

# CHAPTER I

## INTRODUCTION

### 1.1 General Background of the Study

The market is one of the major components of this financial system. The subsystem of this financial market is money market and capital market. Money market is the market consists of short term securities. These are the securities issued for short period or less than one year. Capital market is the market for long term securities. Examples of capital market are shares, bonds, debentures etc. These sources provide the capital to entrepreneurs for long term. It is the market through which the entrepreneur issue securities like shares, bonds, warrants, preferred stock to collect additional fund required to establish, develop and diversify the business. The savings of the scattered publics are mobilized to meet the fund gaps of the business. (*Bhalla; 2007:147*)

Both the money market and capital market are classified into primary market and secondary market. It is discussed in the following lines. The market where goods and services securities are sold to mobilize the saving for the establishment of and operation of business are known as primary market. It is also known as original sale of securities. This market is also known as IPO marketing. This market, securities can be sold either at par, or premium or discount but in the case of Nepal, Nepal Company Act 2063, has restricted to sell the securities at discount. SEBON has licensed different issue managers to perform the job of issue management under the Securities Act 2063. It is the responsibilities of SEBON to control regulate and direct the issue manager to operate the disciplined market in the country.

The market where the secondhand securities are traded is known as secondary market. Securities that are purchased once are traded in secondary market. Hence we can say that Secondary market is the complement of primary market.

They two are interrelated. In the absence of one market another cannot flourish. Secondary market comprises stock exchange and Over-The Counter (OTC) Market. Nepal has started OTC market since 2064. Though it has started but no trading has taken place till to date. Therefore stock exchange is considered as secondary and organized market. The transactions and price movement in secondary market is the basis of economic policy and decision of the government policy. Therefore the entrepreneur through primary market makes the initial public offering (IPO). This market is for raising the additional fund required to establish the company in the country. (*Thapa and Rana; 2011:74*)

An initial public offering (IPO) is a securities offering, in which an enterprise sells its stock publicly for the first time without having a prior price history. A milestone for any company is the issuance of publicly traded stock. While the motivations for an initial public offering are straightforward, the mechanism for doing so is complex. The first time a company issues stock for sale to the public is known as Initial Public Offering or IPO. The company is said to “going public” when this happens. The offering is highly regulated and often surrounded by a lot of media attention. Most of the company starts out raising equity capital from a small number of investors with no liquid market. If a company prospers and needs additional equity capital, at some point the firm generally finds it desirable to “go public” by 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 investor s for the lack of liquidity associated with a privately held company. Through IPO, the founder simply wants to establish a value and liquidity for the stock. (*Van Horne, 2002:578*)

To make an IPO, shares are offered from the company (issuer) with the help of an underwriter who evaluates the company and determines their value, and then sells the shares to investors for a commission. A company becomes public for the purpose of obtaining capital without having to approach private investors

and repay loans. Once public, the company can offer additional share on occasion to raise capital for the expansion without incurring debt.

IPOs can be a risky investment. For the individual investor, it is tough to predict what the stock or shares will do on its initial day of trading and in the near future since there is of the little historical data with which to analyze the company. Also, most IPOs are of the companies going through a transitory growth period, and they are therefore subject to additional uncertainty regarding their future value. An 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. Public Offering is security offering where all investors have the opportunity to acquire a portion of the financial claims being sold. (*Keown & Petty; 2002:471*)

In particular, there are certain ongoing costs associated with the need to supply information on a regular basis to investors and regulars for publicly traded firms. Furthermore, there are substantial one- time costs associated with initial public offering that does 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. Firms going public, especially young growth firms, face market that is subject to sharp swings in valuations. The facts that the issuing firm is subject to the whims of the market makes the IPO process a high-stress period for entrepreneurs. So issuing of share to the general public is easy to raise the fund for the company. This public issuing is made compulsory under Securities Exchange Act in Nepal. Promoters will receive permission from the government authority to establish a public limited company if they show desire to include general public in its equity base. Hence firm needs to sell part of its total equity to the general

public to raise the required fund through public issue of shares in primary market is called Initial Public Issue. It is also called Initial Public Offering (IPO).

Because Initial Public Offerings involves the sale of securities in closely held firms in which some of the existing shareholders may possess non-public information, some of the classic problems caused by asymmetric information may be present. In addition to the adverse selection problems that can arise when firms have a choice of when and if to go public, a further problem is that the underlying value of the firm is affected by the actions that the managers can undertake. This moral hazard problem must also be dealt with by the market. In addition, evidence is presented on three patterns associated with IPOs: (i) new issues under pricing, (ii) cycles in the extent of the under pricing, and (iii) long-run underperformance. Corporate finance activities, including the issuance of securities, provide significant revenues for investment banks (*Dunbar, 1999*).

Investing in the stock market should not be a "heart and gut" affair based on hunches, guesswork, hot tips, rumors or speculation. This is true for investments in securities of companies already listed on the stock exchange; it is also true for investments in securities of companies seeking listing for the first time. Seeking listing on a stock exchange is also called 'going public' or 'flotation'. The purpose of seeking listing is generally to raise funds for the company's business expansion or growth. (*Choudhary; 2005:102*)

The company seeking listing will therefore offer part of its securities to be subscribed by the public, as part of the listing exercise. This offer is called an Initial Public Offering (IPO). Currently, any company wishing to undertake an IPO would have to get the approval from the Securities Commission before the IPO can be carried out. The Securities Commission, in considering an IPO proposal, would take into account the overall suitability of the company undertaking the IPO. Once approved, the company is required to issue a

prospectus that tells about the company, what it does, how it has fared and how it expects to perform in the future.

In Nepal the first public issue of ordinary shares took place more than 50 years back with the public issue of Biratnagar Jute Mills and Nepal Bank Ltd in 1937 A.D. But the development of capital market started in 1976 A.D after the establishment of Security Exchange Centre with the objectives of facilitating and promoting the capital market in Nepal. It was the only capital market institution, which undertook the job of brokering, underwriting and managing public issue, market making for government bonds and other financial services. Security Exchange Centre dealt in the securities as a broker as well as regulatory body. The Centre used to take; buy and sale only on orders from interested investors and confirm them if a price and quantity matched. There was no time limit which a deal took place. It normally took one day to weeks. Due to this, general problems while buying selling shares. Security Exchange Centre was converted into Stock Exchange Limited in 1993, and under its support, the broker system of secondary market was established. Until 2011 A.D. out of 32 brokerage firms, 23 brokerage firms are doing their job regularly and it has given license for new 15 brokerage firms on fiscal year 2011. Nepal Stock Exchange Limited is a non-profit organization it operates under Security Exchange Act 1983. The basic objectives of the Nepal Stock Exchange Limited are to impart free marketability and liquidity to the government bonds and corporate securities. With the establishment of fully fledged stock Exchange, the shares, which the public had held for decades, becomes liquid.

Basically, this study is based on the dealing process in the primary market. As well as the study concerned with the pace public offering and public response to IPO Nepal. As per the provision of Company Act of Nepal, privately held companies cannot issue their shares in public by themselves. The issue must be done through issue managers. Though the company can raise the capital to the

extent of its company by initial public offering. The total amount paid by the promoters at the time of establishment or after time-to-time rising of funds by the company is the paid-up capital.

## **1.2 Statement of the Problems**

The issues in primary market are subject to the directives and regulatory framework of the concerned governing bodies. Hence, the study primarily deals with the process of managing the public issues by the issue managers. One most important feature of the Nepali IPO market is that most retail investors are speculators who bet their money on any kind of IPO without properly analyzing the offer documents. This is partly due to the lack of diversity of stocks in the market which is dominated by the stocks of banks and financial institutions.

Most IPO subscribers in Nepal are short-term investors who are interested to sell the stocks as soon as they are listed in the stocks exchange. Therefore, most of the people view an IPO as a quick way to make money rather than a long-term investment. The problem towards which this study is directed is to identify the 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, how to invest in IPO and how to manage fund for IPO etc.

Nepalese capital market is very small in comparison with other developed stock markets. There are a few numbers of brokers, limited number of listed companies, very few transactions and most importantly investors are unknown about the stock market. If there occur a single malpractice in the functioning of securities market, the whole capital market may damage the national economy badly and if once the investors' confidence were lost it would very difficult to bring it in original condition. Therefore, many problems are found in the field

of public offering in Nepalese stock market rather than other developed countries. In the current situation single investor can apply hundreds of application showing dummy names. As a result they can capture large number of shares. When a single investor captures large number of share, he can influence the company management and stock price too.

There are various types of obstacles existing initial public offering stages in Nepal. In developing country like Nepal, Initial Public Offering is still new phenomenon. The study is concerned with following issues:

- Why people invest their money in stock?
- Why do most of the firm do not like to go to public?
- What are the factors determining sound decision regarding the investment in stock?
- To what extent do responses (over and under subscription) to IPO affect the stock prices?

Therefore, many problems are found in the field of public offering in Nepalese stock market rather than developed countries. Besides these, there are other factors, which slow down the pace of stock market growth in Nepal. They are unfavorable macroeconomics condition, political instability, unconfident investors, weak tax system & slow privatization process.

### **1.3 Focus of the Study**

The focus of the study is on the general investors in Nepal, the volume and portfolio of their investment, and the deceive factors they consider while selecting companies for investment. But the study is also highly concentrated on investment in the stock market, how the investment opportunity on such companies is perceived and made by the general investors could have important impact on the capital market of the country. In the fiscal year 2010/11, 7 commercial banks, 21 development banks, 16 financial institutions

and 2 insurance companies get licensed for initial public offering and right share to the amount of Rs. 777,290,000. (*SEBON: annual report 2010/11*)

Those who own Industrial Units have also trading firms for export and import, and are also involved in various services including banking and finance. If such companies want to “go public”, then the degrading image of their share in the market would definitely hinder the successful completion of public offering of their securities as the investors have declining confidence in their performance.

Hence, the study is aimed at revealing those core factors which could be derived from the investor’s view whether to invest or not in the particular company. Such information generated will help the issue manager to decide which factors should be evaluated to determine if the public offering of the manufacturing firm (issuing company) will be successful or not. The study helps us to find out legal provisions, possibilities, problems and prospects of Initial Public Offering in Nepal. 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.

#### **1.4 Objectives of the Study**

This study focuses on the public response to the primary issue of share in the perspective of Nepal. This study is being undertaken to evaluate the problem and prospect to Nepalese primary share market. 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 access the general views and uses of IPO.
- To analyze the current situation of share market and its management.
- To examine the public response to the IPO.

### **1.5 Significance of the Study**

Stock market reflects the situation of economy. When stock market is booming the economy is good and market is declining the economy is in recession. It represents also the countries policies towards industries. Policy is formulated of regularized by rules and regulation between different Act and Guideline (rules and regulation). This study is needed to find our problems and prospects in the near future. What policies can be formulated, what regulatory acts are needed and necessity of amendments regarding the rules and regulation to develop it and make the market perfect functioning.

It is also needed to find out the views of potential investors and other financial institutions about the related organizations. It will also help to find out the financial status of public going companies. From this study, policy makers will get the knowledge of practical existing rules and regulation. In Nepal, there is still lack of study about initial public offering. Therefore, this study is expected to be helpful for the general investor and the organizations that directly or indirectly related in Public Offering.

### **1.6 Limitation of the Study**

The study mainly focused to analyze certain aspects of primary market in Nepal. The result obtained from this study cannot be generalized. This study tries to explore primary market and its problems in Nepalese capital market. Both primary and secondary data are analyzed. However, this study has some limitations, which are listed as below:

- This study is based on primary as well as secondary data. The secondary data are collected from NEPSE, SEBON, concerned organization and from different financial journals; therefore, the error may exist as they publish.
- Primary data is based on the answer of the respondent. So, it is subjected to be different according to loyalty of the respondents.

- This study covers past and present state of the stock market and investors in Nepal.
- Only selected statistical and financial tools have been employed in this study.

## **1.7 Organization of the Study**

The study organized into five chapters, each devoted to some aspect of initial public offering in Nepal followed by financial institutions in Nepal. The fields of each of these chapters are as follows:

### **Chapter 1: Introduction**

This chapter already contains general background of the study, statement of the problems, focus of the study, objectives of the study and organization of the study.

### **Chapter 2: Review of Literature**

This 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.

### **Chapter 3: Research Methodology**

This chapter describes 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.

### **Chapter 4: Data Presentation and Analysis**

This chapter deals with the presentation and analysis of both primary and secondary data by using mathematical tools and it deals with major finding of the study.

## **Chapter 5: Summary, Conclusions and Recommendations**

This chapter states summary, conclusion and recommendation of the study. The bibliography and annexes are incorporated at the end of the study.

Recommendation sheet, Viva-voce sheet, Declaration, Acknowledgement, Table of contents, List of table, List of figure, Abbreviation has been included at the beginning of this report where as bibliography and appendixes have been included at the end.

## **CHAPTER II**

### **REVIEW OF LITERATURE**

Review of literature means reviewing research studies or other relevant propositions in the related area of the study so that all the past studies, their conclusion and deficiency may be known and further research can be conducted. It is an integral and mandatory process in research works. For this research study the literature survey will be done by consulting libraries, various journals, articles textbooks and other contemporary materials in this study. *(Joshi; 2011:74)*

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. 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 reviews 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 is divided into two parts like conceptual framework and review of related studies.

#### **2.1 Conceptual Framework**

This chapter outlines the theoretical framework underpinning this study. Generally, theory serves as the conceptual architecture, sharpening the context of the study while situating the topic within a broader theoretical discussion. However, it bears mentioning that no one framework is able to capture all of the complexity related to IPO performance.

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

Market in which long term as well as short loan is provided is called financial market. It provides forum in which supplier of funds and user of funds

transaction 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. A financial market can be defined as mechanism bringing together buyers, sellers and financial assets in order to facilitate trading. Financial market is a place, where securities are bought and sold, the facilities and people engaged in such transaction the demand for and availability of securities to be traded and the willingness of buyers and sellers to reach agreement on sales. Financial market plays as an active market where capita resources are transferred from savers to users, where savers let users to use their saving in expectation of multiplied returns from users in specified time period. Financial market consists of capital market and money market. Transactions in short term debt instruments or marketable securities takes place in the money market where long term securities (bonds and stocks) are traded in the capital market. (*Gitman, 2001:30*)

### **2.1.2 Capital Market**

Capital market is the long term funds. Capital market can play vital role to invest on the corporate sectors by the means of securities. The capital market is a financial relationship created by a member of institutions and demands of long term funds (funds with maturities of more than one year) to make transactions. Included among long term funds are securities issue of business and government. The backbone of the capital market is formed by the various securities exchanges that provide a forum of debt and equity transactions. The smooth functioning of the capital market which is enhanced through the activities of investment bankers is important to the long-run growth of business (*Gitman, 1992:456*). The capital market is the trading center for the financial instruments. In capital market different types of financial securities such as ordinary share, preference share, treasury bills and debenture are traded. This market can be divided into two parts:

### i. 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 debentures. Financial transactions such as banks, business houses, saving institutions are individuals come under this non-securities market.

### ii. Securities Market

The security market is known as the market where all types of securities are traded. Security market is 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 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 market in new securities are sold is called primary and the market in which existing securities are resold is called the secondary market. Secondary market are created by themselves actually buying and selling dealers set price at which 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:

#### **A. Primary Market**

In the definition of Primary market made above an addition is to be made. That is depending upon the company offering securities for the first time or in succession, primary market can have public offering as initial public offering or the successive public offering or so on.

#### **B. 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, dealers 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 the 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 and primary market) has been able to acquire securities on the secondary market.

### **2.1.3 Why to go Public and why to Raise?**

The decision to go public is one of the most important and least studied questions in corporate finance. The conventional wisdom is that going public is simply a stage in the growth of a company. The probability of an IPO is positively affected by the stock market valuation of firms in the same industry company's size is significantly correlated with the probability of listing what is more surprising is how a large company must be before it considers going public. In United States, many starts up companies go public to finance their expansion.

This leads to investment of the stock market to investment and growth companies appear to go public not to finance future investment and growth, but to rebalance their account after high investment and growth IPO's are also followed by lower cost of credit and increased turnover in control. Going public provides studies: It enables companies to borrow more cheaply. IPO's are followed by an abnormally high turnover in control. This occurs even though the controlling group always retains large controlling block after the IPO. Going public raise cash usually a lot of it being publicly traded also opens May financial door.

Because of the increased securities public company can usually get better rates when they issue debt so long as these market demanded, a public company can always issue more stock. Thus, mergers and acquisitions are easier to do because stock can be issued as part of the deal. Trading in the open markets means liquidity. This makes possible to implement thing like employee stock ownership plans, which helps to attract top talent. (*Pagano, Paretta & Zingles; 1998:112*)

#### **2.1.4 What are Some Good Methods for Analyzing IPO's?**

Initial public offering IPO is unique stocks because they are newly issued. The companies that issue: IPO have not been traded previously on an exchange and are less thoroughly analyzed than those companies that have been traded for long time. Some people performance provides a buying opportunity while others think that because IPO's have not yet been analyzed and scrutinized by the market, they are considerably riskier than stocks that have a history of being analyzed. A number of methods be used to analyze IPO's but demonstrated past performance analyzing them using conventional means becomes a bit trickier.

If we are lucky enough to have a good relationship with our broker, we may be able to purchase oversubscribed new issues before their clients. These tend to appreciate considerably in price as soon as they become available on the market because demand for these shares is higher than supply the price of oversubscribed IPO's tends to increase until supply and demand come into equilibrium (*www.investopedia.com*).

Here are some points that should be evaluated when looking at a new issue:-

- Why the company elected to go public?
- What will be the company doing with money raised in the IPO?
- What is the competitive landscape in the market for the market for the business's product or services? What is the company's position in this landscape?

- What are the company's growth prospects?
- What is business or company's operating history of any?

IPO is first sale of stock by a company. Companies can be either private or public. Going public means a company is switching from privately ownership to public ownership. Going public raises cash and provides many benefits for the company. Many start-ups went public without any profits and little more than a business plan. For those getting in on a hot IPO is very difficult, if not impossible.

The process of underwriting involves raising money from investors by issuing new securities. Companies' hires investment banks to underwrite an IPO. It's hard to enough to analyze the stock of an establishment company. An IPO company is even trickier to analyze since their will not be a lot of historical information. Look for the usual information and at the same time pay special attention to the management team and how they plan to use the funds generated from the IPO. At the same time we should analyze the underwriters as well. Successful IPO's are typically supported by the brokerages that have the ability to promote a new issue well. Be more of smaller investment banks because they may be willing to underwrite any company. *(Francis; 1992:214)*

## **I. Public Offerings**

It is raising of long term funds for government 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 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.

### **a. Advantages of an IPO**

As discussed above, the primary reasons for conducting an IPO are raise money and to create liquidity for investor, there are also important incident benefits to going public. Objectives benefits include (i) obtaining a readily ascertainable market value for the company's stock, (ii) the ability to make acquisition 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 objectives benefits are the sense of success and accomplishment that accompanies a successful IPO and becoming a publicly traded company.

### **b. Disadvantages of an IPO**

The major disadvantages 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, transaction 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 be 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 are the indirect costs of the time required to be spent on these matters by management.

Also, the management and government of a publicly traded company are more difficult and less flexible. The solicitation of stockholders 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 stockholders' 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. (*Francis; 1992:216*)

### **c. Timing of an Initial Public Offering**

Obviously, not all companies that would like to go public are in a position to do. 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 increase 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 well written business plan to present to prospective underwriters, and (v) attorneys, accountants and public relation 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 issuers in a company's particular industry at the time that the IPO is undertaken. 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. (*Van Horne; 2000:202*)

### **2.1.5 Money Market**

Money market is the market for the short term securities like bills, government bonds, certificates of deposits, bankers' acceptances and commercial paper or promissory notes. It includes both primary and secondary market activities. The money market exists because certain individuals, business, government and financial instruments have temporarily idle funds that they wish to place in some kind of liquid asset or short term interest earnings instruments like this other individuals, business, governments and financial institutions are in need of seasonal temporary financing. Thus, the money market provides the platform for the supplier (who have idle fund for some period) and demand makers of short term liquid funds.

In theory, we found money market is different from the capital. In practice, however in exist countries with efficient financial markets, where money and capital market is combined, the merchant banks are active in both. This is because negotiable market instruments for all practical purpose are simply a short term capital market instruments. Therefore, the techniques and facilities needed to operate money market are almost same as those needed to operate the capital market. (*Mayo; 2006:125*)

### **2.1.6 Common Equity Stock**

There are the offering that entitle the holders or the buyers of the offering the stake on the equity of the issuing company. In addition that are entitled to:-

- Voting right at the general meeting of the company and have the right to control the management of the company.
- Right to share the profits of the company's in the form of distribution of dividend and bonus shares.
- In the event of the winding of the company equity shares capitals are repayable only after repayment of the claims of all the creditors and performance shareholders.

### **2.1.7 Preference Shares/ Preferred Stocks**

Preference shares capital mean, in the case of a company limited by shares that part of the capital of the company, which,

- Carries a preferential right to payment of dividend during the time of the company.
- Carries on a winding up a preferential right to be repaid the amount of capital paid up.
- The different types of preference share:
  - Cumulative preferred stocks
  - Non-cumulative preferred stocks.
  - Redeemable preferred stocks.
  - Non-redeemable preferred stocks.
  - Convertible preferred stocks.

### **2.1.8 Bonds/Debentures**

Debenture includes debenture stock bonds and any other securities of a company, whether constituting a charge on the assets of the company or not. Debenture is a document that either creates a debt or acknowledges it, and any document, which fulfills either of these conditions, is debenture. The characteristics feature of a debenture is as follows:-

- It is issued by the company and is in the form of a certificate of indebtedness.
- It usually specifies the date of redemption. It also provides for the repayment of principal and interest at specified date or dates.
- It generally creates charges on the undertaking of the company.

