CHAPTER-I

INTRODUCTION

1.1 Background of the Study

Nepal is the one of the richest countries in the world in terms of bio diversity due to its unique geographical position and altitudinal variation. The elevation of the country ranges from 60 m at sea level to the highest point on earth, Mt. Everest at 8,848 m, all within a distance of 150 km resulting into climate conditions from sub – tropical to arctic. Nepal is landlocked country, sandwiched between two Asian giants i.e. peoples' Republic of China and India. However, Kolkata port of India and Chittagong / Mongola ports of Bangladesh are used for International trade. Nepal is spread over 147,181 square kilometers. Nepal has 5 development regions, 14 zones and 75 districts.

Nepal is one of the least developed countries in the world with very low per capita income and very low corporate growth rate. The country is in the state of developing its economy but the economy of the country is still base on primitive traditional business. The traditional concept of business and commerce is deep rooted in the consciousness of people and most people are unaware of modern form of commerce. The concept of capital market is new to people. The financial market in Nepal is in early stage. There was not satisfactory growth of business enterprises until the restoration of democracy. Nepal has already launched more than four decades long national plans for economic development. And the currently developing liberal economy in the country is trying to gear up the acceleration of development. However, any strategy for economic development requires a steady supply of medium and long-term funds for productive investment for mobilization of invest able resources.

The most sensitive component for any economies of the world is "capital market". It lays a vital role to direct the country's economic activities. So that it's smooth operation is significant in this free market world for making the economy of the country at ease. It helps to mobilize domestic resources. It's role to provide the best investment opportunity by transferring the funds from surplus sectors to deficit sectors through transaction of stocks. That's why, for the attainment of self-reliant growth of national economy and smooth running of the economic activities of a nation, capital market's role has become major importance in financial management.

Capital market is mainly affected by the political instability, riots, war and depresses economic conditions. In spite of many affecting factors, the capital market of Nepal is showing positively in recent year and Nepalese investor are optimistic towards the development of capital market which is clearly shown from their increasing investment in the share of Nepalese corporations. The NEPSE index is shooting up gradually that indicates the growing market capitalization in the only stock market of the country. It needs continuous research and study for its smooth operation. It should cover all the regions and sector of the country. The government should also gradually deregulate the market according to the global economic movement. The market should promote all types of market instruments as well as inspire all the players of the market. So that, they fell that it is the one of the major place which can drive the economic development of the country at large. Van Horne (1998) states that "When a company formed, it obviously must be finance. Often the seed money comes from founders and their families and friends. For some companies, this is sufficient to get things launched and with retained Earnings, no mare equity are needed. In other situations equity infusions are necessary."

Ordinary share, preference share and debenture are three important securities used by firm to raise fund to finance their activities. Ordinary share provide ownership right to ordinary shareholders. They are the legal owners of the company. As a result, they have residual claims on income and assets of the company. They have right to elect the board of directors and maintain their proportional ownership in the company called the preemptive right. The preemptive right of equity funds through right offering. Right issue does not affect the wealth of shareholders. "The price of the share with on gets dividend into ex-right price and the value of the right. So what the shareholder gains in terms of the value of the right he losses in term of the low ex-right price. However, he will loss if he does not exercise right"(Pandey, 1999:548)Right share are issued to the existing shareholders as a result of increased in capital if current reserve is not sufficient to issue bonus shares. Company usually issued right share to raise the capital. Therefore, issue of right share represents the distribution of shares to the existing shareholders on the proportion of the number of shares they own. The shareholder has an option to purchase a specified numbers of shares at subscription price which is below current market price within specified period of time.

Large number of corporate firms announces and issue right share to increase the capital base if the corporate management felt such need or to comply with the policy directives given by concern authority to increase the capital base from time to time. In our country, Nepal Rastra Bank issues the policy provisions regarding the requirements of minimum paid up capital in commercial bank, which significantly affected the right share issuing practices of commercial banks in Nepal. A company issues right share under the principle of preemptive right of the shareholders. Under this right, the existing shareholders have the first priority to purchase any new equity share issued by the company. Right offering is made generally with the purpose of:

- Maintaining the management control by existing shareholders,
- Minimizing the floatation cost for new issue and
- Protecting the existing shareholders from dilution of their wealth position.

Right issue practice in Nepal has no long history as compare to other developing country. While looking the issue approval from the SEBON researcher can easily notice an increasing trend of issuing right share. During the 15 years period, SEBON has granted right issue approval amounting Rs. 33815.57 million. This amount comes to be the second largest amount among various issue approved by SEBON. Right issue occupied 68.11% of total listed companies given the issue approval only 184 companies issued right share to raise fund. In Nepal, company act 1997 has provisioned about the preemptive right of shareholder in the section 42(4). It stated that if the right is contained in a firm's charter then the firm must offer common stock to existing shareholders. If the charter does not prescribe the preemptive right the firm has a choice of making the sale to its existing shareholders or to an entirely new set of investors. Rights have intrinsic financial values because they are normally afforded at a price somewhat lower than the current market price of stock.

1.2 Focus of the Study

Right offering affects the value of the firm. So right offering is the important financial decision in an organization. The main focus of this study is to find out the trends of right offering in the context of Nepalese stock market. The purpose of this study is to provide the clear vision of the role of right offering on the stock price movement. This study also finds out the uses of right offering, stock price movement and current legal provision regarding right share issue and its importance.

1.3 Statement of the Problems

Issue of right share represents the distribution of shares to the existing shareholders on the proportion of the number of shares they own. So, announcement of right offering is fine rumor to the existing shareholders. From right offering, existing shareholders can purchase the share of the company at subscription price which is for below the current market price. Right offering is defined as one of the popular methods of raising the long term fund as the targeted capital structure of the company or firm requires. In the first time in Nepal, Nepal Finance & Saving Company Ltd. got issue approval of right share in fiscal year 2052/53. After 15 years right share offering is still a new and emerging concept for both investor and organizations. Most of the Nepalese people are not known about the phenomenon of share trading, it is therefore; only few investors are getting advantages from share transaction. Among them large number of people who are the prospective investors are found to be very interested on share trading activities under such circumstance the study is focused on the level of knowledge of generate people on share trading i.e. Right share issue. A shareholder, whose name is in the company book before record date, is entitled to have a proportionate number of new shares at price below market.

We can find the number of the share to be issued by dividing the fund to be raised by the subscription price of each share. We can divide the no. of new share in the number of existing shares to get the number of rights required to subscribe one share of the new stock. It means high subscription price makes more rights needed to buy a share of the stock and vice versa. Value of right can be calculated by using rights on and exercise price. Theoretically, the value of share should increase after the announcement of right offering and then decrease (by value of each right) after the subscription date. But this trend is not found to be followed in Nepalese context. In the above mentioned condition, the problems towards which this study is directed are:-

- What is the existing practice of right issue in Nepal?
- How is the level of knowledge of Nepalese investors about right offering? In other words, how familiar are the Nepalese investors about right offering?
- Does share price fully reflect all the information's accompanying the right issue announcement?
- Do Nepalese investors use available information regarding right issue to maximize their wealth?

- What is the effect of Right Share issue on the market price of the share? In other words, will the right share issue, because it increases the supply of share, have a depressing effect on the share prices?

1.4 Exercise of Rights Issue in Nepal

The history of security market in Nepal began with the flotation of shares by Biratnagar Jute Mills limited and Nepal Bank Limited in 1937. It was first to initiate the issue of equity to the general public. The trend of selling corporate stock began only after the issuance of ordinary shares by the Biratnagar Jute Mills limited. At that time when the issue of shares was concept, there was no any capital market for selling and buying of stocks Legal provision about the capital market was not mentioned. Introduction of the Company Act in 1964, the first issuance of Government Bond in 1964 and establishment of Security Exchange Center in 1976 A. D. were other significant development relating to capital markets. When the Security Exchange Center was establishment, the trading of securities also began. At the current time, there are two secondary markets and they are Security Board of Nepal (SEBON) and Nepal Stock Exchange (NEPSE) which makes available the trading floor of the securities to the investors. SEBON is rigorously working for bringing out with the approval of Government, the Securities Registration and Issuance Regulation for effective provisions of prospectus approval and registration of securities issue, Mutual Fund Regulation for registration and approval of mutual fund operation, and Securities Businesspersons (Merchant Banker) Regulation for developing more competitive and professional merchant banking services. Securities Exchange Center was established with an objective of facilitating and promoting the growth of capital markets. Before conversion into stock exchange it was the only capital markets institution undertaking the job of brokering, underwriting, managing public issue, market making for government bonds and financial services. Nepal Government, under a program initiated to reform capital markets converted Securities Exchange Center into Nepal Stock Exchange in 1993. In the context of right shares, there is no particular guideline. Because of changing the political environment, the corporate sectors are also affected. The different factors like political en-establishment, unsustainable government policy, law economic growth, lack of industrialization and other current factors also affect the development of the corporate sectors. In Nepal, some joint venture companies were established because liberalization policy was implemented by Nepal Government. At that time when the issue of ordinary shares was new practice, there was no the trend of issuance of right shares. The issue of right share is new concept and is adopted by the investors. So the history of the issue and practice of right share is not so long in Nepalese Capital market. The practice of issue of right share has brought significant changes in the Nepalese corporate sector. Nepal Finance & Saving Co was the first company, who issued rights shares in Nepalese stock market in fiscal year 2052/53.

