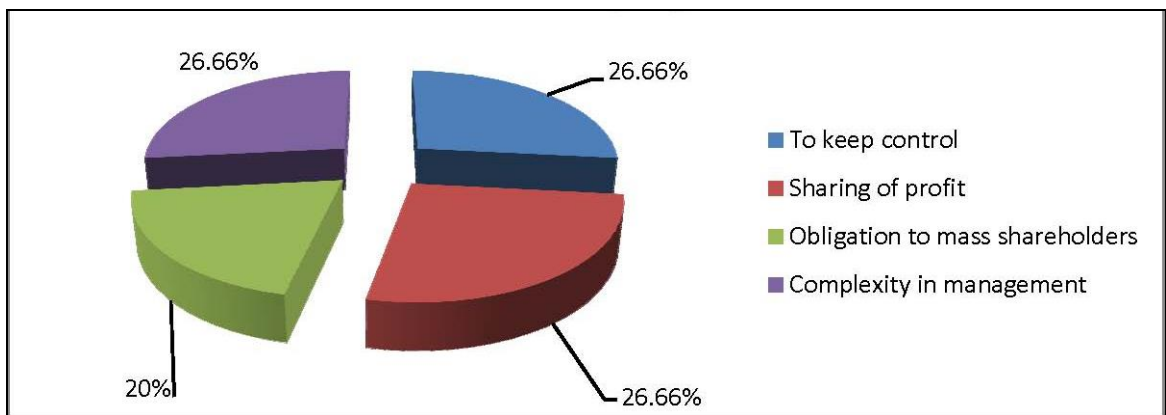
**Reason for not going Public**

S. No.	Alternatives	No. of Respondents	Percentage (%)
A	To keep control	4	26.6 66
B	Sharing of profit	4	26.6 66
C	Obligation to mass shareholder	3	20 0
D	Complexity in management	4	26.6 66
	Total	15	1000

Source: Field Survey, 2013

Table 4.22 and figure 4.20 clearly show that the reason behind most of the companies not going public is they do not want to share profit 26.66%, 26.66% believe company fears complexity in management, 26.66% believes it simply because companies want to keep full control, only 20% believe that companies do not want to increase obligation to mass shareholders.

**Figure: 4.20**  
**Reason for not going Public**



#### 4.8.13 Reason for Limited People Investing in Primary Market

Only limited people invest in the primary market. For the reason asked 20% stated this is due to lack of money, 20% stated due to lack of knowledge 46.66% said people lacks information and only 13.34% stated other reason.

**Table 4.23**  
**Reason for Limited People Investment**

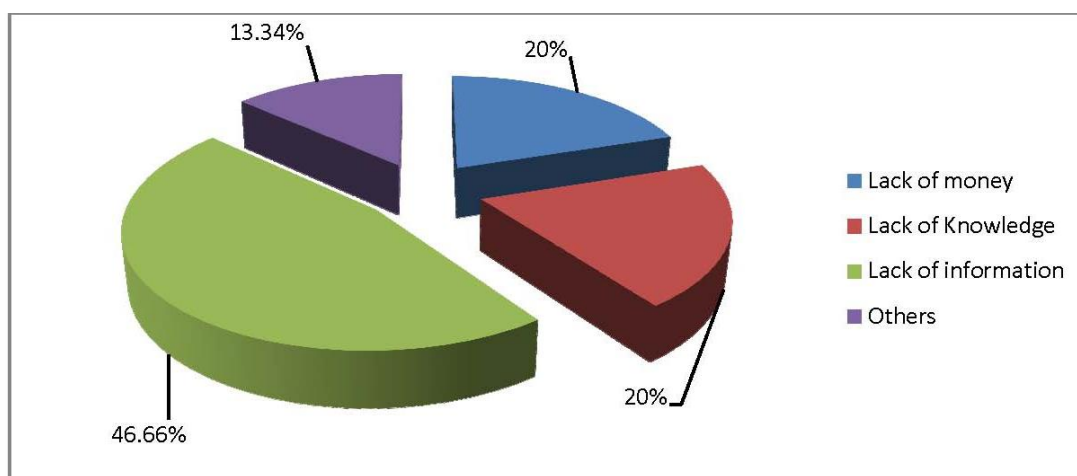
S. No.	Alternatives	No. of Respondents	Percentage (%)
A	Lack of money	3	20
B	Lack of Knowledge	3	20
C	Lack of information	7	46.666
D	Others s	2	13.334
	Total	15	10 00