The different types of debenture are:-

- Secured debenture.
- Unsecured debenture.
- Redeemable debenture.

- Perpetual debenture.
- Convertible debenture.

### **2.1.9 Warrants**

The warrants gives a right to the holder to obtain equity shares specified in the warrant after the expiry of a certain period at a price not exceed the capital price specified in the warrants. The warrant is a tradable and negotiable instrument and is also listed on the stock exchange. It comes in different forms. Such as:

- Bonds with warrants
- Preferred stocks with warrants.
- Beside their instruments there is other instrumental mix available to the investment bankers to provide to the primary market investors. But there are beyond the scope of this manual to describe.

### **2.1.10 Convertible**

Convertible are bonds or preferred stock that can be exchanged for stated number of common stock at the option of the holder within stipulated period of time. A bond can be converted into preferred stock or common stock while the preferred stock can be converted into common stock only. Conversion features increases the marketability of the security. Unlike the exercise price of warrants, the debt and preferred stock is simply replaced by common stock but does not provided additional capital. (*Thapa and Gautam; 2011:202*)

At first time in Nepal, the convertible preferred stock is issued by Everest Bank Limited in 2007 but convertible bond are not practice till date. Beside these instruments there is other instrumental mix available to the investment bankers to provide to the primary market investors. But, these are beyond the scope of this manual to describe.

### **2.1.11 Primary Market and Initial Public Offering**

The primary market itself can be subdivided into seasoned and unseasoned issues. A seasoned 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. This unseasoned new issue is often referred to as Initial Public Offering.

When a company wants to raise funds from the public, it issues securities at first time and announces to the public to exercise the offering and this announcement for the public to raise funds is called Initial Public Offering. It is the raising of long term funds for governments or corporations from a 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 sources of funds on a permanent basis. Public issue means raising of capital directly from the public. Issue of equity obviously creates a value for a company and no doubt it is the major source of capital. (*Van Horne; 2000:220*)

Thus IPO involves raising of funds for governments or corporations from the public through the issuance of various securities in the primary market and is often the only major source of obtaining large sums of fixed rate, long term funds.

### **2.1.12 Investment Considerable to the Potential Investor in the Primary Market**

Rules and regulations alone would not be able to protect the interest of investors. They should be able to analyze and evaluate following their investment decision.

- Investor should select those companies whose shares are regarded as well operating and good future prospects, reliable management, beneficial sectors or higher growth investing in the shares of these companies is less

risky than others. The investors who invest in stock, they must compare the price and the value of the share in the market and should select the share which has lower market price in comparison to its value.

- The investors should take information regarding company's promoters, management effort and efficiently, risk bearing capacity, size, growth, environment, and board directors. Financial status (net worth profit/loss situation etc.) and as well as budgeted statements which can be obtained from memorandum, prospectus. Article so of the concerned company.

### **2.1.13 Investment Consideration to the Potential Investors in the Secondary Market**

Investors should be informed about the following matters before investing in the secondary market.

- Keep information of the companies return to the shareholders in the form for cash dividends, stock dividends, bonus share etc. They should also be informed about earning per share (EPS), book value per share (BVS), price earnings ratio (P/E Ratio), future plan, growth expectancy of the annually, quarterly and half yearly performance reports, profit and loss accounts(P/L A/C). Balance sheet (B/S) and annual reports.
- Analyze the price related information provided by SEBON and NEPSE about the listed companies.
- Study the trading statement and financial analysis of the listed companies published by NEPSE.
- Study articles related to the trading of shares and economic matters published in different newspapers and magazines.
- Study the annual report of SEBON.
- Study the act and regulation concerning to the shareholder's right.
- Once the investors think of, making investment, he approaches to the brokers to choose a firm that is suitable for his needs of investments and select a representatives of the firm with whom he can work. The

representative should be able to furnish the investor, at all times on reasonable choice, information on any specific company's securities.

#### **2.1.14 Pricing Difference**

We may have found that there can be large difference between the price of an initial public offering (IPO) and the price when the IPO shares start trading on the secondary market.

The pricing disparities occur most often an IPO is hot or appeals to many investors when an IPO is "hot" the demand for the securities far exceeds the supply of shares. The excess demand can only be satisfied once trading in the IPO shares begins. This imbalance between supply and demand generally causes the price of each share to rise dramatically in the first hours or days of trading generally causes the price of each share to rise dramatically in the first hours or days of trading. Many times the price falls after initial flurry of trading subsides. (*Reilly; 2008:222*)

#### **2.1.15 IPO by Private Company to the Public**

IPO's are often issued by smaller younger companies seeking capital to expand and also can be done by large privately owned companies looking to become publicly traded. In an IPO, the issuer obtains the assistance of an underwriting firm, which helps it determine what type of security to issue (common or preferred) best offering price and time to bring it to market.

#### **2.1.16 Risky Investment**

IPO's can be risky investment for the individual's investors, it is tough to predict what the stock will do on its initial day of trading and in the near future since there is often little historical data with which to analyze the company. Also, most IPO's are of companies going through a transitory growth period and they are therefore subject to additional uncertainty regarding their future value.

### **2.1.17 Pricing**

Initially, IPO's have been under-priced. The effect of under-pricing and IPO is to generate additional interest in the stock when it first becomes publicly traded. This can lead to significant gains for investors who have been allocated shares of the IPO at the offering price. However, under-pricing an IPO results in "money left in the table" lost capital that could have been raised for the company had the stock been offered at higher price.

The danger of over pricing is also an important consideration. If a stock is offered to the public at a higher price than what the market will pay, the underwriters, may have trouble meeting their commitments to sell shares, even if they sell all of the issued shares, if the stock falls in value on the first day of trading it may lose its marketability and banks even more of its value. (*Chaudhary; 2005:158*)

Investment banks therefore take many factors into consideration when pricing IPO, and attempt to reach offering price that is low enough to stimulate interest in the stock, but high enough to raise adequate amount of capital for the company. The process of determining an optimal price involves the underwriters "syndicate" arranging share purchase commitments from lead institutional investors.

### **2.1.18 Institutions Involved in IPO in Nepal**

This chapter covers different institutions that are involved in the process of IPO and explained in detail the context of Nepal.

#### **i. Issuing Companies:**

Issuing Companies are those companies that are committing IPO to raise required capital for the company from the public. It is also known as the issuer. The issuing companies may be government, private institutions, corporations etc. Their major objective is to raise the required capital to the

company from general public. Several rules and regulations of SEBON should be followed by the issues managers.

According to Company Act, 2062 only public limited companies are allowed to enter in IPO. Section 10 (c), Company Act, 2062 has specifically stated that private company should not issue their share and debenture in public.

## **ii. Issue Manager:**

Issue manager is an institution who is responsible to manage the initial public offering. As per the Securities Act, 2062 Issue managers are institutions holding license from the NEPSE to manage IPO. Till fiscal year 2010/11 SEBON has authorized 16 finance companies (i.e. 7 companies renewed their license and 9 new companies get licensed on fiscal year 2010/11) to serve as issue managers. Issue managers get commission from the issuing company in return. (*Annual report 2010/11 of SEBON*)

Issue managers are the securities businessman who carries out the functions related to public offering on behalf of public company in primary market. They act as a middle man for the distribution of new securities. Hence in conclusion, the people who are responsible for searching investors for the Initial Public Offerings of securities sold in primary market is known as Issue manager. Securities Dealers is a security businessperson who buys securities in his name at the primary market and sells from secondary market either in his own name or on behalf of customers name through Stock Broker. A dealer buys securities at low price and expects to sell then at higher price. They benefit from buying at low and selling at high price.

## **iii. SEBON:**

SEBON is a supreme body of Nepal which regulates the Nepalese securities market. Both the primary as well as secondary market is supervised by SEBON. All financial managers, brokers, investors and general public follow

the rules and regulations published by SEBON. If anyone don't follow and obey its rules will be penalized legally.

SEBON was established on June 7, 1993. Since its establishment, SEBON is trying to improve the legal and statutory frameworks with regards capital markets, issues managers, brokers, dealers, investors etc. the major framework for the securities market is provided by Securities Act,2006 which has given authority to SEBON for the regulation of securities market.

SEBON has its own Board of directors. The board of directors consists of seven members including one full time chairman appointed by the Government for tenure of four years. Other members of the Board include joint secretary of Ministry of Finance, joint secretary of Ministry of Law, Justice and Parliamentary Affairs, representative from Nepal Rastra Bank, representative from Institute of Chartered Accounts of Nepal, representative from Federation of Nepalese Chambers of Commerce and industries, and one member appointed by the Government from among the experts pertaining to management of securities market, development of capital market,financial or economic sector.

Currently, SEBON is focusing on certain activities such as improving corporate governance, improving policy and procedures of securities market, enhancing professionalism of securities businesspersons and developing a clear rules and regulations for merchant banking business. The major functions, duties and powers of SEBON as per the Securities Exchange Act, 2006 are as follows:

- Register securities and approve prospectus of public companies.
- Provide license to operate stock exchanges.
- Provide license to operate securities businesses.
- Permit the operation of collective investment schemes and investment fund program.

- Draft regulations, issue directives and guidelines, and approve by laws of stock exchange.
- Supervise and monitor stock exchanges and securities business activities.
- Take enforcement measures to ensure market integrity.
- Review reporting of issuer and listed companies, and securities businessperson.
- Formulate policies and programs relating to securities markets and advice the Government of Nepal as and when required.

#### **iv. Investors:**

A person who invests their money in financial sector as an expectation of return is known as investors. The primary objective of an investor is to maximization of return and minimization of risk. Investors are those persons who are willing to invest on securities issued in the primary market. They are those persons who are willing to accept a higher level of risk in the hope of collecting higher profit.

#### **v. Banker to the Issue:**

Banker to the issue is commercial banks where application and money are deposited off as and when asked by issue managers. The main responsibility is to provide custodian service to the issuing company. Securities Issue and Issue management Guidelines, 1997 states that issue manager should manage to deposit the collected amount and application in the account of banker to the issue.

The guidelines also states that the collected application and amounts are kept under the custody of both issue manager and banker to the issue until the allotment of the securities. Banker to the issue may also be involved in the process of realizing he proceeds of issue through cheque/draft and release final

certificates to the issue manager for the number of applications and amount collected.

#### **vi. Intermediaries**

In capital market intermediaries means the persons or institutions acting as a middleman between issuing companies and investors. Intermediaries take temporary position of securities during a time period in between a flow of buy orders and a flow of sales order and make earning from the variation in supply the another source of income of intermediaries. At present, it has 38 brokerage firms and 16 issue managers.

Various activities are involved in primary and secondary market. Intermediaries provide services to customers for buying and selling securities, issuing securities, counseling, portfolio management etc. SEBON provides different Acts, rules and regulation and guidelines related to intermediaries for fair securities market.

Stock Broker is a security businessperson who deals on behalf of the investors in buying and selling of securities of listed companies. A stock Broker acts as a middleman who matches buying and selling orders, thereby securing both buyers and sellers. As a member of stock exchanges and a sub-broker as any person who acts on behalf of a Stock Broker as an agent or otherwise, assist the investors in buying and selling or dealing in securities.

#### **vii. Market Maker**

Market Maker is a security businessperson who deals with bonds issued by the government or bond issued as per the guarantee made by the government. It carries out functions relating to public issue of mutual fund, unit fund and buying and selling of equity shares in her/his own name of at least three organized institutions with the objectives of providing liquidity of them.

In fiscal year 2006/07, SEBON provided government bond trading licenses to the securities businesspersons fulfilling the criteria as required by of the Government Securities Trading Management By law, 2005.

**viii. Others:**

**A. Company Registrar's Office (CRO)**

CRO is the regulating body for any institution registered under Company Act, 2053. CRO is the only agency where companies are registered, monitors the operations of the companies and makes arrangements for winding up of the companies when required. As per the Company Act, 2006 public companies must get approval from CRO by publishing its prospectus before carrying out any public issuing activities. CRO check whether relevant information intact with the rules and regulating as prescribed by regulating authorities and if any changes to be made company must be informed within 15 days of received of prospectus.

**B. Nepal Rastra Bank (NRB):**

Nepal Rastra Bank is the central bank of Nepal. It was established in 1956 under the Nepal Rastra Bank Act, 1955, to discharge the central banking responsibilities including guiding the development of the embryonic domestic financial sector. Since inception, there has been a significant growth in both the number and the activities of the domestic financial institutions. The role of NRB in IPO process is to grant Financial Institution approval to involve in different issuing activities. And even to carry out Merchant Banking activities, NRB gives approval.

**C. Nepal Stock Exchange (NEPSE)**

NEPSE Ltd. is a nonprofit organization, operating under Securities Exchange Act, 1983. The basic objective of NEPSE is to impart free marketability and liquidity to the government and corporate securities by facilitating transactions in its trading floor through market intermediaries such as brokers and market

makers. NEPSE opened its trading floor on January 13, 1994 through its newly appointed licensed members and has adopted an “Open Out-Cry” system for the transaction of securities. The trading floor is restricted to listed corporate securities and government bonds with the market intermediaries in buying and selling of securities. The issue manager must get a membership from stock exchange to conduct primary issues.

NEPSE has started automated trading from the date of August 24, 2007 with several features in its automated system. The system is compatible with international practices and it has given due consideration in prevailing laws and practices. The system is also able to eliminate all the possible human errors in the “Open Out-Cry” trading procedures. Therefore, several modifications are made to customize the existing rules and regulations of the country.

#### **2.1.19 Valuing IPOs**

Consistent under-pricing raises the issue of valuation i.e., whether the issuer side or the investor side prices the offering according to the expected net present value of the offering. Since the issuing company in an IPO has no prior trading history, it also lacks a valued market price, which could be used as the issue price. Therefore, the most common way to value an issuing company is by surveying its financial information and comparing it to similar already traded companies. As noted, the results of this type of evaluation are heavily affected by a company’s prior financial performance and accounting information.

In reality, this method of valuing companies is not very effective, since most companies that are going public do so in order to gain resources to grow, while in transition into the next stage in its life cycle. Taking this into account the value of the issuing company is in its growth potential, and not in its historical performance. Reliance on such comparative company analysis in the pricing of IPOs has also been proven to have a very weak ability to explain IPO pricing,

even in cases when earnings forecasts have been included in the analysis. (*Ritter and Moonchul 1999, 417*)

Other research has also shown that IPOs are priced around 50 percent higher than comparable companies that are already traded. In addition, it has been documented that there is a positive relationship between the amount an IPO issue is priced over the average price of similar traded companies and long-run underperformance. (*Ritter and Welch 2002, 1816*)

### **i. The Underwriting Process**

Underwriting is an agreement between the issuing company and financial institution and financial institution like bank, merchant bank, broker or other person, providing for their taking of the shares or debentures to the extent specified in the agreement. Getting a piece of hot IPO is very difficult, if not impossible. To understand why we need to know how an IPO is done, a process known as underwriting when a company once to go public the first thing it does is hire an investment bank is requires. Underwriting is the process of raising money by either debt or equity. We can think of underwriters middlemen between companies an investing public. The biggest underwriter in our Nepal are Nepal merchant Banking & Finance Ltd. Co. (NMBL), Citizen Investment Trust (CIT), NIDC capital market (NCM) etc.

The company and the investment bank will first meet to negotiate the deal items usually discussed include the amount of money a company will raise, the types of securities to be issued and all the dealt in the underwriting agreement. The dealt can be structure in a variety of ways. For example in firm commitment, the underwriting guarantees that a certain amount will rise by buying the entire offer and then reselling to the public. In a best efforts agreement, however, the underwriter sells securities for the company but does not guarantee the amount raise. Also, investment bank does not been all the risk of offering. Instead they form a syndicate of underwriters. One underwriter

leads the syndicate and the others sell a part of the issue. Only a limited number of brokers, dealers are invited the syndicate member themselves do not receive equal allocation of securities for their clients.

During the cooling off period the underwriting puts together what is known as the red-herring. This is an initial prospectus containing all the information about the company expects for the offer-price and the effective date which are known at this time. The company act has made mandatory that any institution going into public offering must the prospectus before issuing the securities to the public. With the red-herring in hand the underwriter and company attempt to hype and build of interest for the issue. They go on road-show, also known as the (dog and pony show) where the big institutional are courted.

As the effective date approaches the underwriter and the company sit down and decide on the price. This is not an easy decision; it depends on the company, the success of the road-show and most importantly, current market condition. Of course it's in both parties interest to get as much as possible. Finally, the securities are sold on the stock market and the money collected from investors.

## **ii. Role of Functional Managers**

Issue managers are also known as investment bankers or underwriters. They are the major players of the primary market who for the commission called underwriting commission. There is efficient functioning of financial institutions. One of these institutions is an investment banker or issue manager firm the firm acts as a middlemen in the distribution of new securities to the public and creates a primary market. Therefore the people or institutions responsible for finding out investors for the initial public offering (IPO's) of securities sold in the primary market are called investment bankers (*Bhattarai; 2006:13*).

Before the amendment of securities exchange act and securities exchange regulation, there were few makers namely Citizen Investment Trust, NIDC Capital Markets Ltd, Rastriya Banijya Bank except Gaurishankar Finance Company Ltd, all others markets makers were actively involved in issue management activities. After the amendment in act and regulation, additional five organizational were permitted to provide issue management service. Among the new entrants are Nepal Sri-Lanka Merchant Banking and Finance Ltd., United Finance Ltd., Himalayan Securities and Finance Ltd.

However, this scenario has been streamlined by second merchant in securities exchange act and regulation by providing separate class of membership in Nepal Stock namely securities dealers (primary market) as per the company act, 2053 all the companies are required to appoint issue manager for raising capital from the general public allotment and other related matters.

Total capital base required to be eligible for markets and securities dealers is rupees 1.5 million paid of capital license for market making and securities dealers is issue to corporate bodies only. Securities dealer are categorized into two securities dealers (primary market) and securities dealers (secondary market).

The role of securities dealers (primary market) is confined to provide and post issue management services, underwriting services and other related services established by dealers. Hence, in today, world of interest and information technology, it is quite popular in USA but in context of Nepal, there not the provision of third and fourth market. Hence organize stock exchange or NEPSE, there not the provision of third and fourth market. Hence organize stock exchange or NEPSE is only place where transaction are done.

This process of issuing securities to the public is called underwriting is caked underwriting and, in this sense, the investment bank is also called an underwriter. The group of underwriter is called an underwriting syndicate. In

other countries investment bankers also provide brokerage services but in Nepal the issue manager only manage initial public offering and provide financial services. Nepal Merchant Banking and Finance Ltd. (NMB), National Finance Company Ltd. (NFL), Citizen Investment Trust (CIT) etc. can be taken as example of issue managers in Nepal managers in Nepal.

### **iii. Functions of Issue Manager or Investment Bankers**

An investment banker performs many others functions rather than only underwriting the securities. This functions as follows:

#### **Advisory**

In the first new meetings with a potential securities issuer, issue manager typically serve as a advisor. The underwriting help the issuing firm analyze it's analyze its financing needs and suggest various ways to raise the needed funds. The underwriters may also function as an advisor in mergers, acquisitions and the re-financing operations. So we can say that basic advisory functions are:-

- Advising the potential security issuer.
- Suggesting various ways to raise needed funds.
- Advising about mergers, acquisitions and refinancing operations.

#### **Administrative Functions**

The investment bankers still are with the issuer the responsibilities of seeing that everything is doing accordance with the relevant securities law. The SEBON Nepal requires that must primary issues be accompanied by negotiation statement the law provides that all investors must have prospectus before they can invest. So, the basic administrative functions can be as follows:

- Filling of the registration statement for issue approval in accordance with laws.
- Producing prompts after the issue approval by securities board Nepal and then distributing to the potential investors.

## **Underwriting**

Underwriting refers to the guarantee by the investment banker that the issues of the new securities will receive a fixed amount of cash. The fine gap between the investment banking houses' purchase of an issue from the issuer at the time they sell it to the public is risky. Because of enforcing changes in market conditions, the underwriters may not be able to sell it at less than the price they have paid for it. So, the basic underwriting functions include:

- To purchase securities from issuers and resell them to the public.
- The resale price must be neither too high nor too low.
- Underwriting functions also include private placement where the investment banker acts as an intermediary in bringing together the issuer and investors.

## **Distributions**

Investment bankers can distribute securities to investors in different ways. The investment banker may issue the securities and then sell them, or the investment banker may act as an intermediary in bringing together the issuer and investors in a private placement. So, the distribution functions can be concluded to distribute the shares to the general public offer underwriting.

## **Other General Functions may be**

- To suggest the company in issuing shares (about the subscription of bond/ shares etc.) e.g. Nepal Merchant Banking.
- To manage the issue i.e. time management of the issue.
- To underwrite securities.
- To collect funds.
- To distribute securities etc. (*Bhattarai, 2006:14-15*)

### **2.1.20 Securities Registration and Issue Approval Guidelines, 2000**

In order to make the process of registration and issue approval simple, fairness and transparent SEBON provided these guidelines under the securities Act 1983

- The company should at least one year and audited balance sheet and profit and loss account should be published during that period.
- With Regards manufacturing companies, the land for factory, office building and storage should purchased, reliable and important equipments should purchased, reliable and important equipments should be purchased, information of term loan and approval of the company from the respective organization should be completed.
- With regards to banks, finance companies, insurance company, business enterprises and other services oriented company, the companies should completed the important infrastructure and should be approved by the respective organization for the issuance of securities.
- The issuer company should carry out general meeting with new shareholders. The company must listen to complain regarding to the issuing securities and should be solved them as soon as possible. The company should obey all the rules, and guidelines issued by Government and SEBON.
- The risk of financial, managerial inflation legal process, globalization, change in government acts and regulations and other important information should be available easily.
- Once the application for the public issue is approved by the SEBON, the IPOs have to make within two months. IPOs should be offered at fixed price as approved by the SEBON for public subscription s that should be opened at least for 5 working days.
- If the company desires to issuer right shares, ordinary shares should be completely issued and should be registered in the stock exchange market. If the company desires to issue at premium, the company must be profitable for two years and the net worth per share must be greater

than net capital. And if the company desires to issue debenture, the objectives taken from amount, time frame of interest, duration, place and process should be clearly mentioned. Moreover the company's property should be audited by specialist and should be approved from NRB.