From the fiscal year 2052/53 the issue of right shares has been started and till the fiscal year 2066/67, the issue of right shares is taken place. There are 184 companies who had issued right shares up to the fiscal year 2066/67. If the company needs additional fund for different purpose, then one of the alternative is the right offerings. In Nepal, there are mostly Banks or the Finance companies who issued right shares. There are very few companies from other sectors who issued the right shares.

Every firm needs adequate capital to perform efficiently. Generally, firms fulfill their financial requirement by issuing equity share, preference share, debentures and long term bonds. Rights issue is one of the instruments to raise additional capital. We can describe the preemptive right or rights as the privilege offered to existing stockholders for buying specified number of additional shares of the company's stock before the stock is offered to outsiders for sale. They have value because generally they are offered at a subscription price somewhat lower than the market price of share. In the secondary market, investors are willing to buy the share that has been attached to the preemptive right. But to buy additional number of shares, the shareholder should have his/her name in company's book before the record date. Hence before the record date, there will be a great demand of share attached with rights. Demand is increased because large numbers of people rush to secondary market in order to enlist their name in the company's book before record date so that they can enjoy the benefits of right offering. On the other hand, existing shareholders generally have no willingness to sell the shares to exercise the rights. Due to this double pressure, the price of share goes upwards.

Theoretically price of share increases after rights offering and decreases after the issue of right share but some practical cases in Nepalese companies have mixed results in this regard. Nepal Finance and Saving Company Ltd. announced issue of right share for the first time (December 1, 1995) when market price of its share was constant at Rs. 110 for two months before announcement. But after announcement, there was only one transaction before the record date that even at a price below its previous market price. Ace Finance Company Ltd. is another example whose stock price was Rs. 410 before the announcement but after announcement there was no transaction at all before the record date. Necon Air's stock was priced at Rs. 309 before the right share announcement but it grew up to Rs. 366 after the announcement. This is the case that follows the price movement consistent with the theory that rights offering announcement appreciates the price of the share. Share prices of the majority companies were decreased after the rights share announcement and decreased rapidly after allotment. Only few companies met the theory. The following table shows the contribution of rights issue in the total public floatation in each fiscal year in which rights issue had taken place.

Each shareholder is issued an option to buy a certain number of new shares and the terms of the option are contained on a piece of paper called "right". Each shareholder receives one right for each shares of the stock owned. This research includes sixteen companies about the right offering.

1.5 Objectives of the Study

Within the periphery of the stated problem of the study, the main objective of this study is to analyze and examine the affect of right offering and its effect on stock price movement in the context of Nepal. However, the specific objectives of the study are as follows:-

- To find out whether Nepalese investors use available information regarding the right issue announcement to maximize their wealth.
- To see and identify right issue practice in Nepalese financial market.
- To find out impact on changes in market price of the stock before and after the announcement of right offering.
- To see the theoretical values of right and its effect of right on stock price.
- To recommend some policies that will help to rectify the current problems in the right issue of securities.

1.6 Significance of the Study

Mainly this case study on right share issue and its effect on market price of stock are very helpful to those existing shareholders and also potential investors who are interested to know about right share. The practice of Right share in Nepal starts from fiscal year 2052/53 but there is hardly to find any research which shows the relationship between information accompanying the right issue announcement on the market price of the share. So, this study emphasis and helps those who want to study in further detail and widely in this field. The significances of the study can be point out as follows:-

- Firstly, this study is very useful to existing shareholders, financial managers, stock-broker, financial counselor and the market maker's of stock marker Nepal.
- The study may draw the attention from every corner of investors and other academicians and also interested parties.

- This study will extremely helpful to the existing shareholders to know about the movement of their share price with respect to the right issue announcement after and before.
- This study is also benefited that the study will provide some valuable input for the further study in this field.
- Students who are studying about the right share in their course they will get benefit by this study.
- With help of this study, I get also know about right share practice in Nepal

1.7 Limitation of the Study

The study will have some limitation. Basically the study is done for the partial fulfillment of masters of business studies. It has been tried to make this study more comprehensive and clear by collecting, tabulating, compiling and presenting recent information as for as possible. Due time constraints, financial problem and lack of research experience, the study has been conducted with the following limitation.

- This study covers only those companies who have been issued right share.
- The study is done for the partial fulfillment for MBS degree in management so it is not a comprehensive study.
- A number of variables are causes or responsible factors in the movement of share prices but this study only on the rights offering and current legal aspects associated there in.
- This study is based on both secondary and primary data which are collected from annual report of SEBON, respected company, issue manager and expert.

Regarding primary data questionnaire and interview are used.

- In case of the primary data, brokers give right to his/her staff to fill the questionnaire and they fill according to their view. This may not represent the companies view.
- The unavailability of plentiful literature on the subject and lack of various references & resources has too handicapped the study to some extent.
- Result of the study would be fully dependent on the accuracy and reliability of the data provided by the respected organization and respondents

1.8 Organization of the Study

The whole study has been divided into five chapters:

Chapter I: Introduction

The first chapter deals with the introduction of the study, background of the study, introduction of financial market, focus of the study, statement of the problems, objectives of the study, limitation of the study, significance of the study, statement of hypothesis and organization of the study.

Chapter II: Review of Literature

The second chapter deals with review of the different available literature review of books, article, reports and thesis related to the study field.

Chapter III: Research Methodology

The third chapter deals with the research methodology which explains the research method used in the study. It includes research design, sources of data, population and samples, sources and techniques of data collection and data analysis tools.

Chapter IV: Data Presentation & Analysis

The fourth chapter is the main part of the study which is the most important chapter of this study. It includes presentation and analysis of data by using financial and statistical tools.

Chapter V: Summary, Conclusion & Recommendations

The fifth and last chapter includes summary of the study, conclusion and recommendation.

Bibliography and appendix will be attached at the end of the study.

CHAPTER - II
REVIEW OF LITERATURE

2.1 Introduction

In introduction chapter described about background of the study, focus of the study, statement of problems, objective of study, limitation of study, significance of the study and organization of the study. This chapter deals with the literature of previous studies on right issue and its impact of share price in more detail and suggestive manner. Regarding the review of literature various books, journal, articles from newspaper, some research reports and magazine related with the topic is reviewed. It covers those studies that are conducted within and outside the country, but no important studied have been conducted in Nepal. This chapter provides some conceptual theory of equity rights issues.

2.2 Right Offering: A theoretical Framework

2.2.1 Preemptive Right

A publicly held corporation can raise equity capital either by selling equity directly to investors or by issuing rights to its share holders. When a corporate offers its shares to existing share holders prior to general public it is termed as right offering. Preemptive rights are the privilege of existing shareholders to participate in a right offering. *(Weston & Brigham, 1992 : 677),* states that the preemptive right gives holders of common stock. The right is made part of every corporate charter in some places and it is necessary to insert the right especially in the charter for others. The Preemptive rights are of two types. First, it protects the power of control of present stockholders. If it were not for this safeguard, the management of corporation under criticism from stockholders could prevent stockholders from removing if from office by issuing a large number of additional shares at a very low price and purchasing these shares itself. It would thereby secure control of the corporation to discourage the will of the current shareholders. The Second and important is protection that the preemptive right affords stockholders concerns dilution of value.