Source: Field Survey, 2013

In the table 4.23 and figure 4.21, the highest part is lack of information i.e. 46.66% which means most people do not invest. In primary market due to lack of information, 20% shows the reason of lack money and lack of knowledge and 13.34% do not invest due to other reason than these.

**Figure: 4.21**

**Reason for Limited People Investment**



**4.9 Major Findings of the Study**

**4.9.1 Findings of Secondary Data**

- Form fiscal year 2007/008 to 2010.11 SEBON approved 252 issues amounting Rs. 43,057.90 millions. Thee higher number of issues is in the year 20100/11 which is 64 and the lowest is in 20007/08 which is only 29.
- A total of 61 public limited companies raised funds amounting too Rs. 10,822.41 million by issuing securities in the fiscal year 2011/12. In the FY 2010/11 a total of 64 companies had raised funds amounting to Rs. 16828.51 million.
- In the last fiscal year, total listed companies in Nepal Stock Exchange Ltd. Were 159 which reached to be 176 in the FY 2011/12. In the FY

2011/12, annual turnover decreased by 45.3% to be Rs. 11,851.11 million as compared to turnover of Rs. 21681.14 million in the FY 2010/11.

- In the FY 2011/12 ,the market capitalization of the listed companies decreased by 26.5% to be Rs. 3,76,871.37 million as compared to market capitalization of Rs. 5,12,939.07 million in the FY 2010/11. In the FY 2011/12 the preliminary estimate of the contribution of market capitalization to the GDP is 31.86%.
- The total paid-up value of the listed securities by the end of the FY 2011/12 reached to Rs. 79,356 million which was Rs. 61140.0 million in the FY 2010/11.

#### **4.9.2 Findings of Primary Data**

- In the present circumstances a single investor or a group of investor can adversely affect the market scenario. This is underprivileged signal to the development of capital market.
- Public response to the financial sectors is higher than non-financial sectors.
- Now-a-days the public response is highly positive, because people are aware, money flow in the market is higher, people now realize the importance of share investment, people have seen that most companies are distributing dividends, and lack of better alternatives for investment.
- The primary sources of data Shows that the major source of information of public offering is media. Public getting information of IPO mostly from print media.
- Most of the investor (46.66%) preference to the relative company's performance before investing their money in stocks.

- People are getting aware to primary market to choose the right sector for investment. Investors are making portfolio of their investment; 40% investor invests their money in one company and 13.34% in more than three companies.
- Profitability is the encouragement factor for investment. The investors think that those companies who are performing well in the market will do better in the future.
- People think that the present environment is suitable for investment 80% people prefer to invest their money in the financial sector.
- This study has found that response to the primary market is highly positive due to lack of opportunities for investment in other sector. Despite this, public are attracted towards shares to increase their value of investment.

## **CHAPTER-V**

### **SUMMARY, CONCLUSION AND RECOMMENDATION**

This chapter embodies three parts of the study; summary, conclusion and recommendation. The first part goes over with summarization of the whole study, the second part depicts the conclusion and the final part presents recommendation in the light of its findings.

#### **5.1 Summary**

The securities market consists of new issue market and Stock Exchange, New Securities are offered to the investors for the first time through Initial Public Offering (IPO). IPO behavior is one of the most important components of capital market. It facilitates the exchange assets by bringing together buyers and sellers of securities. Capital markets provide an effective way of raising money for commercial enterprises and at the same times provide as investment opportunity for individuals and institutions. Thus, IPO has both theoretical and practical perspectives.