- The issuing securities should be registered in Stock Exchange Market for the transaction within 45 days from the date of share allotment.

### **2.1.21 Securities Issue and Issue Management Guidelines**

According to Securities Exchange Act 1983, Section 35(A), SEBON issued this guideline to manage the process of issuance of securities and to make fairness of the issue managers working pattern.

The major points of the guidelines are as follows:

- The respective securities issuance and issue manager should be registered with SEBON under Section 19, Securities Act 1983.
- The issue manager should keep in account whether the issuing securities may register in Stock Market and Securities Exchange Act, 1983.
- The issue managers should have a detail about the company's organization structure, financial status, objectives of issuance of securities and service provided by the company before preparing prospectus.
- Issue manager should kept all the photocopy of approved and registration of securities by SEBON, agreements and all submitted information to SEBON for the easily available information for investors and securities businesspersons.
- The issue managers should listen complains about the issued securities and should be solved as soon as possible.
- The information regarding company, its establishment date, total number of share issue, share price, issue date, number of application, subscription number, share allotment, capital collected etc should be submitted to SEBON after 90 days of closure of securities distribution.

### **2.1.22 Share Allotment Guidelines**

To make allotment fairness and transparent of public issued securities, SEBON issued this guideline. The main points described in this guideline are briefly explained below.

- Share allotment should be made under management describe on Company Act 1997.
- The application number should be collected from the collection center that application should be separated according to qualification, uncompleted information, unsigned application, and amount not deposited according to the application and having double signatures.
- The filtered application should be classified according to the total number of application and application per share.
- Share should be allotted to all applicants and provisional allotment should make after construction categories
- The information of the share allotment must be published in different newspaper within 3 days of share allotment completed.
- The approval of NEPSE is needed therefore the general practices is to attend the allotment meeting and to approve the allotment module. Besides, the representatives of NEPSE attend the allotment meeting providing guarantee that the allotment is fair.
- If there arise any problem while share allotment, the solution should be made according to the decision of SEBON.

### **2.1.23 Theoretical Aspects of IPO**

A large volume of studies conducted in different part of the world covering different period have consistently indicates two patterns associated with IPO issues: IPO Under-pricing and IPOs Long run Underperformance.

Underpriced IPO are those IPO where the IPO issued price is lower than the actual market price. Determining the optimum offer price of IPO issues is the most difficult for investment banking or the Underwriter. If the issued are

priced low then there is a chance of oversubscription and if the price are too high then it might lead to under-subscription. As a result in withdrawal of issue, this is detrimental for the financial aspect as well as reputation of the underwriter. Therefore, the underwriter does have some incentive to under price the issue. Under pricing exist in every market but extent of under pricing may vary among different countries. We reveled in the study that among 33 countries the IPO under pricing ranged from m lowest of 4.2% to the highest of 38.8%. Number of market study also shows the same result. For example, an initial under pricing of 83% in Malaysia, 31.4% in Singapore, 15.9% in Hong Kong, 35.3% in India. Thus, initial under pricing of IPOs seemed to worldwide phenomena even though the extent of IPO under pricing may vary from one country to another (*Ritter; 1998:124*)

Various theories have explained about IPO. One of the most important theories is that IPO are deliberately under-priced by underwriters. Underwriters will under price the issue to ensure the success of issue. It is one of the easiest methods for them to reward their loyal clients. In the same way the issuing company also wants to underpriced the issue's the typical run up in price will create excitement among investors and might prove beneficial for their future issues.

According to Band Wagon Hypothesis, when the investors buy the new issues after seeing that other investors are also buying then Bond Wagon effects may develop. To prevent it the issuing company may want to under-price the issue to induce few early investors to buy and induce a Bond Wagon in which all the other subsequently investors will want to buy. Another theory is Winner-Curse Hypothesis. It assumes that there exist two groups of investors: informed investors and uninformed investors. Although these theories have been criticized on the ground of extreme assumptions and have various other reasons but the fact remains that each of them does possess a limit of truth in them. Most importantly, they do help to understand under pricing.

#### **2.1.24 Issue Managers of Nepal**

Initial Public Offerings (IPO) involves raising of funds for government or corporation from the public through the issuance of various securities in the primary market. The effective functioning of public offerings requires various numbers of financial institutions. One of the most important institutions is investment bankers commonly called as issue manager. The firm who works as intermediaries between the general public and corporation is known as issue manager. The company who offers public issue to the general public is known as Issuing Companies and the intermediary is known as Issue Manager who conducts the IPO process and works as a mediator between public and company. These activities are performed by Merchant Banker in India, Investment Bankers in U.S.

Merchant Banker stands for providing various services relating to capital market and finance to corporate sector. This includes not only the activities for the above purpose in the country but at times arranging funds from outside the country. The merchant bank also provides consultancy to the corporate sector on the issue like finance, capital structure and investment, mergers, takeover and amalgamations, establishing coordination between the government and corporate sector. In fact the merchant banker should be able to provide guideline to an entrepreneur on all matters from the stage of conception of a project in his mind till it goes into commercial production. A good merchant banker would be considered to be one who is expert, honest, has integrity as well as capacity to develop public relations. Whenever a business concern needs funds from the capital market it would usually approach the merchant banker rather than banks or financial institutions.

As per the Securities Exchange Act, 2006 issue managers are institutions holding licenses from Nepal Stock Exchange (NEPSE) to manage public offering issues. A Merchant Banker has been defined under Securities Businessperson Regulation 2006, Section 2 (2) as any approved securities

businessperson who engaged in the securities issuance and issue manager, underwriting of public issue, providing share registration function and provide investment management function services to investors.

So far, NEPSE has authorized 16 finance companies to serve as issue managers. The issue manager who handled the public offering in Nepalese Capital Market is prescribed in the table.

#### **Lists of Issue Managers of Nepal**

| S. NO. | ISSUE MANAGER                                 |
|--------|---|
| 1.     | Elite Capital Limited                         |
| 2.     | Ace Capital Limited                           |
| 3.     | NCM Merchant Banking Limited                  |
| 4.     | NMB Capital                                   |
| 5.     | GROWMORE Merchant Banker Limited              |
| 6.     | Citizen Investment Trust                      |
| 7.     | Nepal Finance Company                         |
| 8.     | Arniko Capital Management Company Limited     |
| 9.     | Vibor Capital Limited                         |
| 10.    | DCBL Bank                                     |
| 11.    | NSM Merchant Banking & Investment Limited     |
| 12.    | Civil Capital Market Limited                  |
| 13.    | Laxmi Capital Market Limited                  |
| 14.    | Investment Management Merchant Banker Limited |
| 15.    | Beed Investment Limited                       |
| 16.    | NABIL Investment Banking Limited              |

*(Source: SEBON Annual Report 2010/11)*

SEBON has been monitoring and supervising the activities related to the issue managers for the past 15 years. Companies Act 1997, Securities Businesspersons Regulations, 2007, Securities Registration and Issue Approval

Guidelines,2000, Share Allotment Guidelines1999 and Securities Issue & Issue Management guidelines1997 provide the legal framework within which the issue companies and the issue managers perform their public issue and issue management activities.

### **2.1.25 Key Provision Related to Issue Manager to Give Reliable and Standard Services as well as Regulatory Regime Prevalent in our Capital Market.**

- Section 4, Securities Issue and Issue Management Guidelines, 1997 stated that the related securities issuance and issue manager should be registered on SEBON in accordance to Securities Exchange Act, 1983 under 19.
- Section 6.4, Securities Issue and Issue Management, 2000 states that while submitting application In SEBO for issue approval, issue manager should take into account whether the issuing securities are qualified to be listed or not under regulation of securities Exchange market listing and securities Exchange Act 1983.
- Section 6.6, Securities Issue and Issue Management Guidelines, 2000 states that while submitting application in SEBO for issue approval, issue manager should take into account whether the issuer company's managerial, technical, economical aspects and future prospects as well as other information presented justify the public issue.
- Companies Act 1997, states that issuer companies are required to take the services of issue manager for the sale and allotment of securities and refunding.
- Section 9, of the Securities Registration and Issue Approval Guidelines, 2000 states that the issue should be opened within 2 months of the issue approval. If the issue is not opened within the given period, Section 9(3), require issue manager to incorporate the changes, if any, relating to technical, financial, economical and managerial aspects in the prospectus and take issue permission for the same from SEBON.

### **2.1.26 Duties, Responsibilities and Authorities given to Issue Managers by Securities Issue & Issue Management Guidelines, 1997**

- Issue manager should obey and make obey to issuing companies as per Company Act, 1997 and Securities Act, 2005.
- While submitting application for securities registration, issue manager should take in account the points explained in the Securities Issue and Issue Management Guidelines, 1997 with regards issuance of ordinary shares, right shares and debentures.
- While submitting application in SEBON for issue approval, issue manager should take account whether the issuer companies, managerial, technical, economical aspects and future prospects as well as other information presented justify the public issues.
- Issue manager should make agreements with the following authorities:  
A Whether issuer companies taking services of other issue managers. The submitted information of issuer companies are completely fair and transparent related to all auditing information, loan related information and other legal information. It should make agreement about the fair advertisement and marketing program should be implied prescribed by issue manager. While publishing information without the agreement and instruction of issue manager may not be answerable. Agreement should be made about the fair advertisement and marketing program should be implied prescribed by issue manager.
- In case of oversubscription of public issue, issue manager should submit the criteria and report of allotment to SEBON within 7 days of allotment. Similarly issue manager should submit the report relating the issue within 90 days of closure of issue.
- The management of Banker to the Issue to collect the application and amounts from the applicants is the prime responsibilities of issue manager.
- The registration and approval of securities by SEBON before public issuance is the duty of issue manager.

- The public manager should inform the issue companies about the number of application, number of securities applied and collected amounts within 45 days of closure of application.
- The major duties of issue manager are hearing of complaints and solving of those complaints relating issued securities from the related persons.
- The issue manger should obey different code of morality provided by SEBON.

## **2.2 Review of Related Studies**

Several studies are focused in the subject related to initial public offering and capital market. Some of related research article are reviewed in this study, which are discussed as follows.

**Dahal (2007)** has published an article "*The performance of Nepalese IPOs*". It was based on 107 IPOs from the FY 1993-2006. The study mainly focused on subscription times of securities on IPO and IPOs return. After the completion of study, he asserted that Nepalese IPOs had been heavily oversubscribed. The study showed that the investors have very high degree of attraction to the IPOs. It was noticed that Nepalese IPOs in terms of issue and subscription had been bumpy during the study period. It also noticed that the investors make 53.25% market adjusted return leading to conclusion that Nepalese IPOs has highly under priced. On other hand, it showed that due to higher under pricing, higher wealth loosed by the promoter. On the study it is found that IPOs return had been affected mainly by the subscription times of issue and general returns of stock market. The study also revealed that the firm size expressed as the size of total assets affects the subscription times of issued positively and the debt equity ratio affects the same negatively.

**Bhattarai (2009)** has published an article "*Capital Market in Nepal*". The investment environment is changing and capital market itself is changing with the pace of time. In this changing market the investors must be able to change

their investment attitude and habits. Development of National economy demands the development of the capital market. But capital market consists of different components such as primary market and secondary market and different institutions involved and participating there on. Therefore the development of capital market cannot be done within a short span of time. But in present era, the era of capital market is growing rapidly due to the technology advancement. The traditional open out system is substituted by computerized or electronic system. In the same way, the compulsion to carry share certificate has been abolished due to the establishment of Central Depository System. It is the system, which is dematerialized the existing share certificates and issues balance certificates. But we are still working traditional system. Our growth rate is very minimal.

**Joshi (2010)** in his article "*PYC Nepal Journal of Management, 2010*" In both financial & non-financial sectors, dividend and retained earnings significantly explain the variations in the share price. The impact of dividend, however, is much more pronounced than that of the retained earnings. The relationship of dividend and share price is positive in almost all cases although in some cases there is a relationship between retained earnings and share price.

**Dongol (2011)** has conducted a study on "*PYC Nepal Journal of Management*". The majority of respondents were holding securities of commercial banks, development banks and finance companies, as their shares are more popular. Insurance companies, manufacturing and processing, hotel and trading companies are less popular categories of shares in Nepalese stock market. The majority of the respondents are not satisfied with the information disseminated by the corporate firms. Similarly, the majority of the respondents argued that the management does not protect the shareholders' interest. The majority also believe that legal provisions are not adequate in protecting shareholders' interest. "Expectation of increase in market price (capital gain)" is the important motive behind investing in the shares and the second

importance to “Expectation of bonus and rights share”. Likewise, regarding the factors affecting the share prices, majority of the respondents ranked the priority to “announcement of bonus share and right issues,” “political-economic events,” and “announcement of cash dividend” respectively.

While the respondents were categorized on the basis of the respondents’ age, i.e., adult investor group (equal to or less than 35 years old) and 35 plus investor group (greater than 35 years old), most of the respondents have expressed common views on most of the issues. Most of the respondents have been found to have strong belief on impact of new information of price movement of the Nepalese stock market based on the flow of the new information. The Nepalese investors are found to be more aware of the new information announcements. The findings of the survey analysis have indicated that the Nepalese stock market is sensitive to new public information. The Nepalese investors believe that the stock prices are adjusted immediately after the occurrence of new events. This is the positive part of the investors as being rational and way to the efficient market as a developing stock market in the South Asian market.

### **2.3 Review of Previous Thesis**

In titled to *Public Response to Initial Public Offering*, so many master researches have been carried out in Nepalese context as well as in the international market. It makes sense go through these past researches to access the trends of overall IPO and pace of stock in Nepalese market.

**Poudel (2006)** has conducted a research on *"Public response to initial public offering in Nepal"*. The objectives of the study are:

- To identify the dealing process of IPO
- To analyze the pace of IPO
- To analyze the public response to the IPO

The major findings of the study are:

- General investors in Nepal do not have sufficient information regarding the primary market.
- They are interested in financial sector than non-financial sector.
- Pace of initial public offering in Nepal seems to be irregular. Even though the organizations process of public offering is quite long, the service provided to the investors seems to be satisfactory public response in stock market is high due to lack of opportunities for investment in other sector.
- Public are attracted towards shares to increase their value of investment.

**Shrestha (2007)** in her thesis “*Capital Market Development in Nepal*” focus on the identification of the problems associated with Nepalese stock market. The study also had attempted to identify the area that provides the potential for the growth of the market. Looking at her study, the data were collected from both primary as well as secondary data. Primary data are collected through questionnaire distributed to number of persons including SEBON, NEPSE, students, businessman, Brokers and investors. Similarly secondary data are collected through annual report of SEBON, newspaper, books magazines etc. Following are the major findings of the study:

- There is no liquidity in the stock market for shares except that of banking and some finance and insurance sectors.
- Lack of coordination between the performance of stock market and the Nepalese economy the performance of manufacturing sector in NEPSE is quite dismal.
- NEPSE is only institution that helps to regulate and control the financial system of the country. The government should launch the program that overcomes the problem faced by Nepalese stock market and take in the long-term growth for economic development.

- Investor's confidence in Nepalese stock market is low because of stock market volatility, low return in investment, inadequate information, lack of financial markets etc.
- The stock market has good prospects for the resource mobilization to finance the productive enterprises in Nepalese economy.
- The size of the market in terms of market capitalization and number of issue is relatively small.

**Pandey (2008)** has conducted a research on the topic of "*Public response to Primary Issue of Shares in Nepal.*" The objectives of the study are:

- To identify the problems of primary share issue market
- To assess the growth of primary issue market
- To analyze the pattern of public response to shares.

Major findings of the study are:

- 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 is that the 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.

**Ojha (2009)** has conducted a study on “*Public response to IPO in Nepal*” focuses on IPO, response to IPO, problems and growth of primary market in Nepal, role of investment bankers, and the pace for IPO. Following are the major findings of the study are:

- Most of the investor in Nepal does not know about IPO.
- They do not want to take risk at all.
- Loans for financial institution for IPO funding is breaking the healthy practice as single man applies from different names and captures large number of shares which ultimately influence company management and stock price too.
- High investors are interested in financial sector than non-financial sector.

**Bhandari (2010)** has conducted a research on “*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 intermediation service in Nepalese Securities Market. Major finding of his study are as follows:

- 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.
- 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.

- 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.
- 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.
- Nepalese Security market is small in quantity and poor in quality as compared to other develop stock market.

**Wagley (2011)** has conducted a study on "A study on impact of SEBON guidelines on IPO" mainly based on secondary data. The main objective of the study is to find out the relationship between SEBON and IPO making institutions. The specific objectives of the study will be pointed out as follows:

- To examine the existing rules, regulations and guidelines related to primary market.
- To examine the effectiveness of these rules, regulations and guidelines.
- To examine the roles duties and responsibilities of the issue manager.
- To study the number of issued approved.
- To study the primary share issue of Nepal.

Major Findings of the study are:

- The study found that most of investors like to invest in banking sector. Investors were found to believe that the share price of banking sector always rises and can earn dividend more compare to others.

- Most of the people prefer pro-rata basis for allotment not the lucky-draw as pro-rata basis assure the investor about getting the share.
- Still most of the people lack information regarding stock so limited numbers of people are investing in primary market..
- The study found that the Nepalese investors preferred IPO as quick way to make money rather than long term investment.
- Nepalese investors are risk averter so of the do not like to invest from credit/loan.
- The study finds capital gain and right share are the most impressive factor to investor for investment. Some investors preferred liquidity and social status as the objectives of the stock investment.

#### **2.4 Research Gap**

Even though numerous studies have been carried out in different part of the world covering different aspects of securities market, stocks trading mechanism and stock pricing behaviors etc. including public response in primary issue of different securities. As Nepalese commercial banking sector occupies the largest share in capital or securities market transaction wise this study intends to be specific about listed commercial banks IPO. In Nepalese context, very few studies regarding IPO have been made. However none of the studies been able to reflect the complete picture of IPO's of listed commercial banks, their performance public response and the prospectus in Nepal. This study also tries to understand the pace of initial public offering, investor response, procedures, rules, regulations and provisions as well as public awareness about it. So this study will be fruitful to those interested person, scholars, students, teachers, civil society, businessmen and government for academically as well as policy perspectives.

## **CHAPTER- III**

### **RESEARCH METHODOLOGY**

Research methodology describes the methods and process applied in the entire the study .In other words research methodology is a systematize way to solve the research problem. Research methodology refers to the various sequential steps (along with a rational, 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 are used. This chapter highlights the research methodology are used for the study.

#### **3.1 Research Design**

Research design is the plan, structure and strategy of investigation conceived so as to obtain answer to research question and to control variance. The research design refers to the entire process of planning and carrying out a research study. It describes the general framework for collecting, analyzing and evaluating data after identifying: (i) what the researcher wants to know, and (ii) what has to be dealt with in order to obtain required information. So, to make any type of research a well-set research design is necessary to fulfill the objectives of the study.

Current research applies both descriptive and analytical techniques to determine the determinants of stock price. It is analytical in the sense that it uses different analytical tools to analyze the investor's preferences toward factor affecting stock price. Similarly it is descriptive in the sense that it clarifies different aspects of investor's preferences. As per the nature of the research primary as well as secondary data have been extensively used.

### 3.2 Population and Sample

Number of companies listed in Nepal Stock Exchange (NEPSE) by the end of F/Y 2010/11 has reached 207 which include commercial banks, development banks, finance companies, insurance companies, manufacturing and processing companies, trading companies, hotels and others. So, population for this study is the total number of listed companies and sample for this study is given in the following table:

**Population and Sample of the Study**

| Sector                      | Population of study | Sample of study | Percentage |
|-----------------------------|---------------------|-----------------|------------|
| <b>Financial Sector</b>     |                     |                 |            |
| Commercial Bank             | 23                  | 7               | 30.43%     |
| Development bank            | 61                  | 10              | 316.39%    |
| Finance companies           | 70                  | 12              | 17.14%     |
| Insurance                   | 21                  | 6               | 28.57%     |
| Total                       | 175                 | 35              |            |
| <b>Non-financial Sector</b> |                     |                 |            |
| Mfg. & Pro. Co.             | 18                  | 4               | 22.22%     |
| Trading co.                 | 4                   | 2               | 50.00%     |
| Hotel                       | 4                   | 2               | 50.00%     |
| Others                      | 6                   | 2               | 33.33%     |
| Total                       | 32                  | 10              |            |

*Source: nepalstock.com*

For the primary data collection students, brokers, investors, bankers, officials of the companies and experts are taken. Response to questionnaire is received from total of 20 persons and compositions of the respondents are as below:

| Profession | Number of respondents | Percentage |
|------------|-----------------------|------------|
| Students   | 4                     | 20.00%     |
| Investors  | 8                     | 40.00%     |
| Bankers    | 3                     | 16.67%     |
| Brokers    | 1                     | 3.33%      |
| Others     | 4                     | 20.00%     |
| Total      | 20                    | 100.00%    |

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

#### **A. Primary Data**

Primary data gives real shape to the work. Discussion and interviews with existing investors, staff members of NEPSE and SEBON, brokers and other concerned parties have been conducted to collect the primary data. As per the requirement of the research a questionnaire was designed for the primary data collection. And then those eleven questions are asked to 25 persons among them 20 respondents (students, businessman, bankers, brokers and others) answered, so the response rate is 80%.