2.2.2 Rights Offering

If the preemptive right is contained in a firm's charter, then the firm must offer any new common stock to its existing stockholders. If the charter does not prescribe a preemptive right, the firm has a choice of making the sale to its existing stockholder or to an entirely new set of investors. If it sells to the existing stockholders, the stock floatation is called a rights offering, each stockholder is issued an option to buy a certain number of the new shares, and the terms of the option are contained on a piece of paper called a right. Each stockholder receives one right for each share of stock owned.

When a company makes a rights issue, it sends a "letter of offer" to its existing shareholders indicating the amount of new shares or coupons to which they are entitled in proportion to their old shareholding. This "Letter of offer is like share purchase warrant in nature generally referred to as rights. These rights must be exercised within a given period, which is relating short, usually, not more than thirty days, unless the date is extended by the company. The privileged subscription is fairly simply in the sense that after the issue has been approved by the company and the controller of capital issues, notices are sent to shareholders indicating that all those who are shareholders within certain recording date may get additional shares in a given proportion. Right of the shareholders when a rights issue is made is as follows.

- First, Subscribed for the New Shares, if the shareholder has sufficient cash to buy the new shares, and if he/she feels that the company will use the money, so raised in a profitable way, and then he/she should take up the rights.
- Second, Sells the rights, the new shares are cheaper than the current market price. Both new and old shares will rank on equal footing when the formulations have been completed.

- Thus, the new zero value paid shares have values for which a third party would be willing to pay. The shareholders who are not happy with the rights issues or equalities, they can sell the rights. The rights are sold through the broker who will Charge commission. *(Gautam and Thapa, 2004 : 139)*

2.2.3 Characteristic of Rights

Studying about right offering the following characteristics of rights can be showed:

- The number of rights that a shareholder gets is equal to the number of shares held by him.
- The price per share, called the subscription price, is determined by the issuing company.
- The number of rights share required to subscribe additional shares is determined by the issuing company.
- Rights are negotiable. The holder of the rights can sell them.
- Right can be exercised only during a fixed period, which is usually about thirty days.

2.2.4 Advantages and Disadvantage of Right Issue

The main advantages of right issue. First, the existing shareholder's control is maintained through the pro-rata issues of the shares. This is significant in the case of closely held company or when a company is going into financial difficulties or is under takeover threat. Second, raising fund through the sale of rights issue rather than the public issue involves less flotation cost as the company can avoid underwriting commission. Third, in the case of profitable companies the issue is more likely to be successful since the subscription price is set much below the current market price. The main disadvantage is to the shareholder's who fail to exercise their rights. They lose in terms of decline in their wealth. Another disadvantage is for those companies whose shareholding is concentrated in the hands of financial institutions because of the conversion of loans into equity. They would prefer pubic issue. (*Pandey; 1999:1002)*

2.2.5 Mechanism of Right Offering

When a company makes a right offering, the board of directors must set a date of record, which is the last date on which the recipient of a right must be the legal owner indicated in the company's stock ledger. Due to the time needed to make bookkeeping entries when a stock is traded, stocks usually begin selling ex-rights without the right being attached to the stock four business days prior to the date of record. The issuing firm sends right to holders of the record-owner of the firm's share on the date of record, which is free to exercise their rights, sell them or let them expire. Rights are transferable and may be traded actively enough to be listed on the various security exchanges. They are exercisable for a specified period of time, generally not more than few months, at a price, called the subscription price, set some hoe below the prevailing market price. Since fractions of shares are not always issued, it is sometime necessary to purchase additional rights or sells extra rights. The value of a right depends largely on the number of rights needed to purchase a share of stock and the amount by which right subscription price is below the current market price. If the rights have a very low value and an individual owns only a small number of shares the rights may be allowed to expire *(Pandey, 1999:1002-1004).*

2.2.6 Significance of Right Issue

The issue of further share is resorted to for a various reasons. A company may, for the purpose of expansion, need additional capital resources. These may be over in the cost of the project and, therefore, additional shares may have to be raise funds. Financial Institutions grading loans may require the company to bring capital in desire proportion to the loan capital. Under the circumstances it is desirable to solicit additional capital for expansion from people who have a special interest in the welfare of the corporation, such as corporation's own stockholders and it also a least costly way of raising capital.

- To avoid external incontinent
- To expand company
- To achieve a more respectable size in the market
- To fulfill the legal requirement imposed by the authority
- To be successful on subscription
- To retain proportional ownership for shareholders
- To decrease flotation cost
- To increase the number of outstanding shares

2.2.7 Limitation of Right Issue

We discussed in the preceding section, the main advantages of right share issue is that it has favorable psychological value on shareholders. It indicates the company's growth to shareholders. Therefore they welcome right shares. But it has also limitations, without proper profit planning an issue of right share might invite over-capitalization. Some limitations are given below:

- "The company can't force its existing shareholders to buy any more shares in the company and hence it is granting them an option to buy these new shares" (Ward; 1995:107)
- Equally there is no reason for any outsider to want to buy these rights in order to take them up. Thus the proposed right issue could fail with the result that the company does not receive its desired injection of new equity funding.
- The shareholders who fail to receive to exercise to sell their rights. They lose in terms of decline in their wealth. Most right issues are underwritten because there is no legal obligation on the part of shareholders to subscribe.
- Issue of right share lowers than market value of existing share too. That may possess negative impact of particular share on capital market.

- It deprives new investor from becoming the shareholders of the company. The control over the management of the company is not diluted and the present management may misuse its position.
- The issue of right share dilutes the existing share's earnings per share if the profit do not increases immediately in proportion to the increase in the number of ordinary shares.

2.2.8 Under and Oversubscription of Right Offerings

A company can ensure the complete success of right offering by having investment banker or group of investment bankers "stand by" to underwrite the unsold portion of the issue. "Underwriting is the insurance function of bearing the risks of adverse price fluctuations during the period, in which, a new security is being distributed"(Weston & Copeland; 1992:891). Most rights offering are made through investment banker, who underwrite and issue the rights. In most underwriting agreements, the investment banker agrees to be a standby arrangement, which is a formal guarantee that any shares not subscribed or sold publicly will be purchased by the investment banker. This guarantee assures the firm that the entire issue will be sold it will not be undersubscribed. The investment banker, of course, charges a higher fee for making this guarantee. Most of right offerings include an oversubscription privilege, which gives stockholders not only the right to subscribe for their proportional shares of the total offering but also right to oversubscribe for any unsold shares. Although the use of the oversubscription increases the chances that the issue will be entirely sold, it does not assure this occurrence, as does the standby agreement. It is possible that the combination of subscriptions and oversubscription will fall short of the amount of the stock the company desire to sell. This privilege is a method of restricting ownership to the some group, although ownership proportions may change slightly. Shares that cannot be sold through the oversubscription privilege may be offered to the public. If an investment banker is used, the disposition of unsubscribed shares may be lest up to the banker.

2.3 Security Market and Common Stocks

A security market can be defined as a place for bringing together buyers and sellers of financial assets in order to facilitate trading. “A securities market can be defined as a place where people buy and sell financials instruments.” In other words, “An organized security market is a place where, or a system through which securities are created and transferred”.

Securities market can be divided into primary market and secondary market. A primary market is the place where corporations and government issue new securities. Primary market is the place for the original sale of securities by an issuer to the public. This is the market in which the government or corporation is directly taken part in the transaction and receives direct benefits from an issue. It is often referred to as initial public offerings. It involves new issues of securities for the first time. In other hand, secondary market is the market for existing shareholders. Secondary markets are those markets in which financial securities already outstanding are exchanged among investors. In this market, the trading between investors to investors takes place. The original issuer has no role in the secondary market and proceeds from securities transactions do not go to them. Nepal Stock Exchange (NEPSE) is an example of organized stock exchange which is the only one stock exchange in Nepal. The function of secondary market is to provide liquidity for securities purchased in the primary market.

A securities market can be classified into money market and capital market on the basis of the maturity of the securities traded in. Money market deals with the trading of securities with less than one year of maturity. It is created for borrowing and lending for relatively short-term funds. Money market instruments include commercial papers, bankers’ acceptance, certificate of deposits, promissory notes, bills of exchange, Treasury bill etc. On the other hand, capital market deals with the securities having more than one year of maturity. All long-term securities issued by corporations and government such as common stock, preferred stock, corporate bonds, government bonds etc are the instruments of the capital market. These capital market instruments can be traded in both primary as well as secondary markets.