The basic objective of this study is to asses public response to the Initial Public Offering (IPO). The primary and secondary both types of data are taken to analyze the objective of the study. Primary data are taken from direct questionnaire provided to the general investors. Secondary data are taken from the publication of SEBON, NEPSE and various merchant bankers.

Although some studies regarding the different issues of capital markets are already conducted in Nepal, the study based on the IPO behavior is perhaps the first in Nepal. This study is based on secondary data with large sample of listed company from different sectors whose issues were offered by SEBON. This study covers almost sectors, companies i.e. commercial banks, development banks, finance companies, insurance companies, manufacturing and processing company, hotels, trading company and others whose issues were offered for issue and are taken as sample. For the purpose of this study, the necessary

secondary data were collected for the period of 2007/08 from the annual reports of SEBON, other bulletins of NEPSE and different websites. This study is based on the time series data analysis 260 observations of the sample companies. The time series data are used to trace out the current situation of IPO behavior. The average mean, multiple bar-diagram, pie-chart were to analyze the picture of IPO behavior.

In the last fiscal year, total listed companies in Nepal Stock Exchange Ltd. were 176 which reached to be 260 in the FY 2011/12. In the FY 2011/12, annual turnover decreased by 45.3% to be Rs. 11,851.11 million as compared to turnover of Rs. 21681.14 million in the FY 2010/11.

In the FY 2011/12 ,the market capitalization of the listed companies decreased by 26.5% to be Rs. 3,76,871.37 million as compared to market capitalization of Rs. 5,12,939.07 million in the FY 2010/11. In the FY 2011/12 the preliminary estimate of the contribution of market capitalization to the GDP is 31.86%.

From the primary data analyzes it is clear that most of the public aware about the IPO only 13.34% don't have heard about IPO. 20% people do not want to take risk while 365 want to invest in IPO even the loan. Most of the respondents 40% seen to be informed about IPO from advertisements. Among the investors 46.66% people given preference to company performance before investment while only 6.66% give preference to brokerage commission if that avails or not 13.34% are interest in the promoter's recognition.

About 80% are interest to invest in financial sector and only 20% are in non-financial sector. From among the financial sectors 46.66% are interested in commercial banks, 33.34% in development banks, 13.34% in financial companies and 6.66% in insurance companies. In the case non-financial sector highest 40% are interested in manufacturing and processing companies, 20% in hotels and 26.66% in trading company. 33.33% people annual return is the ultimate goal for investing, 20% thinks supports for old-age. 26.66% people think that most companies do not go public as they do not want to share profit

with public, whereas 26.66% think it's because they want to keep control with themselves, again 226.66% thinks as it may bring complexity in management. Most of the people 20% show the reason of lack of money for limited people investing in primary market and only 46.66% think it's due to lack of information.

From the study, it is clear that if get opportunity maximum are eager to invest in IPO as in Nepal there lacks alternative for investment.

## **5.2 Conclusion**

The major conclusion of the study is the most of the general investors in Nepal do not have sufficient information regarding the primary market but still they are interested to invest money in the primary market. This is good sign to the expansion of the primary market. As per this study, almost every sector is getting good response from general public. Specifically financial sector is more preferable than non-financial sector. Even among the financial sector most are interested in commercial banks. Vast deviation is found the primary market of Nepal during 2007/08 to 2011/12 period, number of issue approved ranges from 64 at highest in 2009/10 and 2010/11 to 29 at lowest in 2007/08.

The study concludes that most people are in favor of regulation by NRB for IPO funding via financial institutions as it lessens the equal chance of getting allotment. Most of the shares go impart of big investors. This kind of mismanagement in allotment discourages the investors. Contract between the issue manager and the issue company highly affects the whole IPO process, so make this as the people need, it should be regulated. People are eager to know the promoter, company's performance before investment. IPO's handled by bigger brokerages are found to be more successful. Even though the organization's process of public offering is quite long the service provided to the investors seems to be satisfactory. If raising interest of the public into primary market is one of the objectives, then the primary market of Nepal is fulfilling this role gradually.