#### **B. Secondary Data**

To accomplish the above mentioned objectives, this research is based upon the secondary data for the historical performance assessment and the primary data for the qualitative assessment of information. As input for the study, the secondary data that re collected through various published and unpublished documentary type sources. The sources are relied secondary data are as:

- Annual Report – NEPSE, SEBON
- Nepal Merchant Bank & Finance company Ltd.
- NIDC Capital Market
- Citizen Investment Trust
- Quarterly Economic Bulletins, NRB
- Websites
- News papers

Previous Research studies; Dissertation and Articles on the subject

### **3.4 Data Collection Techniques**

Annual report covering different fiscal years of SEBON are collected from its head office at Gaushala. Similarly, trading reports of NEPSE are retrieved from its head office at Singhadarbar. Daily newspapers like The Kathmandu Post, Republica and Rising Nepal are access from library and weekly newspaper

Arthik Abhiyan and business plus are bought myself. Acts and regulatory information are obtained from law as well as official website of SEBON.

### **3.5 Data Processing**

At first data are extracted from above mentioned sources and recorded in the master sheet. The data are often then entered into the spreadsheet to present them into appropriate tables and figures with aid of computer programmers like Microsoft word, Microsoft excel is 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:

#### **3.6.1 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,  $(1+g)^n = (1+g)^1 (1+g)^2 (1+g)^3 \dots\dots\dots (1+g)^n$

Where,

n=Number of years

g=Compound growth rate

Compound growth is calculated 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 Trend Analysis

It is important to analyze trends in ratio as well as their absolute levels, for the trends give clue to whether the financial situation is improving or whether it is deteriorating. In other word trend analysis of ratios indicates the direction of changes. The significance of a trend analysis of ratio lies in the fact that the analyst can know the direction of movement, i.e. whether the movement is favorable or not. Thus, the tools that are used to show grandly increase or decrease of variables over a period of time is known as trend analysis. With the help of trend analysis of the tendency of variables over the period can be seen clearly.

### **3.8 Limitation of the Research Methodology**

A lot of difficulties as well as improper knowledge in this particular subject make it complicated to achieve the objective. Out of 209 listed companies 2 companies i.e. Himchuli Bikash Bank and Birgunj Finance merged and Nepal Bikash Bank Ltd. was disclosed so this study is done with the base of 207 listed companies. Out of 207 listed companies only 45 companies are taken as sample. Due to limitation of time all the methods are shortly described. Primary data is based on the answer of the respondent. So, it is subjected to be different according to loyalty of the respondents. Although various tools can be used to achieve the objectives of the study but only the multiple bar- diagrams and graphs, pie- diagram, percentage, model for measuring growth rates, trend analysis are used. (*Source: SEBON Annual Report 2010/11*)

## **CHAPTER IV**

### **DATA PRESENTATION AND ANALYSIS**

This chapter includes presentation of data and analysis of data to 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 sector wise along with under subscription and oversubscription, growth of public offering and the behavior of general investors.

To meet the objectives of study about the responses of investors, the study is made with questionnaire survey. The study is based on the investors who are willing to invest in IPO and are already involved in financial market. The theme of the study is-what types of company do investors prefer most? The banking and financial sectors take over the very high place but other sectors are not-why? What react can be over come from the investors, if the companies issued the IPO?

In this course of analysis, the collected data have been presented in the tables, figures and diagrams and then analyzed by using financial and statistical tools. The results of the computation have also been summarized in appropriated tables. The samples of computation of each model have been included in annexes.

#### **4.1 Analysis of Secondary Data**

##### **4.1.1 Number of Issue Approved**

The number of issue approved is the total number of issue approved by the Security Board of Nepal. Before issuing securities, the issuing company must make approval from Security Board of Nepal (SEBON). For issue approval and registration, the company must submit requited information within prescribed

format otherwise SEBON may reject it. After registration and issue approval, the company must open issue within three month of issue approval. In case if the issue couldn't be made, then after another date should be fixed consulting with SEBON. The advertisement for application should be published in national daily news paper, the advertisement should consist all actual and real information. The advertisement should be able to identify application collection centre and its duration.

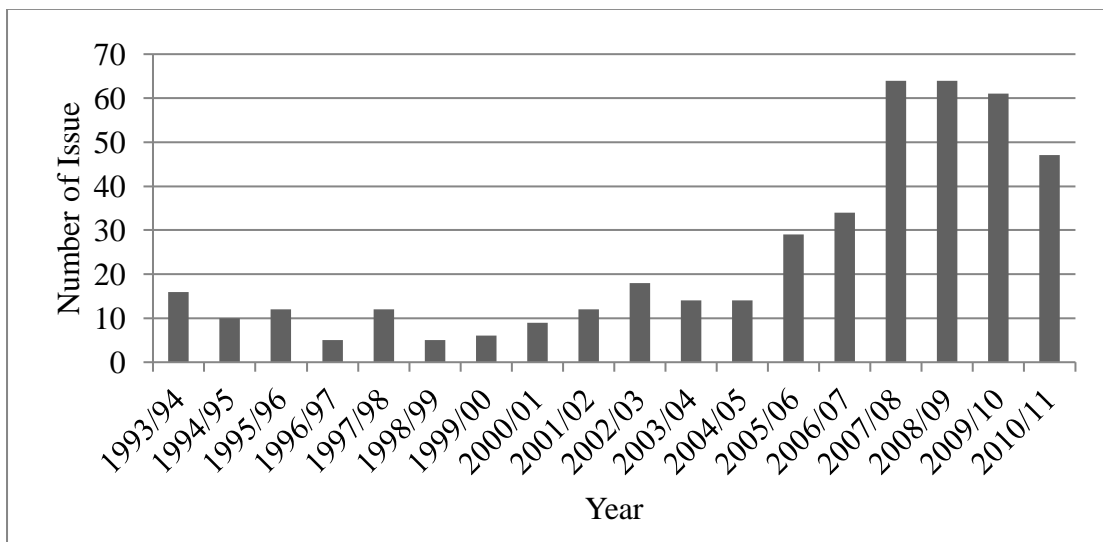
**Table 4.1**  
**Number of Issue Approved**

| Year    | Number of Issue Approved | % of Issue Approved |
|---------|--------------------------|---------------------|
| 1993/94 | 16                       | 3.70                |
| 1994/95 | 10                       | 2.32                |
| 1995/96 | 12                       | 2.78                |
| 1996/97 | 5                        | 1.16                |
| 1997/98 | 12                       | 2.78                |
| 1998/99 | 5                        | 1.16                |
| 1999/00 | 6                        | 1.39                |
| 2000/01 | 9                        | 2.08                |
| 2001/02 | 12                       | 2.78                |
| 2002/03 | 18                       | 4.17                |
| 2003/04 | 14                       | 3.24                |
| 2004/05 | 14                       | 3.24                |
| 2005/06 | 29                       | 6.71                |
| 2006/07 | 34                       | 7.87                |
| 2007/08 | 64                       | 14.81               |
| 2008/09 | 64                       | 14.81               |
| 2009/10 | 61                       | 14.12               |
| 2010/11 | 47                       | 10.88               |
| Total   | 432                      | 100.00              |

*Source: SEBON Annual Report*

Table 4.1 shows that the number of issue approved from 1993/94 to 2010/11. SEBON has approved 432 issues in which highest number of issue approved is in the fiscal year 2007/08 and in the year 2008/09 and the lowest issue approved is in the year 1996/97 and 1998/99. Simultaneously 16 issues are approved in 1993/94, 10 issues in 1994/95, 12 issues in 1995/96 and in 1997/98, 6 issues in 1999/00, 9 issues in 2000/01, 12 issues in 2001/02, 18 issues in 2002/03, 14 issues in 2003/04 and in 2004/05, 29 issues in 2005/06, 34 issues in 2006/07, 64 issues in 2007/08 and in 2008/09, 61 issues in 2009/10 and 47 issues in 2010/11.

**Figure 4.1**  
**Number of Issue Approved**



The figure 4.1 illustrates the number of issue approved from 1993/94 to 2010/11. In the year 2007/08 and 2008/09 highest number of issue approved is 64 and the lowest number of issue approved is only 5 in the year 1996/97 and 1998/99. The trend of number of issue approved is in fluctuating stage up to fiscal year 2004/05 and start to increase heavily up to fiscal year 2007/08 and constant in year 2008/09 and starts to decrease heavily.

#### **4.1.2 Amount of Issue Approved**

Securities Exchange Act, 1983 has made mandatory that the issuing company should register the securities in SEBON and get approval before going to

public. From the fiscal year 1993/94 to 2010/11 SEBON has approved 432 issues of securities amounting to Rs. 56959.48 million. The details are as follows:

**Table 4.2**  
**Amount of Issue Approved**

(Rs. in millions)

| Year    | Amount of Issue Approved | % of Issue Approved | Growth % |
|---------|--------------------------|---------------------|----------|
| 1993/94 | 244.40                   | 0.43                |          |
| 1994/95 | 173.96                   | 0.031               | -28.82   |
| 1995/96 | 293.74                   | 0.52                | 68.85    |
| 1996/97 | 332.20                   | 0.58                | 13.12    |
| 1997/98 | 462.36                   | 0.81                | 39.14    |
| 1998/99 | 258.00                   | 0.45                | -44.20   |
| 1999/00 | 326.86                   | 0.57                | 26.69    |
| 2000/01 | 410.49                   | 0.72                | 25.59    |
| 2001/02 | 1441.33                  | 2.53                | 251.12   |
| 2002/03 | 556.54                   | 0.98                | -61.39   |
| 2003/04 | 1027.50                  | 1.80                | 84.62    |
| 2004/05 | 1626.82                  | 2.85                | 58.33    |
| 2005/06 | 2443.28                  | 4.29                | 50.19    |
| 2006/07 | 2295.5                   | 4.03                | -6.05    |
| 2007/08 | 10668.20                 | 18.72               | 364.74   |
| 2008/09 | 16828.51                 | 29.53               | 57.74    |
| 2009/10 | 10822.41                 | 18.99               | -35.69   |
| 2010/11 | 6777.29                  | 11.90               | -37.38   |
| Total   | 56989.48                 | 100.00              |          |

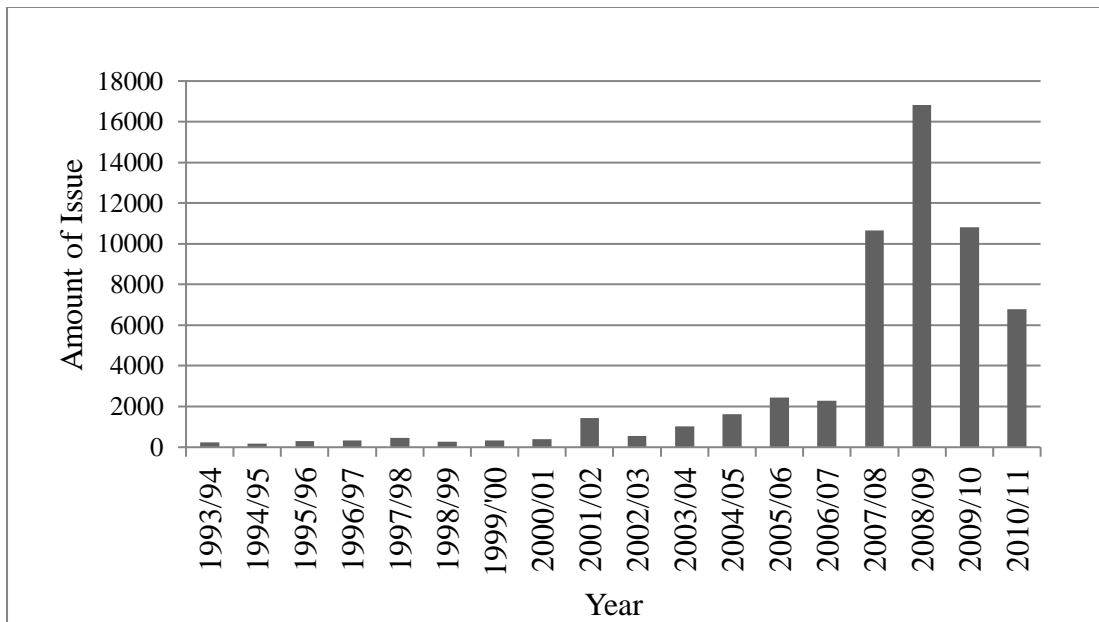
*Source: SEBON Annual Report*

Table 4.2 shows the variation of issue amount approved during 1993/94 to 2008/09 period. The highest amount approved is Rs. 16828.51 million

(42.72%) in the fiscal year 2008/09 and the lowest amount approved is Rs.173.96 million (0.44%) in the fiscal year 1994/95. In fiscal year 2009/10 total amount issued is Rs. 10,822.41 million. Third and fourth highest public issue is Rs.10,668.20 and Rs. 6777.29 million in fiscal year 2007/08 and 2010/11. During the starting period Nepalese capital market is not so popular among investors. Only few investors of Kathmandu valley are trading. But, after 2002/03 more and more people start to enter in market so that capital market starts to increase up to fiscal year 2007/08 and again starts to decrease.

The highest growth in the issue of securities was witnessed in the year 2007/08 and in that year growth of issue in share was 364.74% of the earlier year's issue which indicates that massive growth in issue of securities started in the year 2007/08 after growth of about 251.12% in the year 2001/02.

**Figure 4.2**  
**Amount of Issue Approved**



The figure 4.2 illustrates the trend of amount of issue approval of IPO from 1993/94 to 2010/11. The pick point is in the year 2007/08 which shows that the highest amount of issued approved and the lowest point is in the year 1994/95.

### 4.1.3 Over and Under Subscription of Securities

The demand for securities may be greater or lesser than the issuing amount. When the demand is greater that is over subscription and when lesser that is under subscription. At the time of issue the demand for securities may be greater or lesser than the issuing amount.

**Table 4.3**  
**Over And Under Subscription of Securities**

| Year    | No. of Issue | Over Subscribed |       | Under Subscribed |       | Constant |       |
|---------|--------------|-----------------|-------|------------------|-------|----------|-------|
|         |              | No.             | %     | No.              | %     | No.      | %     |
| 1993/94 | 16           | 16              | 100   | 0                | 0     | 0        | 0     |
| 1994/95 | 10           | 7               | 70    | 1                | 10    | 2        | 20    |
| 1995/96 | 12           | 6               | 50    | 6                | 50    | 0        | 0     |
| 1996/97 | 5            | 2               | 40    | 0                | 0     | 3        | 60    |
| 1997/98 | 12           | 5               | 41.67 | 5                | 41.67 | 2        | 16.67 |
| 1998/99 | 5            | 3               | 60    | 1                | 20    | 1        | 20    |
| 1999/00 | 6            | 4               | 66.67 | 1                | 16.67 | 1        | 16.67 |
| 2000/01 | 9            | 8               | 88.89 | 1                | 11.11 | 0        | 0     |
| 2001/02 | 12           | 5               | 41.67 | 4                | 33.33 | 3        | 25    |
| 2002/03 | 18           | 14              | 77.78 | 3                | 16.67 | 1        | 5.55  |
| 2003/04 | 14           | 12              | 85.71 | 2                | 14.29 | 0        | 0     |
| 2004/05 | 14           | 6               | 42.86 | 7                | 50    | 1        | 7.14  |
| 2005/06 | 29           | 17              | 58.62 | 10               | 34.48 | 2        | 6.90  |
| 2006/07 | 34           | 16              | 47.05 | 14               | 41.17 | 4        | 8.82  |
| 2007/08 | 64           | 19              | 29.68 | 32               | 50.00 | 13       | 20.32 |
| 2008/09 | 64           | 12              | 18.75 | 0                | 0     | 52       | 81.25 |
| 2009/10 | 61           | 28              | 45.90 | 0                | 0     | 33       | 54.10 |
| 2010/11 | 47           | 33              | 70.21 | 2                | 0     | 12       | 29.79 |
| Total   | 432          | 213             | 49.31 | 89               | 20.60 | 130      | 30.09 |

*Source: SEBON Annual Report*

**Table 4.4**  
**Over And Under Subscription of Ordinary Shares**

| Year    | No. of Issue | Over Subscribed |        | Under Subscribed |       | Constant |       |
|---------|--------------|-----------------|--------|------------------|-------|----------|-------|
|         |              | No.             | %      | No.              | %     | No.      | %     |
| 1993/94 | 14           | 14              | 100.00 | 0                | 0.00  | 0        | 0.00  |
| 1994/95 | 10           | 7               | 70.00  | 1                | 10.00 | 2        | 20.00 |
| 1995/96 | 10           | 6               | 60.00  | 4                | 40.00 | 0        | 0.00  |
| 1996/97 | 2            | 2               | 100.00 | 0                | 0.00  | 0        | 0.00  |
| 1997/98 | 8            | 5               | 62.50  | 2                | 25.00 | 1        | 12.50 |
| 1998/99 | 3            | 2               | 66.66  | 1                | 33.33 | 0        | 0.00  |
| 1999/00 | 3            | 3               | 100.00 | 0                | 0.00  | 0        | 0.00  |
| 2000/01 | 5            | 5               | 100.00 | 0                | 0.00  | 0        | 0.00  |
| 2001/02 | 5            | 4               | 80.00  | 1                | 20.00 | 0        | 0.00  |
| 2002/03 | 14           | 14              | 100.00 | 0                | 0.00  | 0        | 0.00  |
| 2003/04 | 10           | 10              | 100.00 | 0                | 0.00  | 0        | 0.00  |
| 2004/05 | 7            | 6               | 85.72  | 1                | 14.28 | 0        | 0.00  |
| 2005/06 | 12           | 12              | 100.00 | 0                | 0.00  | 0        | 0.00  |
| 2006/07 | 15           | 15              | 100.00 | 0                | 0.00  | 0        | 0.00  |
| 2007/08 | 16           | 14              | 87.50  | 0                | 0.00  | 2        | 12.50 |
| 2008/09 | 12           | 12              | 100.00 | 0                | 0.00  | 0        | 0.00  |
| 2009/10 | 28           | 28              | 100    | 0                | 0     | 0        | 0     |
| 2010/11 | 33           | 33              | 100    | 0                | 0     | 0        | 0     |
| Total   | 207          | 192             | 92.75  | 10               | 4.83  | 5        | 2.42  |

*Source: SEBON Annual Report*

When the demand of securities is higher than issued securities, the situation is called the case of oversubscription but if the demand of securities is lower than issued securities that situation is called under subscription of securities. Above table 4.3 shows the oversubscription & under subscription of different companies from year 1993/94 to 2010/11, while issuing their ordinary share to

general public. The table 4.3 gives the information about over and under subscription of securities from 1993/94 to 2010/11 where most of the issues are oversubscribed i.e. 213 which is 49.30% among the total issues and only 89 issues i.e. 20.60% are under subscribed and 130 issues i.e. 30.09% are constant. In the year 1993/94 all issues are oversubscribed.

Table 4.4 shows that during the period of fiscal year 1993/94 to 2010/11 total 207 companies issued common stock for public subscription and among them common stock issue of 192 companies (92.75%) have been oversubscribed, issue of 10 companies (4.83%) have been undersubscribed and remaining 5 companies (2.42%) issue have been fully subscribed. Furthermore, all those companies who issued their common stock in fiscal year 1993/94, 1996/97, 1999/00, 2000/01, 2002/03, 2003/04, 2005/06, 2006/07, 2008/09, 2009/10 and 2010/11 have been fully oversubscribed.

Similarly, during the period highest number of issue is made in the year 2010/11 with 33 companies issuing their shares for public subscription followed by 28 companies in 2009/10, 16 companies in 2007/08, 15 companies in 2006/07 and 12 companies in the year 2005/06 and 2002/03. While lowest number of issue is made in the year 1996/97 with only 2 companies issuing their common stock for public and it is followed by 3 companies in year 1998/99 and 1999/00 respectively.