Security is a claim against real resources either in the form of an income stream or in the form of physical capital or assets. This means security is a piece of paper which serves as evidence of rights. It can be transferred from one investor to another through which rights and conditions are transferred. In other words, it is a legal representation of right to receive future benefits under stated conditions. There are different kinds of securities such as debentures, common stocks, preferred stocks, treasury bills etc. But among them, common stock is being popular. Now days, common stockholders are the real owners of the company. They have rights and privileges like voting and preemptive rights. As owners, they do not get priority in the distribution of assets resulting from a liquidation of the corporation. From this view, common stockholders have to bear risk than bonds and preferred stockholders.

There are three terms which are associated with the common stocks. They are par value, book value and market value. Par value is also known as face value of the common stocks. Par value is the value established at the time of initial issuance. On the other hand, book value means the asset value after deducting liabilities and preferred stock. Market value of common stock is the value determined by the supply and demand factors.

2.4 Efficient Market Theories and Information

An efficient market is defined as the market in which the prices of securities fully reflect all known information quickly and accurately. Its concept assumes that all known information is reflected in the price, including not only past information but also current information as well as events that have been announced but have not yet transpired. The word “Efficiency” as applied to securities market has unfortunately been used to represent a variety of logically distinct concepts. Efficiency can be particularly classified into (a) exchange efficiency, (b) production efficiency and (c) information efficiency. In an efficient market, the prices of securities fully reflect available information. Regardless of the form of information, it is the key to the determination of stock prices. Therefore, it is the central issue of the efficient market concept. An efficient market can exist if the following events occur:

1. A large numbers of rational profit maximizing investors exist who actively participate in the market by analyzing, valuing and trading stocks. These investors are price takers; that is one participant alone can not affect the price of a security.
2. All investors obtain information without cost and have access to information at approximately the same time.
3. Information is generated in a random fashion such that announcements are basically independent of one another.
4. Investors react quickly and accurately to the new information, causing stock prices to adjust accordingly.
5. Furthermore, this concept states that prices changes due to information are independent of one another and move in a random fashion. The piece change occurring today is independent of the one yesterday because it is based on investors' reaction to new independent information coming into the market today.

According to Professor Eugene Fama, there are three hypothesizes of market efficiency. They are explained as follows:

I. Weakly Efficient Market Hypothesis

Weakly efficient market hypothesizes that today's security prices fully reflect all information contained in historical security prices. This implies that no investor can earn excess return by developing trading rules based on historical price or return information. "The market is efficient in the weak sense if share prices fully reflect the information implied by all prior price movements. Price movements in effects are totally independent of previous movements implying the absence of any price patterns with prophetic significance”. So the past prices have no meaningful information to predict future course of price fluctuations which can be used to earn above average return. Furthermore, this hypothesis stipulates that the price of the stocks have absorbed only the stock market information but not the public information. The implication of this hypothesis is that knowing and using the past sequence of price information is of no value to an investor. (*Kean, 1983:120)*

II. Semi Strong Efficient Market Hypothesis

This hypothesis says that market is efficient enough for prices to reflect all publicly available information. Thus, no investor could earn excess return using publicly available resources such as corporate annual reports, NEPSE price information or published investment advisory reports. All publicly available data are earnings, stock splits announcements and dividends, financing difficulties, new products developments and accounting changes. This hypothesis also states that current prices of the stock reflect not only stock market information but also publicly known and available data. A market that quickly incorporates all such information into prices is said to be Semi Strong Efficient. “If the semi strong hypothesis is true, then only a few than what could be earned by using a naïve buy-and-hold strategy.

III. Strong Efficient Market Hypothesis

Strong efficient market hypothesis states that stock prices fully reflect all information; public and non public. This means that no group of investors can excess return through a superior capacity to analyze publicly available information. In other words, if investors transform public information into private information, they do not gain by doing so. “An extreme version of the strong form holds that all non public information, including information that may be restricted to certain groups such as corporate insiders and specialists on the exchanges is immediately reflected in prices. In effect, this hypothesis asserts that stock prices fully reflect all public and non public information and there by no investor can earn abnormal returns.

2.5 Historical Development of Capital Market in Nepal: A Brief Review

Capital market of Nepal has neither a long history nor is very complex. The history of Nepalese capital market dates back to the era of Rana Prime Minister Juddha Samsher. Though the history of capital market dates back to Rana dynasty, it is not still properly developed. The industrial revolution took place in Nepal after the establishment of Biratnagar Jute Mill in 1936 A.D., as the first modern industry in the country. After that, various mills of rice, cotton, sugar and other were established to mobilize the capital for the industrial development. In 1937, Nepal Bank Limited as a commercial bank was established for promoting banking and industrial sector. In the same year, the first industrial act was promulgated which was a favorable step in the history of Nepalese capital market. The history of securities market began with the flotation of shares by Biratnagar Jute Mill, incorporate under Company Act 1936 and Nepal Bank Limited, incorporated under Nepal Bank Act 1937. Introduction of Company Act in 1964 and the first issuance of government bonds in the same year were also other significant developments relating to capital markets. Only few companies had issued their shares to the public before operation of company act. Government was the sole issuing authority when there was absence of developed security market. However, the formal institutionalization began only after the establishment of Security Market Center (SMC) in 1976 under the company act as a joint effort of Nepal Rastra Bank (NRB) and Nepal Industrial Development Corporation (NIDC). This center was established with an objective of facilitating and promoting the growth of capital markets. Before conversion into the security exchange, it was the only capital market institution undertaking the job of brokering, underwriting, managing public issue, market making for government bonds, and other financial services. However, securities trading were insignificant because of absence of private brokers, dealers and investment banks or securities firms.

The Securities Exchange Act was promulgated in 1983 and provision of listing the securities was included in the act. With the promulgation of Securities Exchange Act, SMC was then converted into Securities Exchange Center (SEC) in 13 April, 1984. SEC was established with an objective of facilitating and promoting the growth of capital market. Later, Securities Exchange Act was amended in 1993 in the period of Eight plan for the achievement of the plan objectives of developing capital market. The development process accelerated with the liberalization policy of the government during 1990s. During this period, major initiatives were taken for the development of the securities market, the most important one being establishment of Securities Board of Nepal (SEBON) in 1993 as an apex regulator of securities market. With the establishment of SEBON, Securities Exchange Center (SEC) was converted into Nepal Stock Exchange Ltd. (NEPSE) which is a non-profit organization, operating under Securities Exchange Act, 1983. From that point, NEPSE became responsible for the operation of the market for listed securities and the performance of some self regulatory functions.

Recently, many initiatives were taken for the development of securities market. NEPSE had adopted Automation System in trading floor replacing “Open Out-Cry” system, a system where transactions of securities were conducted on the open auction principle on the trading floor. Similarly, NEPSE granted permission to some brokers for online trading from their premises also. The process of providing license to 27 new stock brokers is also in the pipe-line. Trading hours are also increased to 3 hours from 2 hours in a day and the rate of brokerage commission was also reduced to encourage the investors to participate actively in securities market. Similarly, the practice of circuit-breaker and trading halt to control the undue ups and downs of security prices, opening of trading floor for promoters’ share, etc. are some of the major initiatives taken to develop the security market. As a result one million people are engaged actively in Nepal's share market. Due to increase in the number of daily newspapers and their coverage of share market news, share transactions have gained public attention. Television broadcasting of share prices, talk programmes, interviews and FM radio programmes on stock market have immensely popularized this sector and the general people have noticed the boom effects of share market. *(Joshi, 2003 : 142)*