### 5.3 Recommendations

To make the IPO more efficient, effective and convenient following suggestions are recommended:

1. Investing in shares is a gamble which involves huge amount of risk. To be successful in the stock market, investors should always be clear to his strengths, weakness, requirements, wishes, risk taking capabilities and how to react on different and even changing market conditions. They should not buy the shares of a company until they know details about it.
2. Nepalese capital market is largely dependent on financial sector, which is not good signal for overall development of IPO market and market as a whole in this regard the regulatory body and the government should take a step forward and encourage public issue from other sectors like manufacturing and processing by providing additional facilities such as tax-concessions.
3. Ordinary and right share is found to be the most used financial instrument while other financial instruments like preference shares and debentures are rarely issued. The fact that such ordinary and right shares carry maximum risk to investors on one hand and also cause of ownership to issuing company seemed to be forgotten. In this regard, it's recommended that root cause beneath.
4. The huge amount of securities traded in each fiscal year comes from financial sectors and rest few from non-financial sectors which is not good signal for IPO market. The SEBON and other concern authorities should conduct public awareness and investors education programs to increase the level of investor's awareness.
5. The stock market lacks the existence of sophisticated investors. So it is recommended to the regulatory bodies to carry out programs using various media and spot programs to inform and attract the potential investors, both individual and institutional investing into shares.

6. The information and financial statements of the companies should be disseminated properly and timely.
7. The market intermediaries should be educated, trained and professionalized by conducting the various program like On the Job training, Technical training etc.
8. The government should allow foreign investors to invest in Nepalese capital market.

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## Appendix - I

### A Survey on Investors Response to Initial Public Offering in Nepal

Please tick ( ) the correct answer. (Tick one or more, if applicable)

1. How did you get idea/Information to make investment into primary issue of securities?
  - a. From Friends and Relatives
  - b. From media
  - c. From Stock brokerage
  - d. From others
  
2. In which sector do you think public have better opportunities for investment?
  - a. Banking sector
  - b. Finance/ Development Bank
  - c. Insurance Companies
  - d. Manufacturing
  - e. Other
  
3. Do you have experience of investment in IPO?
  - a. Yes
  - b. No
  
4. Are you aware about the financial performance of companies?
  - a. Very much
  - b. Moderately
  - c. Little
  - d. Not at all
  
5. Are you have the satisfactions on the returns of your investment?
  - a. Yes
  - b. No
  - c. Don t know
  
6. By which special characteristics are you impressed (purpose) to invest your money in Public offering?
  - a. Divivend
  - b. Right Share
  - c. Capital Appreciation
  - d. No brokerage Commission
  - e. Company Performance

7. Do you read prospects of the company before investment?
  - a. Yes
  - b. No
  
8. What are your bases of decision for investment?
  - a. Market Index
  - b. Profitability
  - c. Friends opinion
  - d. Market whim
  
9. What is the source of fund that you used in IPO?
  - a. Loan (Credit)
  - b. Personal fund
  
10. What is your opinion that the firm not like to go IPO?
  - a. Sharing profit
  - b. Management Complicity
  - c. Obligations of Public
  - d. Enough Funds
  - e. Others
  
11. How many companies have you invested in?
  - a. Single Company
  - b. Up to 5 Companies
  - c. 5-8 Companies
  - d. More than 10 Companies
  
12. In which instrument (securities) do you make the investment?
  - a. Common stock
  - b. Debenture/Bonds
  - c. Prefer red stock
  - d. Others
  
13. Main cause of over application in initial offering is due to
  - a. Lack of investment opportunity
  - b. High Dividend Distribution
  - c. Low interest rate on bank
  - d. Other
  
14. In your opinion, what is the best investment Decision
  - a. Own business
  - b. Investment in securities
  - c. Bank balance
  - d. Other
  
15. What is the reason that the limited number of people investment in IPO?
  - a. Lack of money
  - b. Lack of information
  - c. Lack of knowledge
  - d. Other (Specify)

Name: .....

Address: .....