#### **4.1.4 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, 207 companies have already been listed till the end of 2010/11. The total paid up capital of these companies amounted to Rs. 100238.85 million. The most instigating aspect of this total paid up capital is the contribution from financial sector that includes commercial bank, shown in table 4.5:

**Table 0.5**  
**Publicly Issued Companies**

| S.N | Sector                       | No. of Companies | Percent | Paid up value (Rs. in millions) | Percent |
|-----|------------------------------|------------------|---------|---------------------------------|---------|
| 1   | Commercial Banks             | 23               | 11.00   | 41806.19                        | 41.71   |
| 2   | Development Banks            | 61               | 29.67   | 16864.69                        | 16.82   |
| 3   | Finance Companies            | 70               | 33.97   | 15301.08                        | 15.26   |
| 4   | Insurance Companies          | 21               | 10.05   | 3585.29                         | 3.58    |
| 5   | Manufacturing and Processing | 18               | 8.61    | 2539.74                         | 2.53    |
| 6   | Trading                      | 4                | 1.91    | 83.42                           | 0.08    |
| 7   | Hotels                       | 4                | 1.91    | 1615.15                         | 1.61    |
| 8   | Others                       | 6                | 2.87    | 18443.29                        | 18.40   |
|     | Total                        | 207              | 100     | 100238.85                       | 100     |

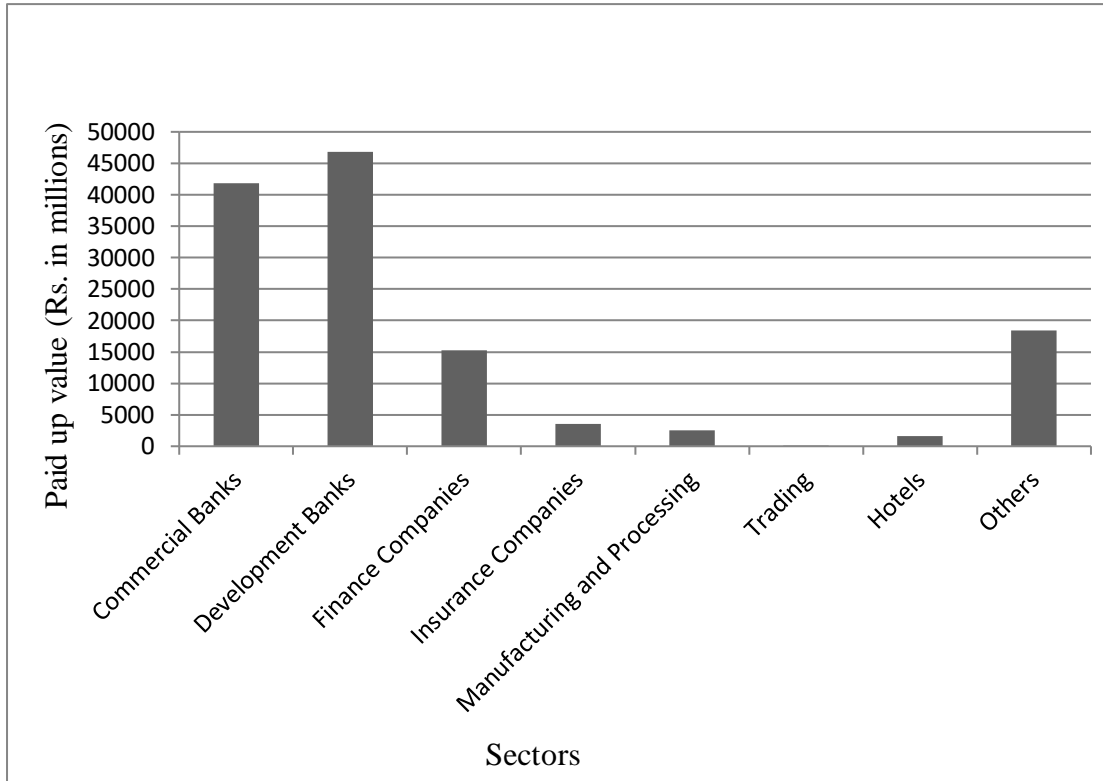
*Source: SEBON Annual Report*

As shown in table 4.5 out of 207 listed companies 175 companies belong to financial sector (i.e. commercial banks, development banks, finance companies and insurance companies), which is about 84.54% of the total listed companies in NEPSE. Similarly, from paid-up value perspective commercial banks occupies 41.71%, development banks have 16.82%, finance companies accounts for 15.26% and insurance companies have 3.58% of the total paid-up value. Together as financial sector, they account for 78.98% of the total paid-up value.

Whereas, 32 companies belong to non financial sector (i.e. manufacturing and processing, trading, hotels and others), which is about 15.46% of the total listed companies. Manufacturing and processing sector accounts for only 2.53%.

Similarly, trading, hotel and others account for 0.08%, 1.61% and 18.40% of the total paid-up value respectively.

**Figure 4.3**  
**Paid up value**



#### **4.1.5 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 2010/11 is Rs. 6665.18 million. It is Rs. 11851.11 million in FY 2009/10.

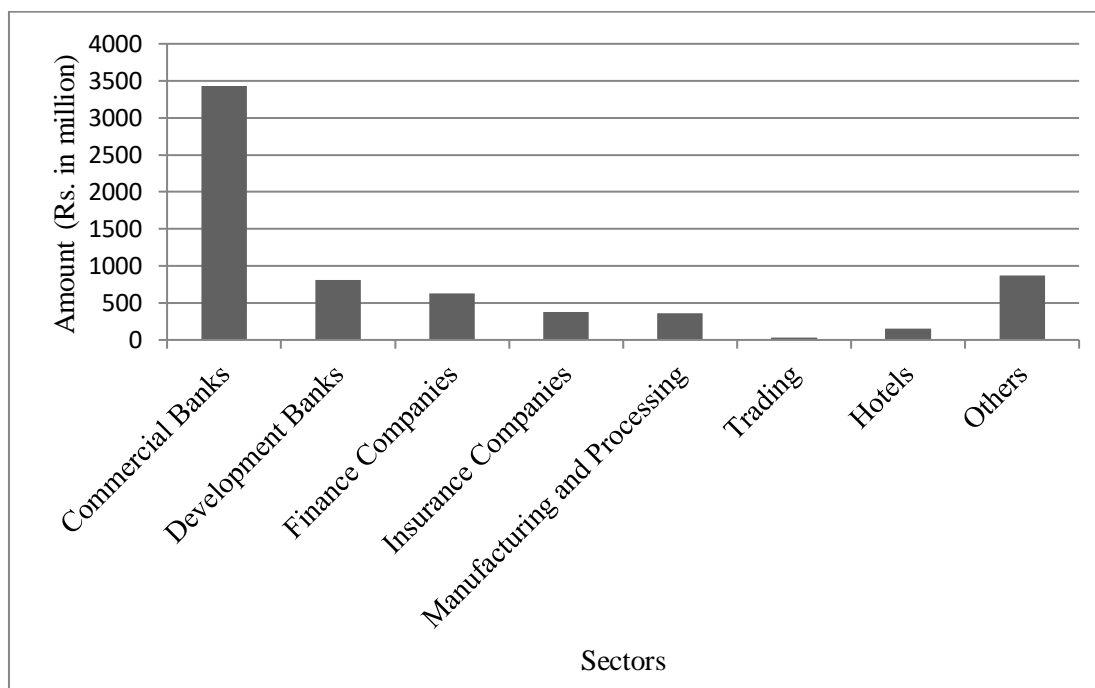
**Table 4.6**  
**Sector-Wise Annual Turnover**

| SN | Sector                       | Amount<br>(Rs. in millions) | Percent<br>(%) |
|----|------------------------------|-----------------------------|----------------|
| 1  | Commercial Bank              | 3431.82                     | 51.49          |
| 2  | Development Bank             | 813.24                      | 12.20          |
| 3  | Finance Companies            | 630.74                      | 9.46           |
| 4  | Insurance Companies          | 377.15                      | 5.66           |
| 5  | Manufacturing and Processing | 363.06                      | 5.48           |
| 6  | Trading                      | 27.53                       | 0.41           |
| 7  | Hotels                       | 151.92                      | 2.28           |
| 8  | Others                       | 869.76                      | 13.05          |
|    | Total                        | 6665.18                     | 100            |

*Source: SEBON Annual Report*

As shown in table 4.6, among 8 sectors, the contribution from financial sector is about 78.80% that includes commercial banks, development banks, finance companies and insurance companies. On the other hand, contribution from non-financial sector is about 21.20% which includes manufacturing and processing, trading, hotels and other companies. Among 8 sectors, commercial banks have highest i.e. 51.49% contribution and trading have lowest i.e. 0.41% contribution. The figure 4.6 demonstrates that trading amount of financial sector companies is much higher than that of non-financial sectors. And also shows that commercial banks contribute highest and trade contribute lowest among all these sectors.

**Figure 4.4**  
**Sector-wise Annual Turnover**



#### **4.1.6 Analysis of Market Capitalization**

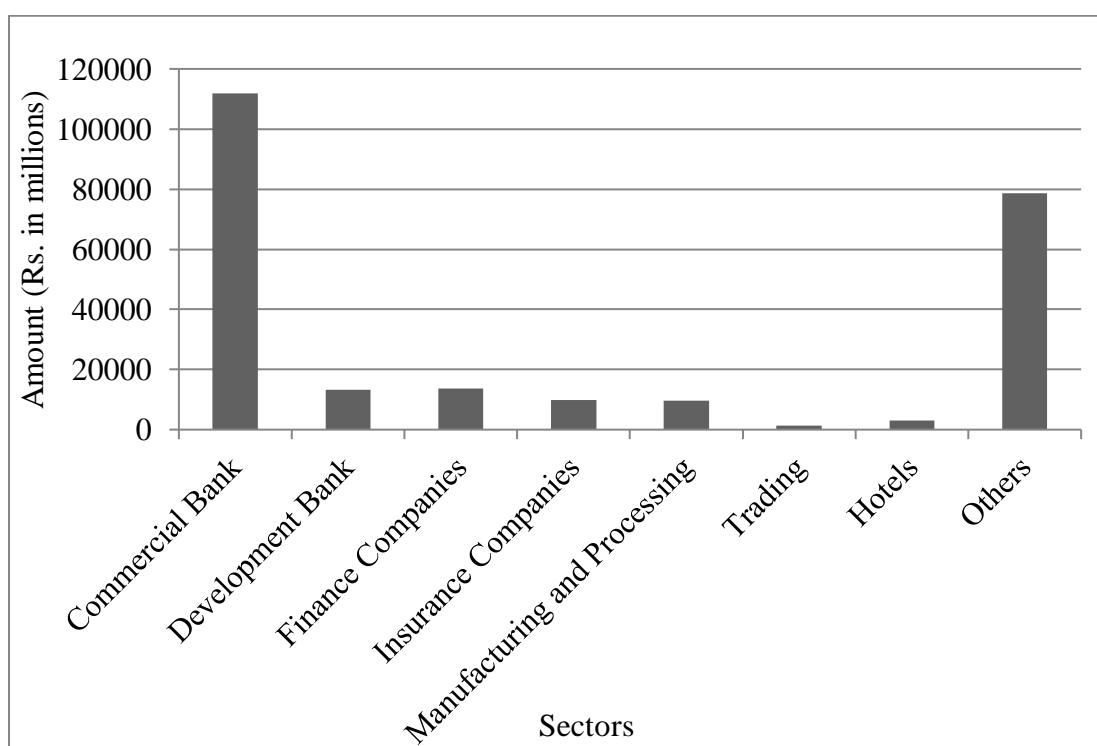
By the end of the FY 2010/11, the percentage contribution of market capitalization on nominal GDP is estimated to be Rs. 24.02%. The market capitalization in the FY 2010/11 is Rs. 241513.95 million and is presented below in table 4.7. By analyzing the sector wise market capitalization, banking sector is highest among all sectors. Commercial banks capture 46.35%, development banks 5.47%, finance companies 5.70% and insurance company 4.12%. Similarly, manufacturing and processing 3.90%, trading 0.57%, hotels 1.26% and others companies captures 32.57%.

**Table 4.7**  
**Sectors-wise Market Capitalization**

| SN | Sector                          | Amount<br>(Rs. in millions) | Percent |
|----|---------------------------------|-----------------------------|---------|
| 1  | Commercial Bank                 | 111938.05                   | 46.35   |
| 2  | Development Bank                | 13210.54                    | 5.47    |
| 3  | Finance Companies               | 13756.06                    | 5.70    |
| 4  | Insurance Companies             | 9937.18                     | 4.12    |
| 5  | Manufacturing and<br>Processing | 9577.84                     | 3.97    |
| 6  | Trading                         | 1380.74                     | 0.57    |
| 7  | Hotels                          | 3040.64                     | 1.26    |
| 8  | Others                          | 78672.90                    | 32.57   |
|    | Total                           | 241513.95                   | 100     |

*Source: SEBON Annual Report*

**Figure 4.5**  
**Sectors-wise Market Capitalization**



The figure 4.5 proves that most of the market capitalization is on the financial sector, mainly on the commercial banks and rest remains with non-financial sector, mainly on others.

#### **4.1.7 Investor Response to IPO**

##### **4.1.7.1 Financial Sector**

Financial Sector includes commercial bank, development banks, finance companies & insurance companies.

##### **4.1.7.1.1 Investor Response to Commercial Banks**

There are 32 commercial banks among which only 23 are listed in the stock exchange. Nepal Arab Bank Limited (NABIL Bank) is the first commercial bank to issue Share to public. Public issues of commercial bank are highly appreciated by public. Investors give high priority and response to the public issue. From the population of all total of 23 only 7 are taken as sample.

**Table 4.8**

**Investor Response to Commercial Banks**

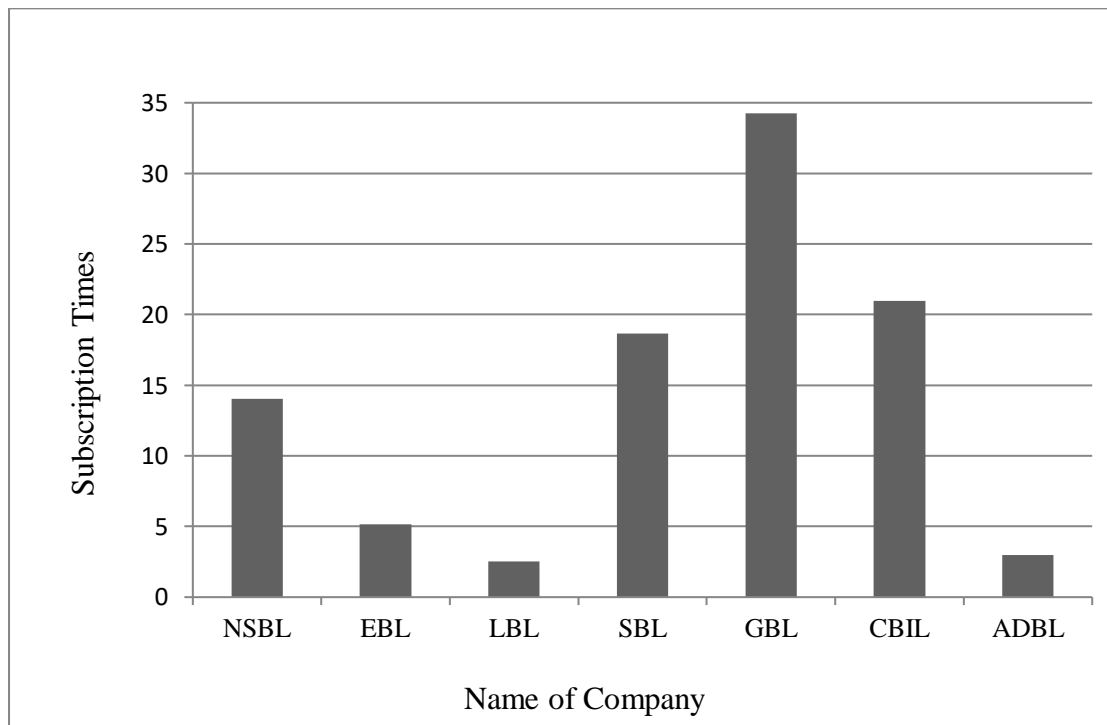
| S. No. | Name of Company | Share Issued | Applied   | Year | Subscription times | Result     |
|--------|-----------------|--------------|-----------|------|--------------------|------------|
| 1.     | NSBL            | 360000       | 5056921   | 1994 | 14.04              | Over Subs. |
| 2.     | EBL             | 360000       | 18515663  | 1995 | 5.14               | Over Subs. |
| 3.     | LBL             | 1925000      | 4838488   | 2003 | 2.51               | Over Subs. |
| 4.     | SBL             | 1500000      | 27979950  | 2005 | 18.65              | Over Subs. |
| 5.     | GBL             | 3000000      | 102899626 | 2008 | 34.25              | Over Subs. |
| 6.     | CBIL            | 3000000      | 62990520  | 2009 | 20.98              | Over Subs. |
| 7.     | ADBL            | 9600000      | 28510303  | 2010 | 2.97               | Over Subs. |

*Source: SEBON, Annual Report*

The table 4.8 gives the information about issued shares and applied shares of commercial bank, where we have found applied number of shares is higher

than the issued one, i.e. all the issues are oversubscribed. Subscription times of listed sample banks ranges from 2.51 to 34.25. For the 3000000 shares issued by Global Bank Ltd. 102899626 shares have been applied that means it was oversubscribed 34.25 times. Similarly 20.98 times subscription in the case of Citizen Bank International Ltd., 18.65 times in Siddhartha Bank Ltd., 14.04 times in Nepal SBI Bank Ltd., 5.14 times in Everest Bank Ltd., 2.51 times in Laxmi Bank Ltd. and 2.97 times in Agriculture Development Bank Ltd. So, it is clear that commercial banks share issues are getting overwhelming response from Investor. Investor found to be interested in shares of commercial banks. It also can be said that in the mid period of sampling the subscription rate is going to increase highly and declines in the latest sampling period due to decrease in NEPSE index.

**Figure 4.6**  
**Investor response to Commercial Banks**



The figure 4.6 shows that highest subscription is in the case of GBL with highest bar while the lowest bar shows that LBL is least subscribed.

#### 4.1.7.1.2 Investor Response to Development Bank

There are 61 development banks listed in the stock exchange. From the population of 61 only 10 are taken as sample. The table 4.9 shows that Gorkha Development bank limited has highest subscription (i.e.108.32 times) than others sample development banks but all the issues are oversubscribed. Whereas Malika Bikash bank has 54.84, Clean Energy development bank ltd. has 36.46, Pashupati Bikash bank has 22.07, Vibor bikash bank has 7.18, Manakamana Development bank has 5.42, Sewa Bikash bank has 27.68, Diyalo Bikash bank has 12.31, Arniko Development bank has 5.10 and Rara Bikash bank has 3.75 subscription times.

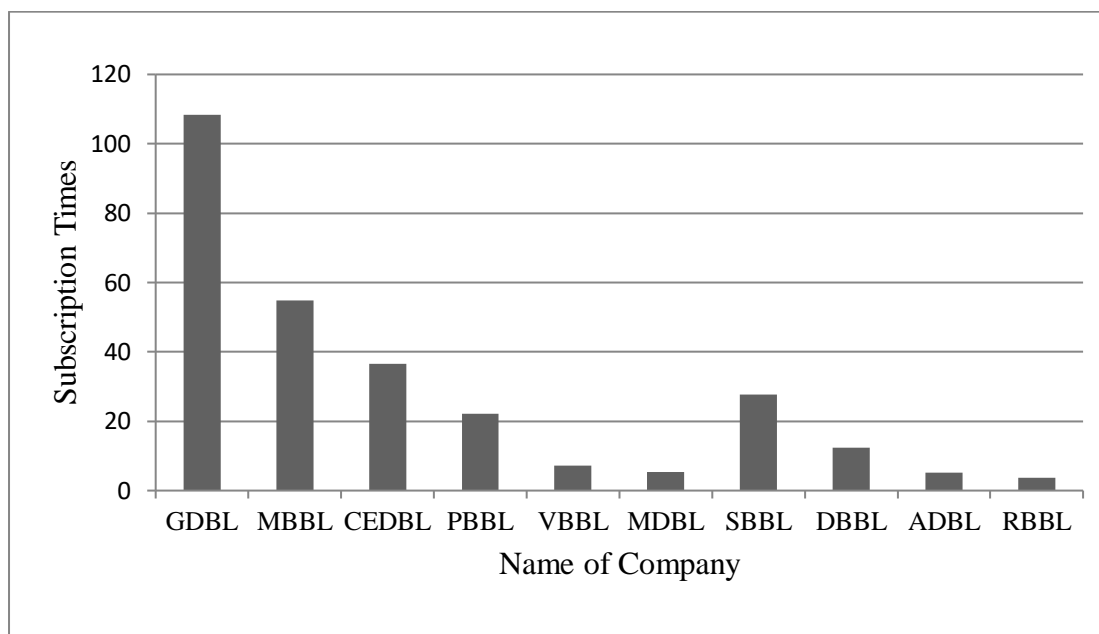
**Table 4.9**  
**Investor Response to Development Bank**

| S.No. | Name of Bank | Shares Issued | Shares Applied | Issued Year | Subscripti on times | Result    |
|-------|--------------|---------------|----------------|-------------|---------------------|-----------|
| 1.    | GDBL         | 960000        | 103987200      | 2006        | 108.32              | Oversubs. |
| 2.    | MBBL         | 150000        | 8226900        | 2007        | 54.84               | Oversubs. |
| 3.    | CEDBL        | 960000        | 35003040       | 2008        | 36.46               | Oversubs. |
| 4.    | PBBL         | 800000        | 17657840       | 2009        | 22.07               | Oversubs. |
| 5.    | VBBL         | 2652000       | 19042951       | 2009        | 7.18                | Oversubs. |
| 6.    | MDBL         | 3000000       | 16260000       | 2010        | 5.42                | Oversubs. |
| 7.    | SBBL         | 400000        | 11072000       | 2010        | 27.68               | Oversubs. |
| 8.    | DBBL         | 350000        | 4308500        | 2010        | 12.31               | Oversubs. |
| 9.    | ADBL         | 980000        | 4998000        | 2011        | 5.10                | Oversubs. |
| 10.   | RBBL         | 660300        | 2476125        | 2011        | 3.75                | Oversubs. |

*Source NCML, NMB, NFC, NEFINSCO, SEBON*

**Figure 4.7**

**Investor Response to Development Bank**



The figure 4.7 shows that among sample development banks highest subscription is in the case of Gorkha Development Bank limited with highest bar and lowest in the case of Rara Bikash Bank limited with lowest bar. The NEPSE is going on increase up to fiscal 2009, so the banks which issues on this period have highest subscription rate.

**4.1.7.1.3 Investor Response to Finance Companies**

There are altogether 70 listed finance companies from which 12 are taken for research investor response.