2.6 Establishment of Nepal Stock Exchange (NEPSE)

2.6.1 Introduction

Nepal Stock Exchange Limited (NEPSE) is the only one organized stock market in Nepal facilitating the trading of corporate securities mainly common stock, which opened its trading floor in 1994. prior to the establishment of NEPSE, secondary market was operated over the counter facility managed by Security Exchange Center (SEC). The Nepalese security market is growing at a slow rate as it has to overcome various obstacles that it has to face due to lack of proper development of market. In the field of securities market, Nepal Rastra Bank (NRB) and Nepal Industrial Development Corporation (NIDC) had made a joint effort to establish Security Market Center (SMC) in 1976 for the development of securities market. The main objective behind the establishment of this center was to mobilize public saving for ensuring public ownership in the shares of public limited companies and to encourage people to participate in business activities. Thus SMC was responsible for undertaking the job of brokering, underwriting, managing public issue, market making for government bonds and other securities market services. In order to promote the stock exchange business, SMC made a series of studies in the beginning both public limited companies and devising the ways and means of understanding the business of buying and selling in securities. In pragmatic reality, however, the center become nothing more than the satellite organization of NRB to undertake the over burdened functions of the later in selling government securities that comprise treasury bills, development bonds, etc. After a long period of seven years, doing nothing substantial in the frontiers of stock exchange business, the Security Market Center (SMC) passed a new Securities Exchange Act in 1983 to revitalize its role in the capacity of a merchant banker in view of acting as a legally acknowledged some stock exchange house. After 1980s onward, the center tried to create some securities exchange norms. But all it became not encouraging to develop the securities exchange business in view of lack of dashing leadership since the level of understanding about the pros and cons of stock exchange was relatively poor. The enactment of new Securities Exchange Act in 1983 became landmark in the Nepalese history of stock exchange and this brought change in nomenclature to the extent that the title of the center changed to Securities Exchange Center(SEC) in 13 April, 1984. Securities Exchange Center (SEC) was established with an objective of facilitating and promoting the growth of capital markets. As it was only one institution in the field of capital market, SEC was responsible to undertake the job of brokering, underwriting, managing public issue, market marking for government bonds and other financial services. Later in 1993 in the period of Eighth plan, Securities Exchange Act was amended for the achievement of the plan objectives of developing capital market.

Only then after, the development process of Nepalese capital market accelerated with the liberalization policy of the government. In 1993, the government, under a program initiated to reform capital markets, converted the Securities Exchange Center (SEC) into Nepal Stock Exchange Ltd. (NEPSE). NEPSE, 99 percent owned by the government, NRB and NIDC, is a non-profit organization, operating under Securities Exchange Act 1983. From that point, NEPSE became responsible for the operation of the market for listed securities and the performance of some self-regulatory functions under the supervision of the newly created Securities Board of Nepal (SEBON).

NEPSE opened its trading floor on 13th January, 1994 adopting “Open Out-Cry” system of trading through its licensed members. Nepal government, NRB, NIDC and licensed members are the shareholders of the NEPSE. The basic objective of NEPSE is to impart free marketability and liquidity to government and corporate securities by facilitating transactions in its trading floor through members and market intermediaries such as brokers, market makers, etc. A huge number of securities of existing financial, manufacturing, banking, service and production entities are traded in NEPSE. Only the securities of existing companies are traded there whose securities are listed in NEPSE. In comparison to other stock market of the world, we have nothing countable achievements in the case of secondary market. However, what the Nepalese stock market did in almost two decades of its establishment is considered a watershed in the history of the securities market of Nepal. Nevertheless, some historic initiatives took place in recent years.

NEPSE has adopted Automation System in its trading floor replacing “Open Out-cry” system and some of the stock brokers are also given permission for online trading from their own premises. It is also in the process of increasing the number of stock brokers and it has already increased the daily trading hours to 3 hours in a day. Over –The –Counter (OTC) market has also started its operation here the securities of de-listed companies and non-listed companies can be traded. Similarly, the practice of circuit-breaker and trading halt are introduced in stock transactions to control the unexpected fluctuations of stock prices. The number of listed companies in NEPSE reached 176 and the market capitalization has also increased amounting Rs. 377 billion at the end of fiscal year 2009/10. The total amount of securities traded in the fiscal year also increased and stood at Rs. 11.86 billion.

2.6.2 Board of Directors of NEPSE

The board of directors of NEPSE consists of nine directors in accordance with Securities Exchange Act, 1983. Six directors are nominated by Government of Nepal and different institutional investors. Two from the licensed members and the last one is general manager of NEPSE who is the Ex-Offcio Director of the Board.

Table 2.1

Board of Directors of NEPSE

S. N.	Name of organization	No. of Directors	Designation
1	Ministry of Finance	1	Chairman
2	Security Board	2	Director
3	Nepal Rastra Bank	2	Director
4	Nepal Industrial Development Corporation	1	Director
5	Licensed Members	2	Director
6	General Manager	1	Director

(Source: NEPSE Annual report 2066/67)

2.6.3 Capital Structure of NEPSE

The authorized and issued capital of the exchanged is Rs 50 million. Of this Rs 30.41 millions is subscribed by Nepal government, Nepal Rastra Bank, Nepal Industrial Development Corporation and Licensed Members.

Table 2.2

Capital Structure of NEPSE

S. N.	Shareholders	Rs in million	Percentage (%)
1	Nepal Government	20.48	58.67
2	NRB	12.08	34.60
3	NIDC	2.14	6.13
4	MEMBERS	0.21	0.60
	Total	**34.91**	**100**

(Source: NEPSE Annual report 2066/67)

2.6.4 Trading Arrangements in NEPSE

I. Trading System of NEPSE

NEPSE has adopted an "Open Out-Cry System". It means transactions of securities are conducted on the open action principle on trading floor. The buying broker with the highest bid will post the price and his code number on the buying columns while selling broker with the lowest offer will post the price and his code number on the selling column on the quotation board. The market quotes their bid and offer price match contracts between the buying and the selling brokers or between the brokers and market makers that are concluded on their floor.

II. Trading Days and Hours of NEPSE

NEPSE has fixed the trading days and hours during which the brokers are allowed to enter the floor to make the transactions.

Table 2.3

Trading Days and Hours of NEPSE

Types of Trading	Days	Trading Time
Regular trading	Sunday to Thursday	12 Noon to 1 pm
Odd trading	Monday	2 pm to 3 pm
Odd trading	Friday	11am to 12 Noon

(Source: NEPSE Annual report 2066/67)

III. Ordering Lots in NEPSE

Trading lots of securities listed in the NEPSE are fixed on the basis of the face value of securities. If the listed securities are shares or other than shares in this case the board lot is fixed on the basis of the face value of the securities. If the face value of the securities is Rs 10, the minimum number of shares that is to be traded is 100. In the same way, if the face value of the shares is Rs 100, then it is 10. The securities other than shares, having the face value of the Rs 1000 must be traded in number of one and in multiples of the same. If the listed securities are debentures or bonds, the minimum tradable lot is fixed on the basis of face value of the securities. If the face value is Rs 100, the tradable lot is 100 and if it is Rs 1000, the tradable lot is 10. In the both cases any number of securities more than started above can be traded. It is to be notified than no securities can be traded in fraction. The transaction of regular trading should be on at least lot. The transactions of less than 10 shares are admitted by an odd lot trading hours. There is no odd lot transaction in case of debenture.

IV. Price Regulation

The percentage for the fixation of an opening price has been reduced from 10% to 5% since the fiscal years 2003/04. It means the opening price of any day shall not be more or less than 5% of the previous trading day's closing price. Once the transactions are done with in this range, the price can be changed with in a limit of 2% in each consecutive transaction.

V. Settlement

NEPSE adopted a T+5 system. The existing system of settlement has been changed from T+5 to T+3. The changed system has been implemented since 17 July 2003. Under the prevailing system the transactions done on the trading floor need to be settled within 3 working days excluding the transaction date. Settlement will be carried out on the paper- versus- payment basis.

VI. Brokerage Commission

The rate of brokerage commission on equity transactions ranges from 1% to 1.5% depending on the traded amount. The rate of brokerage commission on debenture ranges from 0.15% to 0.75%. As per the rules, the rate of brokerage commission is listed below:

Table 2.4

Commission on Shares Transactions

Traded Amount	Rate of Commission
Up to Rs 25000	1.5%
Rs 25001 to Rs 50000	1.4%
Rs 50001 to Rs 100000	1.3%
Rs 100001 to Rs 500000	1.2%
Rs 500001 to Rs 1000000	1.1%
Above Rs 1000000	1.0%

(Source: NEPSE Annual report 2066/67)

Table 2.5

Commission on Corporate Bond Transactions

Traded Amount	Rate of Commission
Up to Rs 100000	0.75%
Rs 100001 to Rs 500000	0.60%
Rs 500001 to Rs 1000000	0.45%
Rs 1000001 to Rs 5000000	0.30%
Above Rs 5000000	0.15%

(Source: NEPSE Annual report 2066/67)

2.6.5 Listing Fees of NEPSE

The listing fees and the annual fees to be paid by the listed companies are based on the capital of the company. The rates currently applications are as follows:

Table 2.6

Listing Fees of NEPSE

Paid up to capital	Fees (Listing)	Fees (Annual)
Up to Rs 10 million	0.20% or minimum Rs 15000	Rs 15000
Above Rs 10 million to Rs 50 million	0.15% or minimum Rs 45000	Rs 25000
Above Rs 50 million to Rs 100 million	0.10% or minimum Rs 75000	Rs 35000
Above Rs 100 million	0.075% or minimum Rs 100000	Rs 50000

(Source: NEPSE Annual report 2066/67)

2.7 Securities Board of Nepal (SEBON)

Securities Board of Nepal (SEBON) was established on June 7, 1993 as an apex regulator of securities market in Nepal. It was established under the provision of Securities Exchange Act 1983 (first amendment) with the objective to promote and protect the interest of investors by regulating the securities market and its working transparent. It was also responsible for the development of the securities market in the country. Since its establishment, SEBON has been concentrating its efforts on improving the legal and statutory frameworks which are the bases for the healthy development of the capital market. As a part of its continuous efforts to build a sound system, the Securities Exchange Act 1983 was amended for the second time on Jan 30, 1997. This amendment made mandatory for all capital market intermediaries to be registered with SEBON before undertaking securities business and to report their financial and trading activities to it. This amendment also paved the way for establishing SEBON as an apex regulatory body as it widened the horizon of SEBON by bringing market intermediaries directly under its jurisdiction and also made it mandatory for the listed companies to submit their annual and semi-annual progress reports to SEBON. Moreover banking and financial institutions have to submit their quarterly progress reports.

Besides, SEBON was also made responsible for the development of security market in Nepal by promoting the interest of the investors by regulating the issuance, sale and distribution of securities and purchase, sale or exchange of securities. It is made an apex organization with effective regulatory unit in 1997 with a responsibility of regulating and supervising market intermediaries involved in the primary issues as well as in the secondary transaction of securities. Thus, SEBON has an important role of developing the capital market by making securities transaction fair, healthy, efficient and responsible. The role of SEBON is rigorously increasing in the field of securities market as the securities market has shown its dynamism with the rising number of companies floating shares, increase in the number of listed companies, 30 significant increase in market capitalization and market index, and percent of turnover on market capitalization.

2.7.1 General Objectives of Securities Board of Nepal (SEBON)

General Objectives of Securities Board of Nepal (SEBON) are as follows:

- To promote and protect the interest of the investors by regulating the issuance, sale and distribution of securities and purchase, sale or exchange of securities.
- To supervise, look after and monitor the activities of stock exchange and corporate bodies carrying on securities business.
- To render contribution to the development of capital market by making securities transaction fair, healthy, efficient and responsible.

2.7.2 Functions, Duties and Power of SEBON

As per the Securities Related Act, 2006, t5eh major functions, duties and power of Securities Board of Nepal (SEBON) are as follows:

- Register securities and approve prospectus of public companies.
- Provide license to operate stock exchanges.
- Provide license to operate securities business.

- Permit the operation of collective investment schemes and investment fund program.
- Draft regulations, issue directives and guidelines, and approve bylaws of stock exchanges.
- Supervise and monitor stock exchanges and securities business activities.
- Take enforcement measures to ensure market integrity.
- Review reporting of issuer and listing companies and securities businesspersons.
- Conduct research, study and awareness programs regarding securities markets.
- Coordinate and cooperate with other domestic as well as international securities related regulatory agencies.
- Formulate policies and programs relating to securities markets and advise the Government of Nepal as and when required.

2.8 Initial Financing

2.8.1 Venture Capital

When a company is formed, it obviously must be financed. Often seed money comes from the founder and their friends and families. For some companies, this is sufficient to get things launched but for others, additional external equity are necessary. There are two ways in which additional equity can be managed and they are venture capital and initial public offering. Venture capital (VC) represents fund invested in an existing, relatively new enterprises. Wealthy investors and financial institutions are the major sources of venture capital but there are several sources as well. A venture capital firm will seek capital in advance from external investor. Such investors include insurance companies, public pension funds, endowments and foundations, bank holding companies, individuals and others. "One reason that new companies find venture capital firms attractive in that a venture capitalist typically view their investment as long-term and are willing to wait several years before repaying their return" *(Rao, 1982:542).*

It is another way financing a business. Venture capitalists invest in new or young firms in return for equity in the firm. They are not lenders but they are equity investors at a stage at which the firm's shares do not yet trade on public market. Unlike most equity investors, venture capitalists typically play an active role in selecting management and overseeing strategy. They normally seek to sell their shares within a few years, usually by taking the firm public and selling their shares on the public equity markets. Venture capital is a well-established form of financing in the many countries.

2.8.2 Initial Public Offering (IPOs)

A closely held firm can raise fund through initial public offering. If a new firm is growing, usually the owners will want to take the company public with a sale of common stock to outsiders. This procedures and alternatives for raising funds is called going public. "Going public means selling some of a company's stock to outside investors and then letting the stock trade in public market, and desire to convert into corporations" *(Brigham, Gapenski & Ehrhardt, 2001:698)* . In other words, whenever stock in a closely held company is offered to the public for the first time, the company is said to be going public. The market for the stock which is just being offered to the public is called the initial public offering (IPO) market.

Public offering of various securities for raising funds by both government and corporations to the general public are made through the investment bankers. Investment banker acts as a middleman who brings together suppliers and users of long-term funds in Capital market. The major function of investment banker is to buy the securities from the issuing company and then resell them to investors at a high price. This difference in the purchasing price and selling price is called 'spread' or commission to the investment banker. Thus public offering involves rising of funds for government or corporations from public through the issuance of various securities in the primary market and is often the only major sources of obtaining large sums of long-term funds. There are substantial one time costs related with IPOs that may be either direct or indirect costs. Direct costs are legal, administrative, underwriting fees, auditing and the dilution related with selling shares of an offering price.

The company can issue new shares to raise funds through one of the following ways:

i. Through investment bankers to the general public in a public offering.
ii. On a pro-rata basis to existing shareholders through a right offering.
iii. Through a dividend reinvestment plan.
iv. To employee through employee stock purchase plan.
v. To single buyer (or very small number of buyers) in private placement.

When a firm goes public, the various changes arise with the firms, which are described below:

i. The firm is being systematically controlled and formal after going public. The financial techniques like ratio analysis and Dupont sys tem of financial planning and control are needed for the system control.
ii. The outside investors should get information on time after going public though the founders may continue to have majority control.
iii. The publicly owned typically draws on a board of directors which should include representatives of the public owners and other external interest group to held ultimate sound plans and policies.
iv. The firm must have breadth of management in all business effectively.

A number of securities are issued in the new issue market which is a primary market for raising funds. A number of securities include equity shares, preference shares, debentures, warrants, convertible securities, zero coupon bond & convertible and cumulative convertible preference shares.

2.9 Right Offering: A Theoretical Framework

When a company needs additional funds for a long-term purpose, it can raise the fund by issuing common stocks at a subscribed price on a pro-rata basis to existing shareholders instead of selling common stocks to new investors. This method of issuance is called Right Offering. Right offering is very much popular in Nepalese capital market and it is also known as privileged subscription. The existing shareholders have right to purchase certain number of new shares at subscribed price on pro-rata basis. The existing shareholders receive one right for each share of stock they hold, so this type of issuance of shares is known as right offering. They have an option to buy new shares at subscription price by using rights and terms of the option are contained on a piece of paper called a right. A specified number of rights are required to purchase the new shares. The companies are allowed to issue right share provided the shares already issued are fully paid who have already issued shares to the public. The companies can issue right shares to the existing shareholders under the principle of pre-emptive right. Right offering helps to reduce flotation costs. It also protects the existing shareholders from dilution in wealth and control power.

2.9.1 Pre-emptive Right

In simply, preemptive right is the right to do something before others. The common stockholders are the real owner of the company so that they have certain right which is called Preemptive Right. In this right, the existing stockholders have right to purchase any additional shares issued by the company before they are offered to public. If the firm's charter contains preemptive right, then the firm must offer any new common stock to existing shareholders. If the preemptive right is not contained by the firm's charter, then there is no compulsory to issue new common stocks to the existing shareholders. The company has choice of making the sale of the existing stockholders or to an entirely new set of investors. If it sells to the existing shareholders, this issue is called right offering.