The table 4.10 shows that in all the investor response to finance companies we found over Subscription all the time. That means investor is also interested in finance companies shares. Highest over Subscription of 77.30 times is in the case of Prabhu Finance Ltd (PFL), Where 37107840 shares are applied for only 480000 shares. There is 31.06 times in Crystal Finance Ltd (CFL), 26.24 times in Api Finance Ltd (AFL), 21.93 times in Kaski Finance Ltd (KFL), 4.58 times subscription in IME Financial Institution Ltd (IMI-FIL), 13.04 times

subscription in Suryadarshan Finance Company Ltd. (SFCL), 10.42 times in Unique Financial Institution Ltd. (UFIL), 9.93 times in Swastik Merchant Finance Company Ltd. (SMFCL), 13.89 times in Zenith Finance Ltd. (ZFL), 5.93 times in Valley Finance Ltd. (VFL) and the least subscribed but still over-subscribed is in the case of Capital Merchant Banking & Finance Ltd (CMBFL) by 2.02 times. This all shows those investors are interested in shares of finance companies.

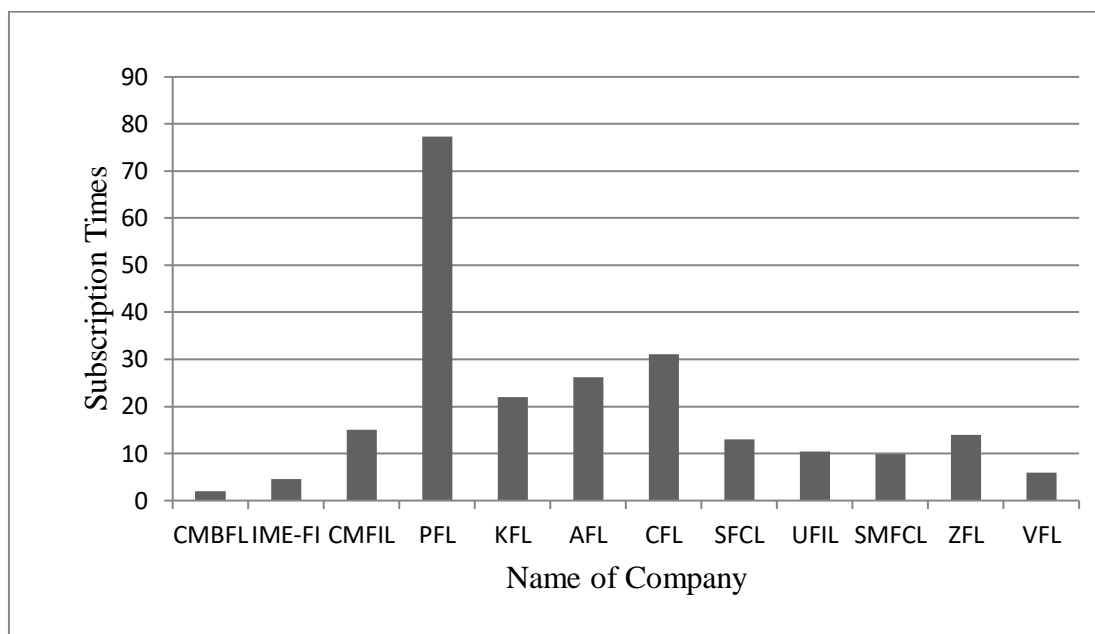
**Table 4.10**  
**Investor Response to Finance Companies**

| S.No. | Name of Company | Shares Issued | Shares Applied | Issued Year | Subscription times | Result    |
|-------|-----------------|---------------|----------------|-------------|--------------------|-----------|
| 1.    | CMBFL           | 280000        | 565881         | 2005        | 2.02               | Oversubs. |
| 2.    | IME-FI          | 175000        | 801552         | 2006        | 4.58               | Oversubs. |
| 3.    | CMFIL           | 200000        | 3000000        | 2007        | 15.00              | Oversubs. |
| 4.    | PFL             | 480000        | 37107840       | 2007        | 77.30              | Oversubs. |
| 5.    | KFL             | 200000        | 4387000        | 2008        | 21.93              | Oversubs. |
| 6.    | AFL             | 180000        | 4723740        | 2009        | 26.24              | Oversubs. |
| 7.    | CFL             | 210000        | 6522810        | 2009        | 31.06              | Oversubs. |
| 8.    | SFCL            | 400000        | 5216005        | 2010        | 13.04              | Oversubs. |
| 9.    | UFIL            | 400000        | 4168105        | 2010        | 10.42              | Oversubs. |
| 10.   | SMFCL           | 300000        | 2979005        | 2010        | 9.93               | Oversubs. |
| 11.   | ZFL             | 420000        | 5833800        | 2010        | 13.89              | Oversubs. |
| 12.   | VFL             | 1280000       | 7590400        | 2011        | 5.93               | Oversubs. |

*Source NCML, NMB, CIT, SEBON, NEFINSCO*

**Figure 4.8**

**Investor Response to Finance Companies**



The figure 4.8 clearly shows that PFL is highly subscribed while CMBFL is least subscribed. However no company is under subscribed.

**4.1.7.1.4 Investor Response to Insurance Companies**

For the study only 6 companies are taken from the population of 21.

**Table 4.11**

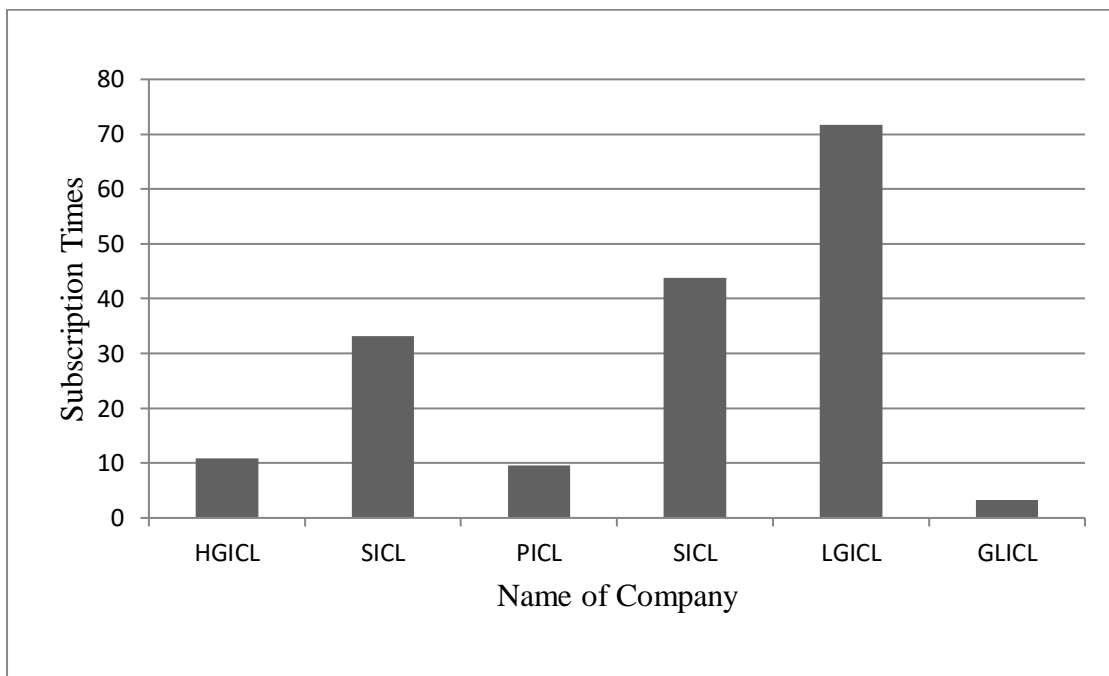
**Investor Response to Insurance Companies**

| S No. | Name of Company | Shares Issued | Shares Applied | Issued Year | Subscription times | Result    |
|-------|-----------------|---------------|----------------|-------------|--------------------|-----------|
| 1.    | HGICL           | 120000        | 225756         | 1994        | 10.85              | Oversubs. |
| 2.    | SICL            | 1020000       | 33886541       | 2003        | 33.22              | Oversubs. |
| 3.    | PICL            | 200000        | 1913620        | 2004        | 9.57               | Oversubs. |
| 4.    | SICL            | 250000        | 10939650       | 2006        | 43.76              | Oversubs. |
| 5.    | LGICL           | 250000        | 17932751       | 2007        | 71.73              | Oversubs. |
| 6.    | GLICL           | 1080000       | 3488405        | 2011        | 3.23               | Oversubs. |

*Source: NCML, NMB, CIT, SEBON*

The table 4.11 shows the investor response to insurance companies ranges from 71.73 Subscription times to 5.23 times. The highest subscription is 71.73 times for 250000 shares of Lumbini General Insurance Company Ltd (LGICL) and the lowest subscription is 3.23 times for 1080000 shares of Gurash Life Insurance Company Ltd. (GLICL). There are 10939650 shares applied for 250000 shares of Shikhar Insurance Company Ltd. (SICL) that is 43.76 times over subscription. In case of Sagaramatha Insurance Company Ltd. (SICL) 33.22 times oversubscribed. There is 10.85 times subscription for 120000 shares of Himalayan General Insurance Company Ltd. (HGICL).

**Figure 4.9**  
**Investor Response to Insurance Companies**



The figure 4.9 shows that the Lumbini General Insurance Company Limited has highest subscription rate whereas Gurash Life Insurance Company Limited has lowest subscription rate among the sample insurance companies.

#### 4.1.7.2 Non-Financial Sector

Non-Financial Sector includes Manufacturing & Processing Companies, Trading Companies, Hotels and others. Up to the fiscal year 2010/11 end, there are 32 non-financial sector companies listed. From those here 10 are taken as sample.

**Table 4.12**  
**Investor Response to Non-financial Sector**

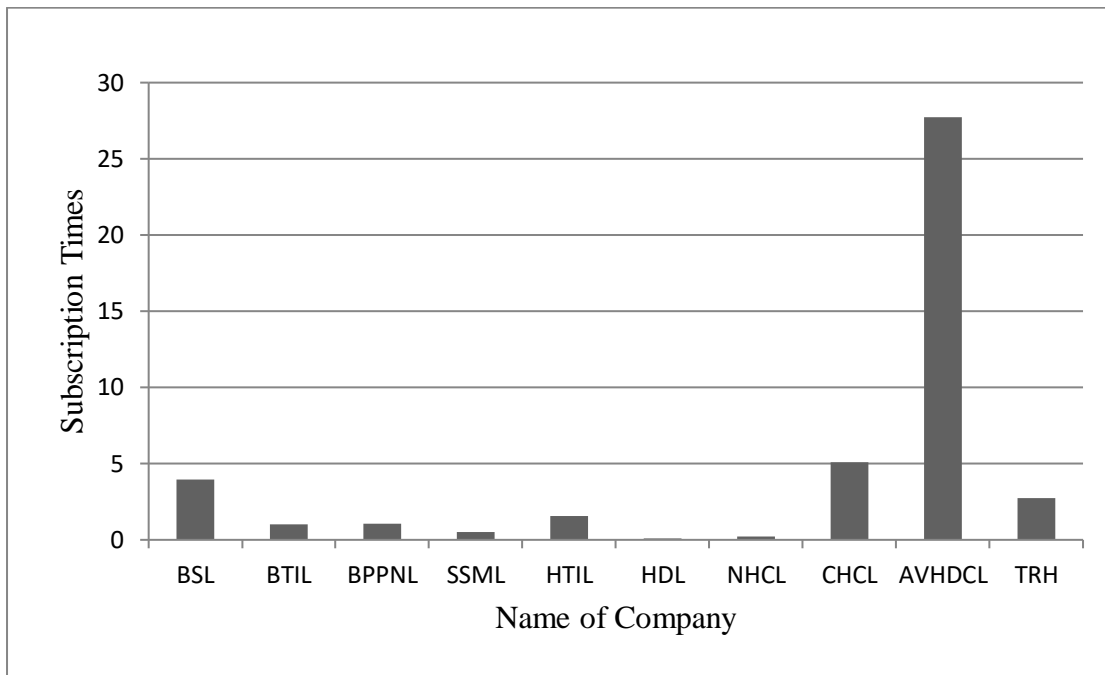
| S. No. | Name of Company | Issued Shares | Applied Shares | Issued Year | Subscription times | Investor Response |
|--------|-----------------|---------------|----------------|-------------|--------------------|-------------------|
| 1.     | BSL             | 50000         | 197150         | 1994        | 3.94               | Over subs.        |
| 2.     | BTIL            | 75000         | 75000          | 1994        | 1.00               | Constant          |
| 3.     | BPPNL           | 1050000       | 1101135        | 1996        | 1.05               | Over subs.        |
| 4.     | SSML            | 465000        | 245985         | 1997        | 0.53               | Under subs.       |
| 5.     | HTIL            | 1200000       | 1884000        | 1999        | 1.57               | Over subs.        |
| 6.     | HDL             | 17344600      | 183347         | 2001        | 0.11               | Under subs.       |
| 7.     | NHCL            | 1400000       | 301700         | 2004        | 0.22               | Under subs.       |
| 8.     | CHCL            | 2374100       | 12104112       | 2005        | 5.10               | Over subs.        |
| 9.     | AVHDCL          | 515000        | 14287748       | 2009        | 27.74              | Over subs.        |
| 10.    | TRH             | 5859390       | 16113322       | 2010        | 2.75               | Oversubs.         |

*Source: NCML, NMB, CIT, NSML*

From the table 4.12 it is found that the subscription of three companies to be under-subscribed, one company to be remains constant and the rest of 6 companies to be over-subscribed. Arun Valley Hydropower Development Company Limited has highest subscription i.e. 27.74 times. Shreeram Sugar Mills Ltd., Himalayan Distillery Ltd. & National Hydropower Co. Ltd., have the Subscription of 0.53, 0.11 and 0.22 times respectively. Oriental Hotels has high Subscription of 6.29 times. Birat Shoe Ltd., Himgiri Textile Industries Ltd., Brikuti Pulp & Paper Nepal Ltd., Taragaon Regency Hotels Ltd. and Chilime Hydro Power Co. Ltd. have Subscription of 3.94, 1.57, 1.05, 2.75 & 5.10 times respectively.

**Figure 4.10**

**Investor Response to Non-financial Companies**



The figure 4.10, it is clear that AVHDCL is highly subscribed with 27.74 times Subscription while Himalayan Distillery Ltd is least subscribed with 0.11 times among the non financial companies.

#### **4.1.8 Trend Analysis**

Trend analysis is an analysis of financial ratio over time used to determine the pattern of growth. Trend Analysis informs about the future expected values of studied variables. It gives a glimpse of future expected value if the same growth level is achieves. This information is crucial for management to make decision regarding future. This method is widely used in practice.

##### **4.1.8.1 Trend Analysis of Number of issue approved**

Trend analysis helps to predict the future. Here numbers of issues approved are forecasted with the help of trend analysis.

**Table 4.13**

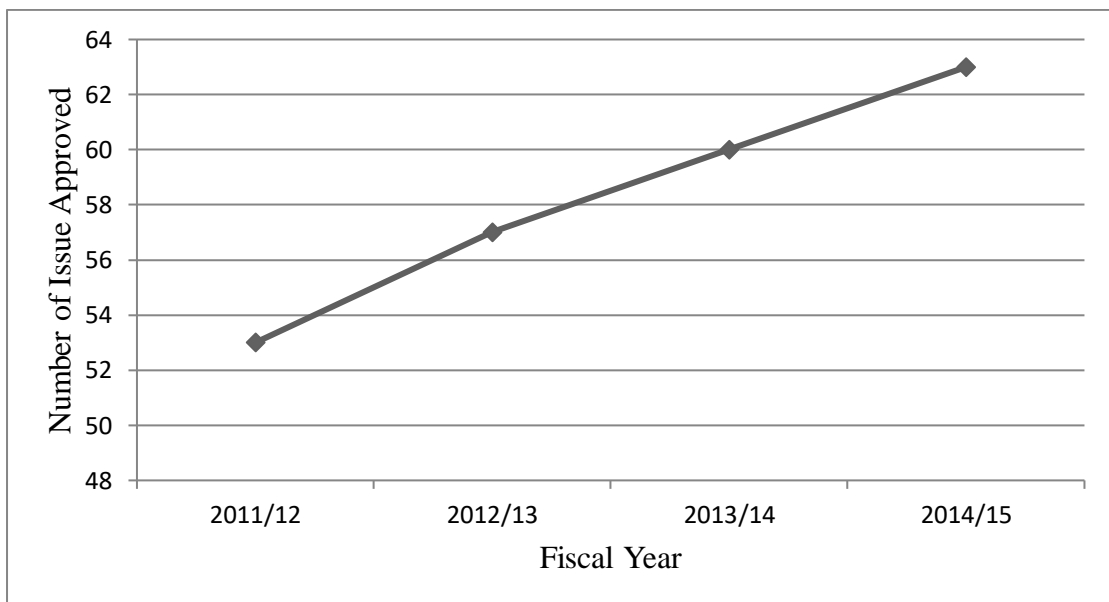
**Trend Analysis of Number of Issue Approved**

| Intercept<br>(a) | Slope<br>(b) | Forecasted Number of Issue Approved |         |         |         |
|------------------|--------------|-------------------------------------|---------|---------|---------|
|                  |              | 2011/12                             | 2012/13 | 2013/14 | 2014/15 |
| 24               | 3.1414       | 53                                  | 57      | 60      | 63      |

The table 4.13 and figure 4.11 predicts the forecasted number of issue approved for the coming four years on the basis of current 18 years. Slope is positive, so the number of issue is in increasing trend.

**Figure 4.11**

**Trend Analysis of Number of Issue Approved**



#### **4.2 Primary Data Analysis**

To meet the objectives of the study about the responses of investors, the study is made with questionnaire survey. The questions are responded from 20 respondents.

#### 4.2.1 Response about the meaning of CDS

**Table 4.14**

**Response about the meaning of CDS**

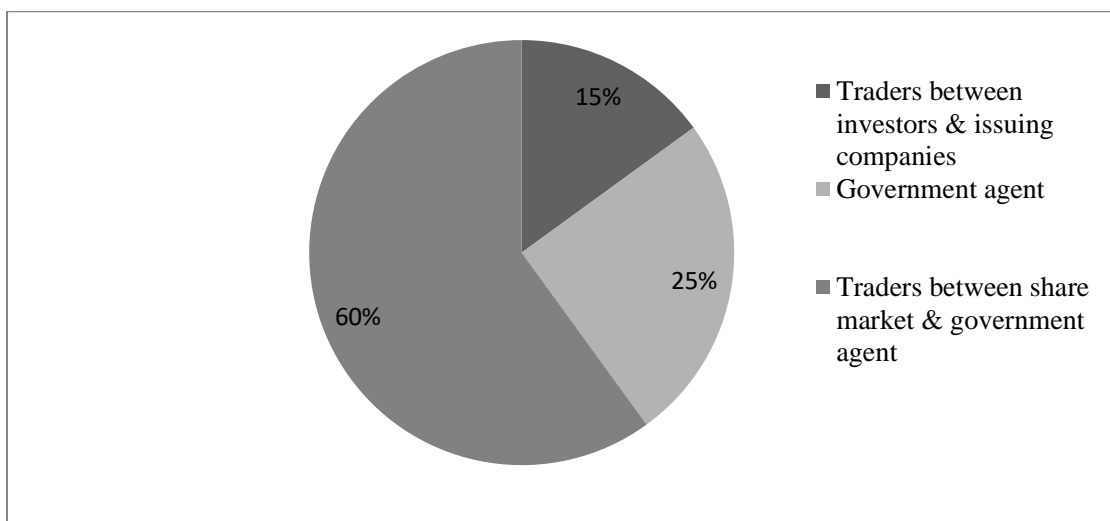
| Alternatives                                    | No. of Respondents | Percentage (%) |
|---|--------------------|----------------|
| Traders between investors & issuing companies   | 3                  | 15             |
| Government agent                                | 5                  | 25             |
| Traders between share market & government agent | 12                 | 60             |
| Total   | 20                 | 100            |

*Source: Field Survey*

The table 4.14 and figure 4.12 shows that out of 20 respondents, 60% response that the meaning of CDS is the traders between share market and government agent, 25% response that the meaning of CDS is the government agent and only 15% reply that the meaning of CDS is the traders between investors and issuing companies.

**Figure 4.12**

**Response about the meaning of CDS**



## 4.2.2 Reasons for Establishing CDS by Government

**Table 4.15**

**Reasons for Establishing CDS by Government**

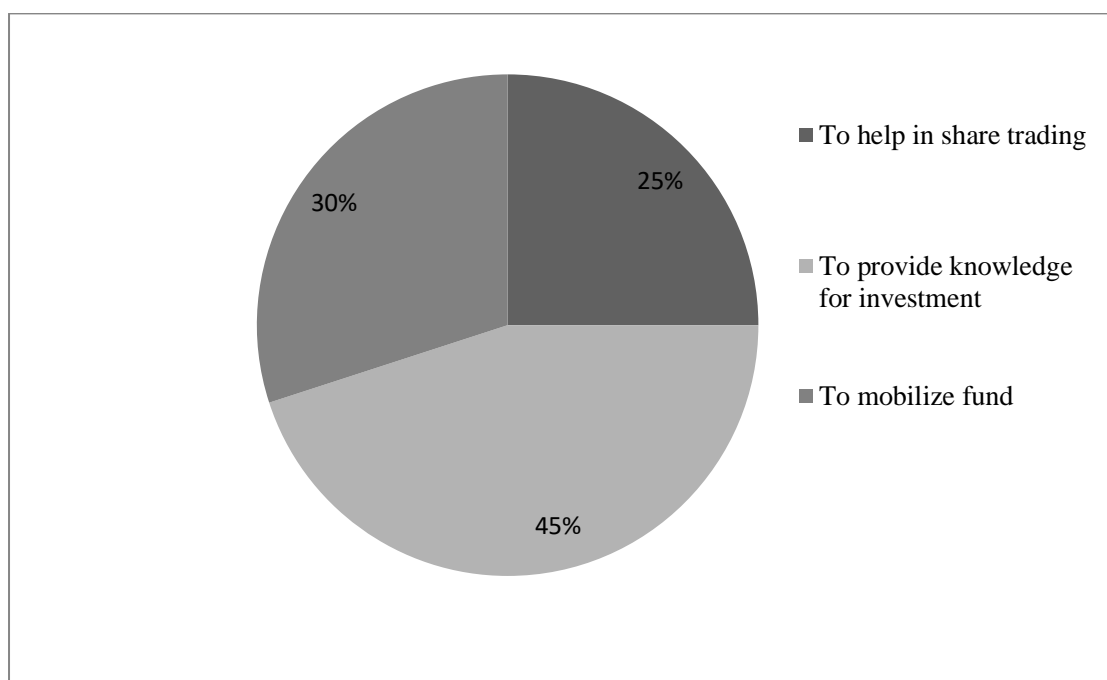
| Alternatives                        | No. of Respondents | Percentage (%) |
|-------------------------------------|--------------------|----------------|
| To help in share trading            | 5                  | 25             |
| To provide knowledge for investment | 9                  | 45             |
| To mobilize fund                    | 6                  | 30             |
| Total                               | 20                 | 100            |

*Source: Field Survey*

The table 4.15 and figure 4.13 shows that out of 20 respondents, 25% say that that the reasons for establishing CDS by government is to help in share trading, 45% reply to provide knowledge for investment and remaining 30% say the reasons for establishing CDS is to mobilize fund.

**Figure 4.13**

**Reasons for Establishing CDS by Government**



### 4.2.3 Response for Share Market

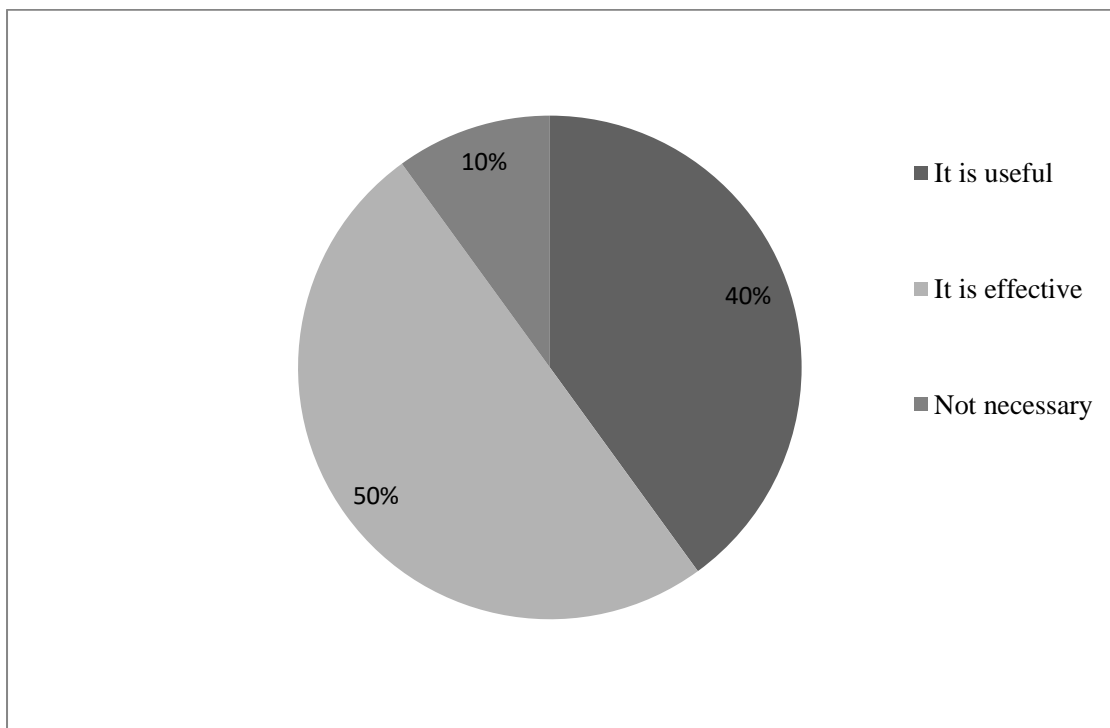
**Table 4.16**  
**Response for Share Market**

| Alternatives    | No. of Respondents | Percentage (%) |
|-----------------|--------------------|----------------|
| It is useful    | 8                  | 40             |
| It is effective | 10                 | 50             |
| Not necessary   | 2                  | 10             |
| Total           | 20                 | 100            |

*Source: Field Survey*

The table 4.16 and figure 4.14 shows that out of 20 respondents, 50% response that the share market is effective, 40% response that the share market is useful and remaining 10% reply that it is not necessary.

**Figure 4.14**  
**Response for Share Market**



#### 4.2.4 Sector's Share Desirable for the Investors

**Table 4.17**

**Sector's Share Desirable for the Investors**

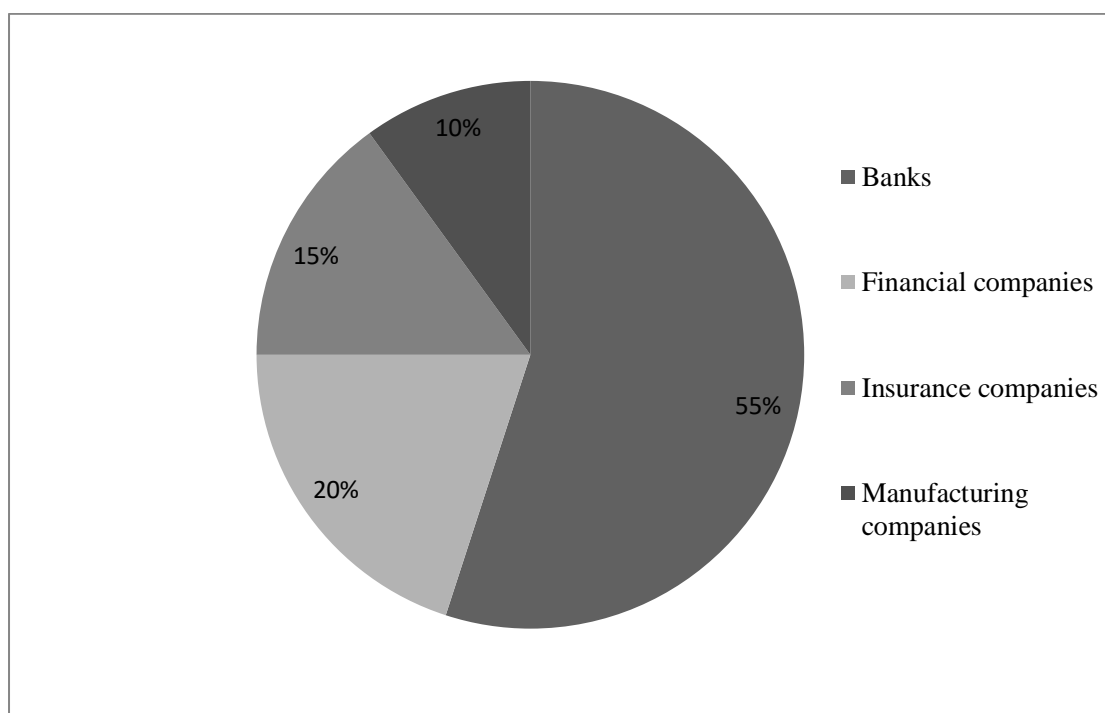
| Alternatives            | No. of Respondents | Percentage (%) |
|-------------------------|--------------------|----------------|
| Banks                   | 11                 | 55             |
| Financial companies     | 4                  | 20             |
| Insurance companies     | 3                  | 15             |
| Manufacturing companies | 2                  | 10             |
| Total                   | 20                 | 100            |

*Source: Field Survey*

The table 4.17 and figure 4.15 shows that out of 20 respondents, 55% response that the banks sector's share is desirable by the investors. 20% respondents desire financial companies, 15% respondent's desire insurance companies and remaining 10% desire on manufacturing companies.

**Figure 4.15**

**Sector's Share Desirable for the Investors**



#### 4.2.5 Response about Securities, Stock and Shares

**Table 4.18**

**Response about Securities, Stock and Shares**

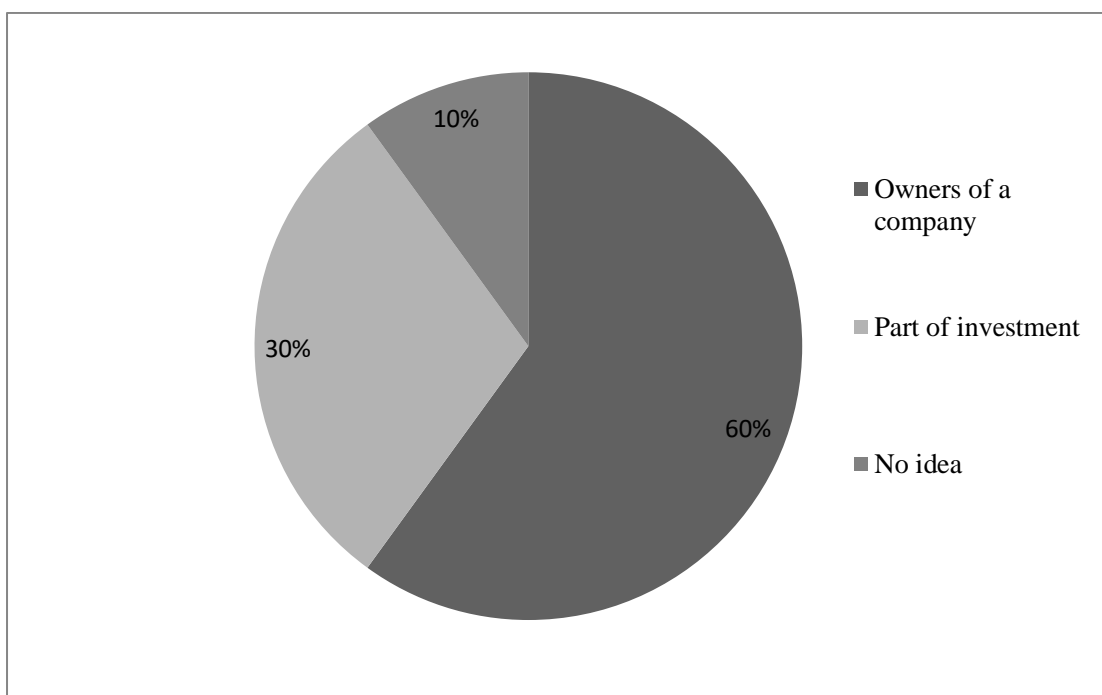
| Alternatives        | No. of Respondents | Percentage (%) |
|---------------------|--------------------|----------------|
| Owners of a company | 12                 | 60             |
| Part of investment  | 6                  | 30             |
| No idea             | 2                  | 10             |
| Total               | 20                 | 100            |

*Source: Field Survey*

The table 4.18 and figure 4.16 shows that out of 20 respondents, 60% response that the securities, stock and shares are the owners of the company. 30% respondents reply that the part of investment and only 10% reply that they have no idea.

**Figure 4.16**

**Response about Securities, Stock and Shares**



#### 4.2.6 Response for Findings the Information about IPO

**Table 4.19**

**Response for Findings the Information about IPO**

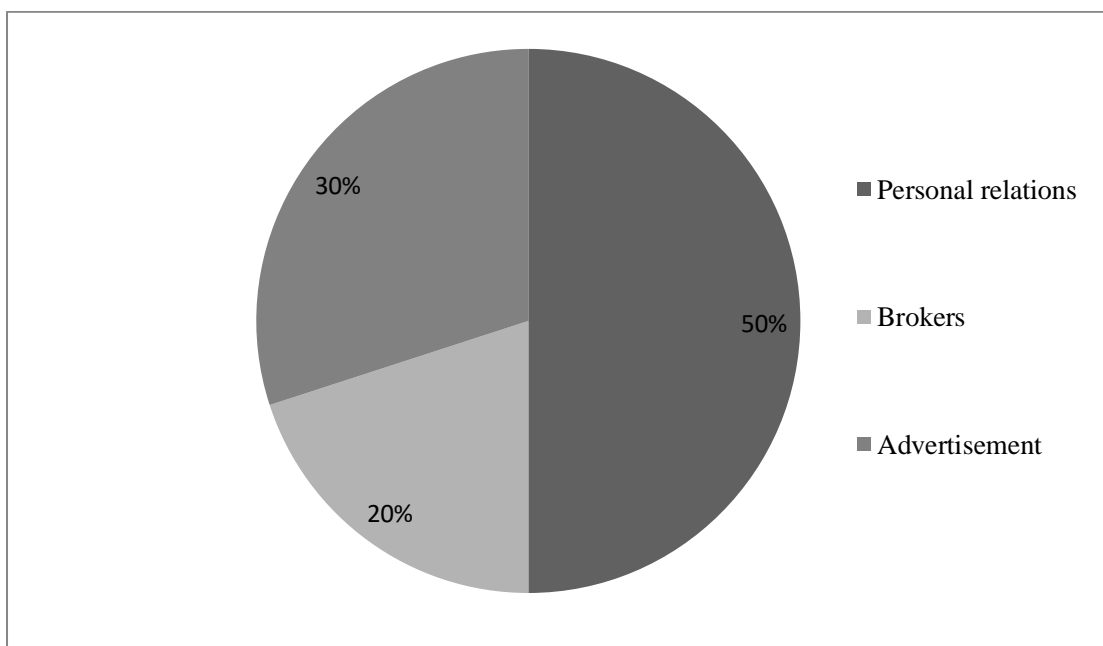
| Alternatives       | No. of Respondents | Percentage (%) |
|--------------------|--------------------|----------------|
| Personal relations | 10                 | 50             |
| Brokers            | 4                  | 20             |
| Advertisement      | 6                  | 30             |
| Total              | 20                 | 100            |

*Source: Field Survey*

The table 4.19 and figure 4.17 shows that out of 20 respondents, 50% response that they get the information about IPO by the personal relations, 20% respondents get the information about by brokers and remaining only 30% respondents get information about IPO by advertisement.

**Figure 4.17**

**Response for Findings the Information about IPO**



#### 4.2.7 Reasons for Investing in Share

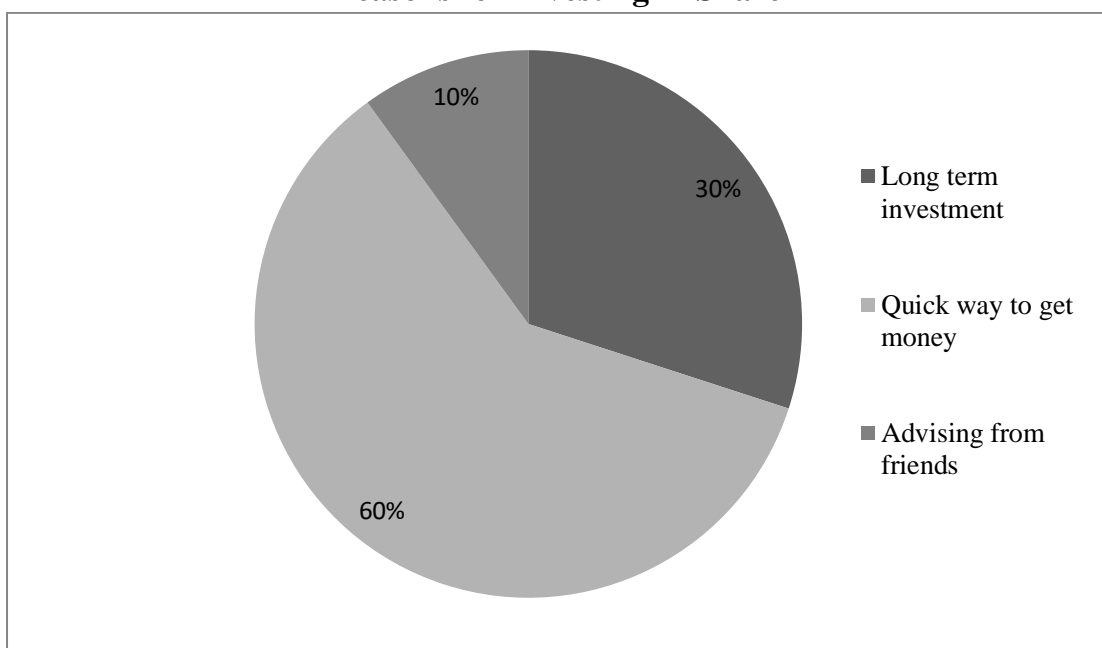
**Table 4.20**  
**Reasons for Investing in Share**

| Alternatives           | No. of Respondents | Percentage (%) |
|------------------------|--------------------|----------------|
| Long term investment   | 6                  | 30             |
| Quick way to get money | 12                 | 60             |
| Advising from friends  | 2                  | 10             |
| Total                  | 20                 | 100            |

*Source: Field Survey*

The table 4.20 and figure 4.18 shows that out of 20 respondents, 60% response that the reasons for investing in share is the quick way to get money, 30% respondents reply the reason for investing in share is that it is long term investment and remaining only 10% choose by advertising from friends.

**Figure 4.18**  
**Reasons for Investing in Share**



#### 4.2.8 Influencing Factors for Investing in IPO

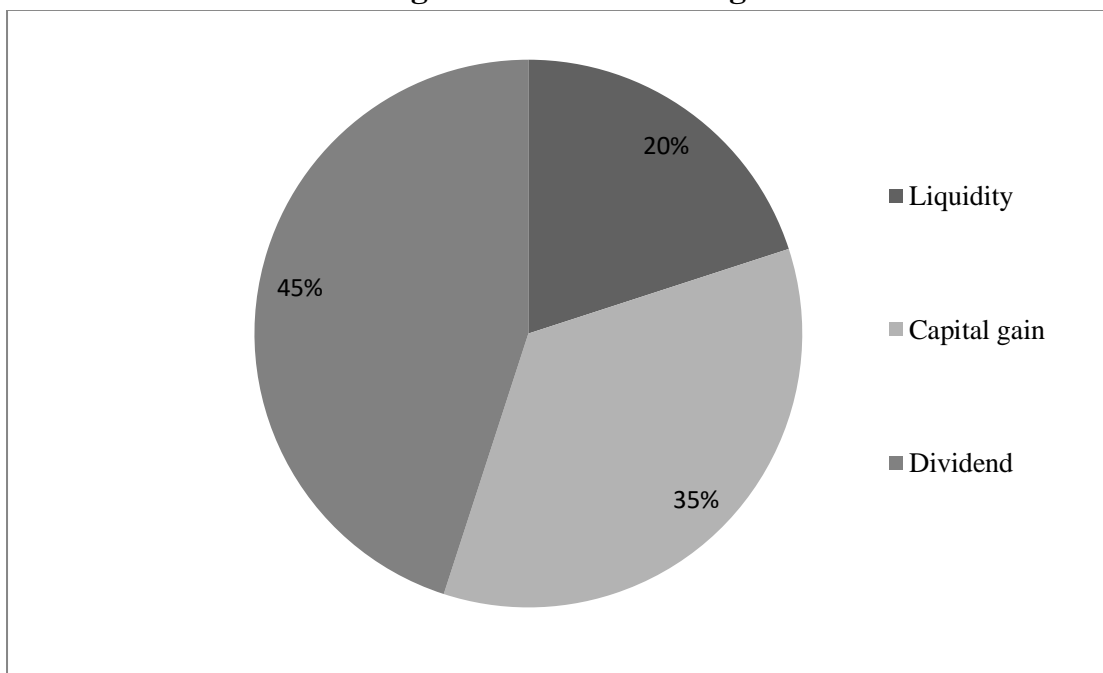
**Table 4.21**  
**Influencing Factors for Investing in IPO**

| Alternatives | No. of Respondents | Percentage (%) |
|--------------|--------------------|----------------|
| Liquidity    | 4                  | 20             |
| Capital gain | 7                  | 35             |
| Dividend     | 9                  | 45             |
| Total        | 20                 | 100            |

*Source: Field Survey*

The table 4.21 and figure 4.19 shows that out of 20 respondents, 20% respondents say that the influencing factors for investing in IPO is liquidity, 35% choose for capital gain and most of the respondents i.e. 45% say that the that the influencing factors for investing in IPO is dividend.