“Common stock holders often have the right, called the pre-emptive right, to purchase any additional share sold by the firm. In some states the pre-emptive is automatically included in every corporate charter, in other it is necessary” *(Weston & Brigham, 1990:677).* The existing shareholders have right to purchase new additional shares under the preemptive right so that they can preserve their proportionate ownership in the company. They can purchase new shares of the stock at subscription price on pro-rata basis. For example- if one of the existing shareholders has 1000 shares of the company which declared 10:1 right shares issue, then he can purchase 100 additional shares of the company. In this way, he can preserve his proportionate ownership in the company. Under the preemptive right, the existing shareholders have option to buy new common stocks. If the company sells the new shares to the existing shareholders, it is called right offering. “Each shareholder is issued an option to buy a certain number of new shares, and the terms of the option are listed on a certificate called a stock purchase right, or simply a right. If a stockholder does not wish to purchase any additional shares, then he or she can sell the rights to some other person who wants to buy the stock” *(Brigham, Gapenski & Ehrhardt, 1988:607).* In many countries ‘Right’ is a negotiable instrument and therefore transferable. And it must be logically transferable and negotiable because while someone may have sufficient money to exercise the rights and they may actually exercise such rights but some others may not have the sufficient money to exercise all the rights, so they can exercise the rights partially. That means some rights are exercised and some might be sold.

“Right are important tool of common stock financing without which, stockholders would run the risk of losing their proportionate control of the corporation” *(Gitman, 1988:607).* The purpose of preemptive right is to protect the control power of present stockholders. It also protects the stockholders against a dilution of value of the stocks. For example- suppose 1000 shares of common stock each with a price of Rs. 32, were outstanding making the total market value of the firm Rs. 32000. If additional 1000 shares were sold to new investors at Rs. 20 per share or for Rs. 20000, this would raise the total market value is divided by the new total shares outstanding a value of Rs 22 per share is obtained. The old shareholders thus lose Rs 10 per share and the new stockholders will get Rs 10 profit per share. Thus selling common stocks at a price below the market value would dilute the value of stock of present stockholders. Similarly, new stockholders get benefit because of this issuance. Thus preemptive right prevents such occurrence

As the preemptive right states that the existing shareholders get first chance to buy newly issued common stocks as well as new issued securities convertible into common stock. The existing shareholders can purchase certain number of shares which is determined the number of old shares in relation to the total shares outstanding. One share means one share. The company declares how many rights are required to purchase one new share by the existing shareholders. For example- if Mr. X owned 5 shares in ABC company which declared 3:1 right share issue. Then Mr. X can purchase 1 new share of the company through right offering.

2.9.2 Reason of Right Offering in the Context of Nepalese Stock Market

The offering of additional shares to the existing shareholders through right is known as right offering. The company offers to buy new shares of common stocks to the existing shareholders. Right issue is a privileged given to the existing shareholders that helps them to keep their control position proportionately equal and the issuing price will also be lesser than the market price. When the company issues securities by privileged subscription, it mails to shareholders one right for share of the stock held. The existing shareholders can purchase additional new shares according to the term & condition of right offering. The subscription price per share, the expiration date of the offering and the number of rights required to purchase one new share of the stock are specified by the term & condition of the right offering. Generally subscription price will be lower than market price of the stock. So it will help to maximize the capital gain of the shareholders. The exiting shareholders have three choices which are (I) exercise the right, (II) sell the right and (III) let the right expire. The stockholders exercise the right to purchase additional new shares of the stock at subscription price on pro-rata basis because the subscription price is generally less than the current market price and they may have sufficient money. Similarly, in second case, the existing shareholders sell the rights partially, if they have not sufficient money to purchase new shares. Similarly, some people may have the money but for them the right share may not be so profitable option in comparison to other options available. So they have right to sell the right. Likewise, somebody may not have the money to exercise the right, so they can sell all the rights. If the shareholders have not sufficient rights to purchase one new share or the value of the rights is negotiable then only they let the rights to expire. That means they do not exercise the rights. Generally the subscription period is about three weeks.

Nepal Rastra Bank is the central bank of Nepalese banks. So it imposes legal requirement for increment of the equity base at certain standard level. To fulfill the legal requirements, right share issue is one of the popular practice for raising the additional capital funds and it is enthusiastically increased because it minimize the flotation cost, lower the cost of funds and avoids the difficulties in raising funds through public offering. Now a day, the issuing of right shares is being popular and right shares are issued by the company which is formed by the combination of certain number of banks and finance companies because only one finance company or the bank can not fulfill the legal requirements which is imposed by the Nepal Rastra Bank.

The reason of the issuing right shares by the company is to raise the additional capital fund. Right is an option of the existing shareholders to purchase the certain number of new shares at subscription price during a given period of time. So right share is an opportunity to the existing shareholders given by the company. The company issue the right shares to raise additional needed fund which contains; (I) the number of rights required to purchase one new share, (II) the theoretical value of right and (III) the effect of right issuing on the value of ordinary shares. Rights can be exercised at a subscription price which is generally below than the current market price. If the stockholders are the stockiest want to hold control power on the management of the company by electing as a director and if the value of the right is higher, then rights are exercised. If the shareholders exercise the rights, then right offering can not hamper on the shareholders' wealth. Rights can be either exercised or sold on the stock market. But the wealth of the shareholders will be reduced if they neither exercise nor sell the rights. Some of the shareholders own few numbers of shares and they feel that it does not matter to them about the changes of the management. Because of this type of nature, their wealth will be reduced. Right has expiration date, so shareholders have to purchase before expiration date otherwise their rights will be expired ca not purchase new shares. There are some irrational investors or shareholders who neither nor sell the rights. As a result, they will get their wealth reduced. So the company normally must be sure that the rights will be exercised without fearing any adverse wealth implications for its existing shareholders. Because of this reason, the company fixes the subscription price which is much below than the current market price. *(NEPSE)*

I. Significance of Right Offering

The company has various reasons to issue the further new shares i.e. right issue and that may be for need of additional capital funds, the expansion of the company etc. it is least costly way to raise capital funds. So it has many significances which are described below:

- **Minimization of Flotation Cost**

One of the important advantages of right offering is the minimization of flotation cost. The flotation cost of right offering will be lower than the flotation cost of public offering. The adjusted or the downward price pressure may be avoided through right offering.

- **Retention of Proportional Ownership for Shareholders**

Another significance of right offering is that the existing shareholders can maintain their ownership proportion. This means if the company issues new shares to new investors and the existing shareholders may not have sufficient funds to purchase new shares, then their ownership proportion will decline. So right offering is the way to maintain ownership proportion by the existing shareholders. But there is no obligation to purchase new additional shares by the existing shareholders through right offering.

- **Achievement of fully Subscribed of Right Issue**

Generally subscription price is lower than the current market price of the stock. And the company sets such price of the stock because of the rational investors. This means if the company sets the subscription price higher than the current market price, then the rational investors would prefer to purchase shares in the market rather than the expensive new shares of the company. Because of this reason, the subscription price must be set in such a way that is lower than the current market price and the issue is more likely to be successful.

- **Increment in the Number of Outstanding Shares**

The number of outstanding shares is increased by the issue of right shares. This increment in the number of shares promotes the active trading in the stock market. If a large amount of funds is required to trade the stock, then small investors may be unable to trade minimum unit of stocks. They are unable to trade because of the holding additional number of shares and reduction in share price which diversify in their portfolios.

- **Being Permanent Capital**

Ordinary shares or the right shares both are irredeemable. So the company gets a permanent capital funds. Because of the irredeemable nature of right shares, the company has no liability for cash outflow.

- **Expansion of the Company**

For the purpose of expanding the company, additional fund is required to finance the expansion. So the right share is issued to expand the company.

- **Indication of Higher Profit**

Right share is declared by the board of directors and whose expectation is rising in earnings of offset the additional shares. So it is an indication of higher future profit.

- **For bringing the Market Price of Share within more Popular Range**

The effect of right shares is to decrease in share price and to increase in the number of outstanding shares. If the performance of a share is strong which leads to increase in market value than popular range, then the determination of the company's management is that the price of the share will be higher than (moving and of) the popular trading range and the company will be sure that the price of the shares becomes high within the popular range. If it happens the smaller investor can also be able to involve in trading and also can make a large number of different stock in their portfolios.