**Figure 4.19**  
**Influencing Factors for Investing in IPO**



#### 4.2.9 Reasons for Some Company does not want to go to Public

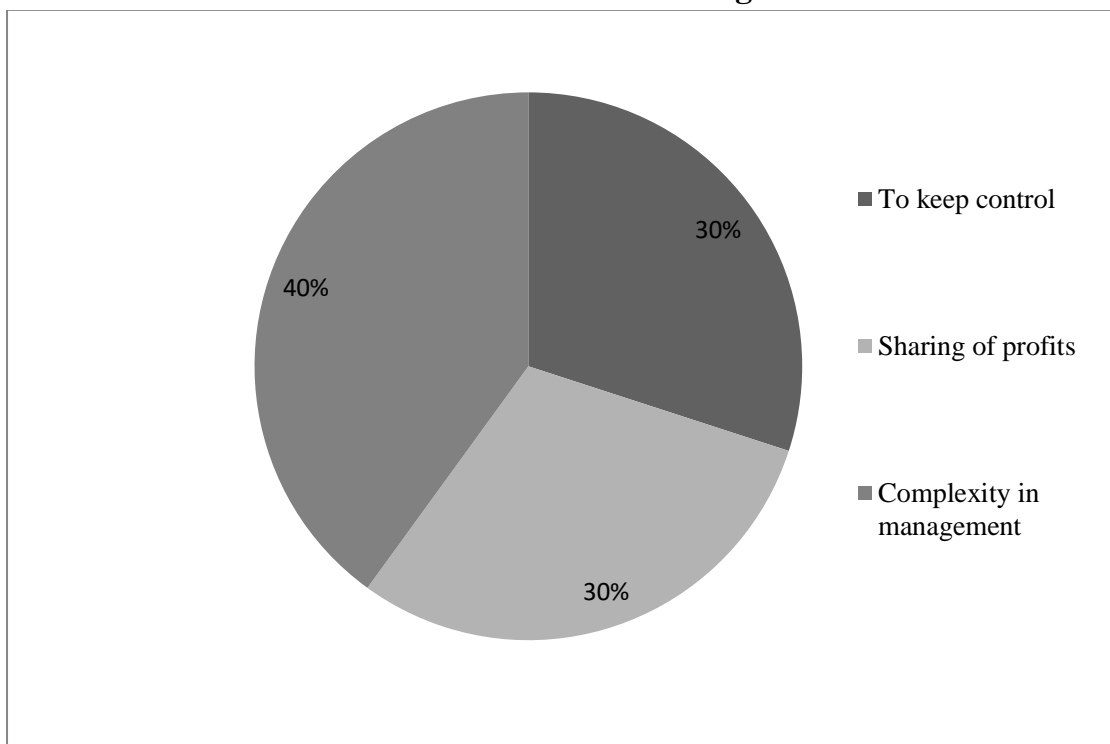
**Table 4.22**  
**Reasons for Some Company does not Want to go to Public**

| Alternatives             | No. of Respondents | Percentage (%) |
|--------------------------|--------------------|----------------|
| To keep control          | 6                  | 30             |
| Sharing of profits       | 6                  | 30             |
| Complexity in management | 8                  | 40             |
| Total                    | 20                 | 100            |

*Source: Field Survey*

The table 4.22 and figure 4.20 shows that out of 20 respondents, 30% respondents say that the reasons for some company does not want to go to public to keep control and also 30% say for sharing profits and remaining 40% reply that it is complexity in management.

**Figure 4.20**  
**Reasons for Some does not Want to go to Public**



#### 4.2.10 Reasons for Only Few People Invest in IPO

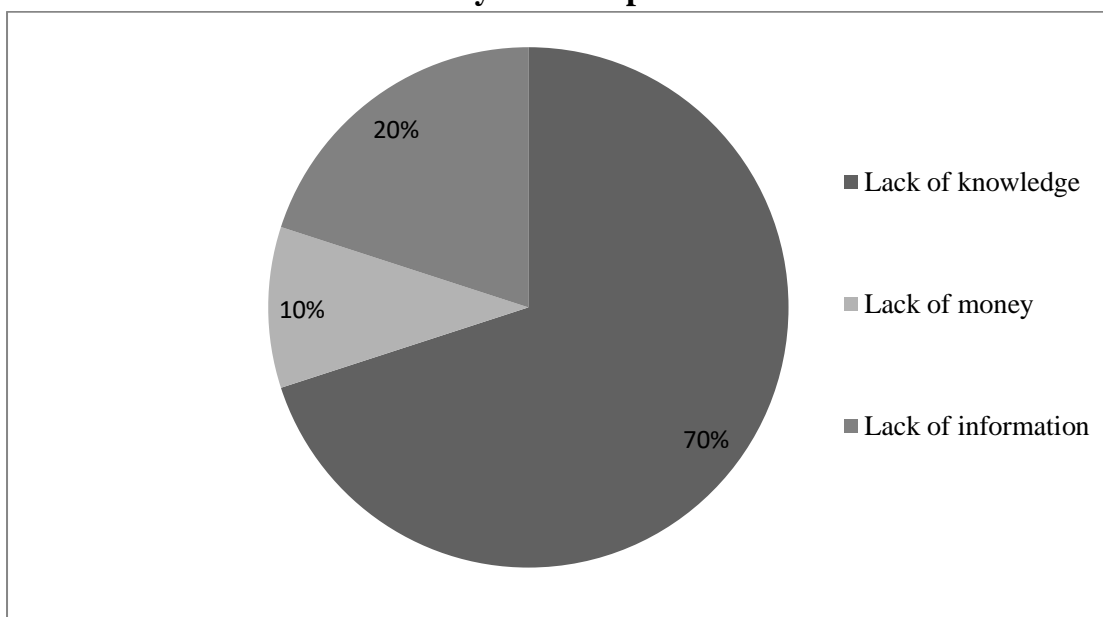
**Table 4.23**  
**Reasons for Only Few People Invest in IPO**

| Alternatives        | No. of Respondents | Percentage (%) |
|---------------------|--------------------|----------------|
| Lack of knowledge   | 14                 | 70             |
| Lack of money       | 2                  | 10             |
| Lack of information | 4                  | 20             |
| Total               | 20                 | 100            |

*Source: Field Survey*

The table 4.23 and figure 4.20 shows that out of 20 respondents, 70% respondents give reasons for only few people investing in IPO is the lack of knowledge, 10% respondents reply lack of money is the factors and remaining 20% say that the reasons for only few people invest in IPO due to lack of information.

**Figure 4.21**  
**Reasons for Only Few People Invest in IPO**



#### 4.2.11 Reasons for Decreasing the Interest on Investing on IPO These Days

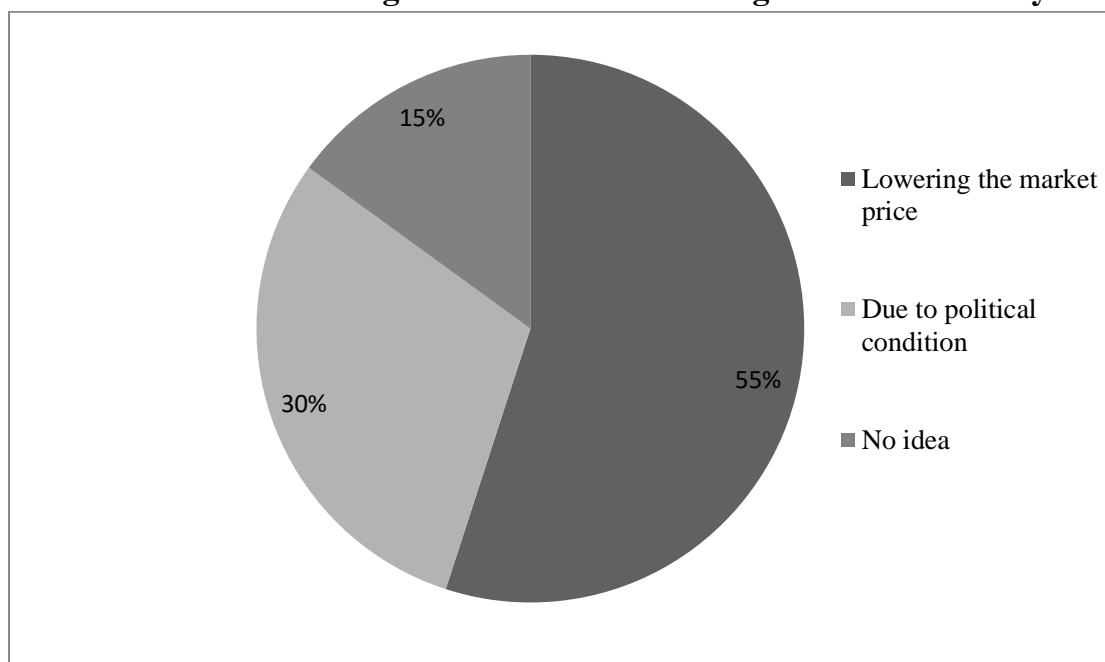
**Table 4.24**  
**Reasons for Decreasing the Interest on Investing on IPO These Days**

| Alternatives               | No. of Respondents | Percentage (%) |
|----------------------------|--------------------|----------------|
| Lowering the market price  | 11                 | 55             |
| Due to political condition | 6                  | 30             |
| No idea                    | 3                  | 15             |
| Total                      | 20                 | 100            |

*Source: Field Survey*

The table 4.24 and figure 4.22 shows that out of 20 respondents, 55% respondents say that the reasons for decreasing the interest on investing on IPO these days is that the lowering market price, 30% gives reasons for decreasing the interest on investing on IPO these days is due to political condition and remaining 15% say they have no idea.

**Figure 4.22**  
**Reasons for Decreasing the Interest on Investing on IPO These Days**



## **4.3 Major Findings of the Study**

### **4.3.1 Major Findings from Secondary Data**

- From the fiscal year 1993/94 to 2010/11 SEBON has approved 432 issues of securities amounting to Rs. 56959.48 million. The highest number of issues is in the fiscal year 2007/08 and 2008/09 and lowest number of issues is in fiscal year 1996/97 and 1998/99. The highest amount approved is Rs. 16828.51 million in the fiscal year 2008/09 and the lowest amount approved is Rs. 173.96 million in the fiscal year 1994/95.
- During the period of fiscal year 1993/94 to 2010/11 total 207 companies issued common stock for public subscription and among them common stock issue of 192 companies (92.75%) have been oversubscribed, issue of 10 companies (4.83%) have been undersubscribed and remaining 5 companies (2.42%) issue have been fully subscribed.
- Out of 207 listed companies 175 companies belong to financial sector and 32 companies belong to non financial sector. Similarly, from paid-up value perspective commercial banks occupies highest percentage i.e. 41.71 and trading occupies lowest percentage i.e. 0.08.
- By the end of the FY 2010/11, the percentage contribution of market capitalization on nominal GDP is estimated to be 24.02%. The market capitalization in the FY 2010/11 is Rs. 241513.95 million. By analyzing the sector wise market capitalization, banking sector is highest among all sectors.
- Share applied is higher than share issues in all the sample of financial sector, so that sample financial sectors are oversubscribed but there is seen undersubscribed in sample non financial sectors.
- Among the sample financial sectors Global bank has highest subscription rate in commercial banks, Gorkha development bank has highest subscription rate in development bank, Parbhu finance companies in finance companies and Lumbini General insurance companies in insurance companies. Whereas, Arun Valley Hydropower

Development Company limited has highest subscription rate among non financial sectors.

- Forecasted number of issue approved is slightly increased on the coming years than on the fiscal year 2010/11.

#### **4.3.2 Major Findings from Primary Data**

- Most of the respondents' response that the meaning of CDS is the traders between share market and government agent.
- Among the respondents, 25% say that that the reasons for establishing CDS by government is to help in share trading, 45% reply to provide knowledge for investment and remaining 30% say the reasons for establishing CDS is to mobilize fund. The study found that mainly the source of information about IPO is advertisements and personal relations.
- Among the respondents 50% response that the share market is effective, 40% response that the share market is useful and remaining 10% reply that it is not necessary.
- Mainly the respondents want to invest on Banks.
- Among respondents, 60% response that the securities, stock and shares are the owners of the company. 30% respondents reply that the part of investment and only 10% reply that they have no idea.
- A mainly personal relation is making aware to the respondents to get the information about IPO.
- Most of the respondents response that the reasons for investing in share is the quick way to get money
- 20% respondents say that the influencing factors for investing in IPO is liquidity, 35% choose for capital gain and most of the respondents i.e. 45% say that the influencing factors for investing in IPO is dividend.
- Among respondents, 30% respondents say that the reasons for some company does not want to go to public to keep control and also 30% say

for sharing profits and remaining 40% reply that it is complexity in management.

- Mostly respondents give reasons for only few people investing in IPO is the lack of knowledge,
- Most of the respondents say that the reasons for decreasing the interest on investing on IPO these days is that the lowering market price.

## **CHAPTER V**

### **SUMMARY, CONCLUSION AND RECOMMENDATIONS**

#### **5.1 Summary**

IPO is one of the mechanisms of primary market where the issuance of new securities takes place in the public. Securities offered in the first time may be debt or equity offering. Different financial intermediaries of capital market play an important role in the process and procedures in IPO of the capital market. IPO is a process of offering shares of a privately owned company to the public. In other word it is selling of securities to the general public for the first time. Primary market which avails fund to the issuer provides opportunity to invest to the small investors as well. This kind of public offering includes different kind of cost like legal fee, auditing fee, underwriting fee & time cost. Companies go public for various reasons, mainly to raise funds for operations and to be publicly traded in the stock markets, or to meet regulatory requirements.

Companies go public often by appointing issue managers and underwriters, while issue managers assist in selecting suitable securities to issue and manage subscription process, underwriters appointed by the issue managers structure and issue the IPO create syndicates and allocate the shares to the public. This study focuses on investor response to IPO, problems and growth of primary market in Nepal. Even first public issue was in 1973 A.D., secondary market come into existence only in 1993, after the conversion of Security Exchange Center in Nepal Stock Exchange Ltd. With the enactment of Securities Ordinance 2005, all companies going public must be registered at the SEBON before issuance of securities and must publish prospectus after getting SEBON's approval.

Most of the investors in Nepal lack the knowledge about IPO and if even they know, they do not want to take risk at all. For this prevailing situation of the country can be another reason. Loans from financial institution for IPO funding is breaking the healthy practice as single man applies from different names and captures large number of shares which ultimately influence company management and stock price too. IPO can be a risky investment as historical data of the issuing company affects it. As IPO's are generally under priced which attracts more investors. And if IPO's are overpriced, this may create problems to underwriters as they may not meet their commitment to issuing company. Nepali investors have developed an increasing interest in the capital market. Before 2/3 years i.e. up to fiscal year 2008/09 the primary market has been fast growing. The majority of initial Public Offerings (IPOs) are highly oversubscribed. However though investing in IPOs often guarantees returns; there also are risks in such investments. The investors should be aware of these risks and return.

From 1993/94 to 2010/11 SEBON has approved 432 issues amounting Rs. 56989.49 million. The highest number of issues is in the year 2007/2008 and 2008/2009 which is 64 and the lowest is in 1996/1997 and in 1998/1999 which is 5 only. In the issues 213 is oversubscribed, 89 were undersubscribed and 130 were constant. While analyzing, the Investor response in financial sector is higher than non financial sectors. It gives the clue that public are more attracted toward financial sector than non-financial sector.

From the primary data analyzes it is clear that Most of the respondents' response that the meaning of CDS is the traders between share market and government agent which is establish mainly to provide knowledge for investment. Among the respondents 50% response that the share market is effective, 40% response that the share market is useful and remaining 10% reply that it is not necessary. Mainly the respondents want to invest on Banks. Among respondents, 60% response that the securities, stock and shares are the

owners of the company. A mainly personal relation is making aware to the respondents to get the information about IPO. Most of the respondents response that the reasons for investing in share is the quick way to get money. Among respondents, 30% respondents say that the reasons for some company does not want to go to public to keep control and also 30% say for sharing profits and remaining 40% reply that it is complexity in management. Most of the respondents say that the reasons for decreasing the interest on investing on IPO these days is that the lowering market price.

## **5.2 Conclusion**

The development of capital market in Nepal cannot be considered as satisfactory. This is evident from the facts and figures available in the capital market performance with regards to IPO during last 18 years. The IPO condition in Nepal is not satisfactory due to the fluctuation pattern of issuance of securities. Major conclusions are as follows: The financial sectors comprises commercial banks, development banks, issuance companies, finance companies etc has been dominating the Nepalese IPO market as revealed by the number of issues and amount of issued offered the study period. There is lack of investment opportunities cause the IPO market is highly depends upon the ordinary and right shares. The IPO of debentures and preference share is in underdeveloped situation in Nepal.

Most of the company's IPO received overpowering demand from the public which result the over-subscription of their issues. Furthermore, finance sectors have been oversubscribed and non- finance sector have been under-subscribed. Moreover, the IPO of ordinary shares are more preferred instrument by general public as a result most of the ordinary shares are oversubscribed. The year-wise IPO during the study period has been fluctuating. However investor's response to IPO is increasing heavily up to fiscal year 2008/09 and then somehow falls. SEBON is implementing different regulation related to primary and secondary market. Securities Board related Regulations, Stock Exchange Operation

Regulations, Securities Businesspersons (Broker, Dealer and market maker) Regulation are implemented.

Various guidelines have been issued to regulate and make primary market transparent and fairness. Securities Regulation and Approval Guidelines, Securities Issue and Issue Management Guidelines, Share Allotment Guidelines are some of the guidelines to promote and regulate primary market in Nepal. 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 in part of big investors. This kind of mismanagement in allotment discourages the investors. Contract between the issue manager and the issuing company highly affects the whole IPO process. People are eager to know the promoter, company's performance before investment. IPO's handled by bigger brokerages are found to be more successful.

### **5.3 Recommendations**

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

- 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.
- 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.
- 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.

- 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.
- As investment bankers play a vital role in the IPO process, they should try to give more transparent, fast, hassles free service so that more public involve in the IPO.
- Small investors are also the part of primary market, so IPO funding through financial institution should be strictly regulated to discourage the big investors who apply in names of relatives, friends etc.
- The information and financial statements of the companies should be disseminated properly and timely. The market intermediaries should be educated, trained and professionalized by conducting the various program like On Job training, Technical training etc. etc.
- Further studies can be conducted by increasing sample size, by increasing number of observations and by using other methodologies.

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# APPENDICES

## Appendix-I Questionnaires

This questionnaire is a part of my research work entitled “A Case Study of Public Response to Initial Public Offering”. I request you all to fill this questionnaire with sincerity. Your response will have direct impact on research outcome, so I request you to be honest.

### **Personal Information:**

Name: ..... Occupation: .....

Age/Sex: ..... Education:  
.....Qualification.....

Address.....

### **Questions for the survey**

- 1) What do you mean by CDS?
  - a. Traders between investors and issuing companies
  - b. Government agent
  - c. Share markets and government
  
- 2) Why government has established the CDS?
  - a. To help in share trading
  - b. To mobilize fund
  - c. To provide knowledge for investment
  
- 3) What do you think about the Share Market?
  - a. It is useful
  - b. It is effective
  - c. Not necessary

- 4) Which sector's share is desirable for the investors?
  - a. Banks
  - b. Financial companies
  - c. Insurance companies
  - d. Manufacturing companies
  
- 5) What do you know about securities stock and shares?
  - a. Owners of a company
  - b. Part of investment
  - c. No idea
  
- 6) Where do you find the information about IPO?
  - a. Personals relations
  - b. Brokers
  - c. Advertisement
  
- 7) Why do you invest in share?
  - a. Long term investment
  - b. Quick way to make money
  - c. Advising from friends
  
- 8) What are the influencing factors for investment in IPO?
  - a. Liquidity
  - b. Capital gain
  - c. Dividend
  
- 9) Why some company does not want to go to public?
  - a. To keep control
  - b. Sharing of profit
  - c. Complexity in management

10) Why only few people invest in IPO?

- a. Lack of knowledge
- b. Lack of money
- c. Lack of information

11) Do you know why the interest on investing on IPO is decreasing these days?

- a. Lowering the market price
- b. Due to political condition
- c. No idea

**Appendix-II**  
**Calculation of Trend Analysis**

**Number of Issue Approved**

| Year (X) | $x=X-A$ | Number of Issue<br>Approved (Y) | $x^2$                  | $xY$             |
|----------|---------|---------------------------------|------------------------|------------------|
| 1993/94  | -8.5    | 16                              | 72.25                  | -136             |
| 1994/95  | -7.5    | 10                              | 56.25                  | -75              |
| 1995/96  | -6.5    | 12                              | 42.25                  | -78              |
| 1996/97  | -5.5    | 5                               | 30.25                  | 27.5             |
| 1997/98  | -4.5    | 12                              | 20.25                  | -54              |
| 1998/99  | -3.5    | 5                               | 12.25                  | -17.5            |
| 1999/00  | -2.5    | 6                               | 6.25                   | -15              |
| 2000/01  | -1.5    | 9                               | 2.25                   | -13.5            |
| 2001/02  | -0.5    | 12                              | 0.25                   | -6               |
| 2002/03  | 0.5     | 18                              | 0.25                   | 9                |
| 2003/04  | 1.5     | 14                              | 2.25                   | 21               |
| 2004/05  | 2.5     | 14                              | 6.25                   | 35               |
| 2005/06  | 3.5     | 29                              | 12.25                  | 101.5            |
| 2006/07  | 4.5     | 34                              | 20.25                  | 153              |
| 2007/08  | 5.5     | 64                              | 30.25                  | 352              |
| 2008/09  | 6.5     | 64                              | 42.25                  | 416              |
| 2009/10  | 7.5     | 61                              | 56.25                  | 457.5            |
| 2010/11  | 8.5     | 47                              | 72.25                  | 399.5            |
| Total    |         | $\sum Y = 432$                  | $\sum x^2 =$<br>484.50 | $\sum xY = 1522$ |

Assume,  
A=2002.5  
Now,

$$a = \frac{\sum Y}{N} = \frac{432}{18} = 24$$

$$b = \frac{\sum xY}{\sum x^2} = \frac{1522}{484.50} = 3.1414$$

Now for coming years,

For 11/12,

$$\begin{aligned} Y &= a + bx \\ &= 24 + (3.1414 \times 9.5) \\ &= 53 \end{aligned}$$

For 12/13,

$$\begin{aligned} Y &= a + bx \\ &= 24 + (3.1414 \times 10.5) \\ &= 57 \end{aligned}$$

For 13/14,

$$\begin{aligned} Y &= a + bx \\ &= 27372.20 + (3507.46 \times 11.5) \\ &= 60 \end{aligned}$$

For 14/15,

$$\begin{aligned} Y &= a + bx \\ &= 27372.20 + (3507.46 \times 12.5) \\ &= 63 \end{aligned}$$