- **Getting Positive Psychological Value by the Shareholders**

The company has brought prospects with growing earning and the announcement of right offering is taken as favorable news by the investors. They can take part in this offering for increment in future dividends. If the investors accepts right offering, the company gets cash to invest for profitable investment opportunities and which indicates the positive psychological value of the investors or the shareholders. The price of the stock may be actually rise after certain time period instead of decrement in value of share after right issue. The stockholders can protect their value of the shares and control position of the company through preemptive right.

- **Achievement of a more Respective size in the Capital Market**

Every shareholders get additional share on pro-rata basis after the right offering by the company. And some of the new shares are sold by old shareholders which indicates that the achievement of the company as a more respectable size in the capital market.

- **Fulfillment of The Legal Requirement Imposed by the Authority**

Nepal Rastra Bank is the central bank of Nepalese banks. So it imposes legal requirement for increment of the equity base at certain standard level. To fulfill the legal requirements, right share issue is one of the popular practice for raising the additional capital funds and it is enthusiastically increased because it minimize the flotation cost, lower the cost of funds and avoids the difficulties in raising funds through public offering.

I.Limitations of Right Offering

There are many advantages of right offering like it indicates the company's growth to shareholders and it has favorable psychological value on shareholders which is the main advantage. But inspite of all advantages, it has also some limitations which are described below:

- The existing shareholders have an option to purchase new shares but the company can't force them, which is the drawback of right offering
- The shareholders who neither exercise nor sell their rights, their wealth position will be decreased. There is no obligation about the subscription by the shareholders, so most of the right issues are underwritten.
- The market value of the existing shares is also decreased after the right share issue which may posses negative impact of particular share on the capital market.

- There is no reason for outside investors who want to buy rights to take them up. So, the proposed right issue could be fail if the company does not get its desired injection of new equity funding.
- "Yet another disadvantage is for those companies whose shareholding is concentrated in the hand of financial instructions because of the conversion of loan into equity. They would prefer public of share rather then right issue" *(Pandey, 1999:1006).*
- If the profit does not increase immediately in proportion to the increment of the number of ordinary shares, then the earning per share of the existing share will be diluted because of right share issue.
- The control position of the management remains same because of this, the right issues depresses the new investors from being the shareholders of the company. And the current management may misuse its control power.

2.10 Right Offering Vs Public Offering

Right offering and public offering both are the issue of common stocks. But right offering is issued for the existing shareholders and public offering is issued for new investors. However, there are some differences exist between these offerings which are described below:

1. A right issue is likely to be more successful than public offering because the right offering is made to the investors who are familiar with the operations of the company.
2. Right issue is not underwritten, so flotation cost of right issue is lower than public offering.
3. A right issue has issue price lower than the public offering.
4. The principal sales tool in the right offering is the discount from the current market price, whereas with the public offering, the major selling tool is the investment banking organization.

2.11 Market Vs Theoretical Value of Right

Immediately after the announcement of the right offering, the market price of the stock would increase by some amount but theoretically it is said that the right offering does not affect the value of the shareholders. So we should be aware that the actual value of a right may differ somewhat from theoretical value because of irregular exercise, sale of right over the subscription period, transaction cost and speculation. However, arbitrage limits the deviation of actual value from the theoretical value. If the price of right is significantly lower than its theoretical value, the arbitragers will buy the rights and exercise to purchase new stocks, and downward pressure on the theoretical value of the right. If the price of right is significantly higher than its theoretical value, shareholders will sell the rights and buy the stocks in the market. Such action will avert downward pressure on the market price of the right and upload pressure on the market price of the stock. These arbitrage actions will contribute as long as they are profitable. The market price of the right is generally different from the theoretical value of right. The difference between market as well as theoretical value of right is depended upon how the firm's price is expected to behave during the period when the right is exercisable. The investors can get much higher returns when stock price is raised if they buy rights instead of the stocks itself.

2.12 Procedural Aspects of Right Offering

A right issue is the selling of the ordinary shares to existing shareholders of the company. The new shares must be issued to the existing shareholders on pro-rata basis. When the stocks traded in the capital market during announcing period, then the investors (buyers and sellers of the stocks) may get problem, who will get the right? To avoid this confusion, the board of directors of the company fixed record date to give certainty about the possession of right. This record date is the last date on which the recipient of a right must be legal owner indicated in the company stock ledger. Ex-right date is the date on and after which the right no longer goes to the stock. Ex-right date is the book closer date on which and after which bookkeeping entries will not be done. Ex-right date is normally four days before the holder of record date. The issuing firm sends rights to holders of record owners of the firm share on the date of record, who are free to exercise their rights, sell them or let them expire. Rights are transferable, so they must be exercised within specify period of time which is generally not more than few months at the subscription price. The company also declares that how many numbers of rights are required to purchase one new share and there is not possible about the trading of fractions of shares. So the existing shareholders may purchase the additional rights or sell the extra rights. The value of right depends largely on the number of rights required to purchase one new share of the stock and the amount by which the right's subscription price is below than the current market price. If the value of right is high, the rights will be exercised but if the value of the right is low and the small investors have less number of shares, then the rights are not exercised. For example - if the XYZ Company needs Rs 400 million funds and the board of directors (BOD) decided to raise the funds through right offerings. The BOD met on 1st January 2004 and declared right offering under the preemptive right of the existing shareholders. The shareholders must record their name until 15th February 2004 which was declared by BOD. 11th February is the ex-right date and those who purchase shares on and after this date will not receive rights and receive by the seller of the shares. In the above example 15th February 2004 is record date and any investor who buys shares before 11th February (ex-right date) must record his or her name in the company until 15th February 2004 to receive right shares.

If a company needs additional fund for a long-term purpose, it can issue new common stocks by privilege subscription. If the company sells such stocks, then it must mail to its stockholders. Each stockholder receives one right for each share of the stock owned. The stockholders have right to purchase new additional shares but the company can't force to buy such securities because the stockholders have an option t purchase new stocks according to the term of the right offering. The term specify that how many rights are required to purchase one new share, the expiration date of offering and the subscription price per share. The stockholders have three choices about their rights which are (1) exercise the rights to purchase additional new shares, (2) sell the rights because they are transferable or (3) let the right expire that means do nothing. The subscription period is generally 3 weeks. If a stockholder wants to purchase shares of additional stock but he or she has less right to purchase additional shares. For example- if he or she 58 shares of the stock in a company, then he or she has 58 rights and the number of rights required to purchase new share is 4. Then he or she can buy 14 full shares. If he or she likes to buy 15th share, then he or she should purchase 2 additional rights. But the shareholders should buy the stock before ex-right date. The stock is said to be sell with right-on through the record date and after record date, the stock is said to be sell ex-right that is the stock is traded without rights attached. Investors those who purchase stocks after this date do not receive the rights to subscribe additional stocks. *(SEBON)*

2.13 Procedures of the Issue of Right Shares in Nepal

The company act 2053 of Nepal conducts about the right issue which is regulated by Security Board of Nepal (SEBON). There are some complications about the actual mechanics and the sequence of events in the case of rights offerings in the context of Nepal. This will therefore be useful to outline briefly the actual procedure by which a right issue practice is typically made in Nepal. Certain rules and regulation must be followed by the companies which are described by the company act 2053 and their respective memorandum and article of association. Generally the following procedures are considered before right offering in the context of Nepal:

- The determination of the quantum of further capital requirement and the corporations, in which the rights issue might be offered to existing shareholders, should be considered by Board of Directors (BOD).

- Annual General Meeting (AGM) should pass the proposal of Board of Directors (BOD) by its majority.
- The company should notify to Nepal Rastra Bank (NRB), Nepal Stock Exchange(NEPSE),Security Board of Nepal(SEBO/N)and Office of the company Register sufficiently with prospectus in advance of the date of board of record meeting at which the rights issue is likely to be considered, and should get permission from them.
- Make announcement with prospects which gives a general indication of the reasons, which have made the issue desirable, the purpose for which the new money is to be used.
- Letter of provisional allotment or rights offering to the shareholders with prospects gives advising to the existing shareholders about the rights offerings, the number of new shares allocated to each given number of old shares, the subscription price of the right issue. After the announcement date, this letter will be sent.
- After the receipt of the letter of provisional allotment, the allotment must be accepted or renounced, and payment in full or partial, must be made for those shares which are renounce.
- The shareholders who participated in the rights offering announcement will get the certificates. Shareholders who have accepted and fully paid up their allotment can renounce the actual share certificate in favor of a third party. Because of nontransferable instrument such practice are not seen in Nepalese context.
- The resolution of the board of director to distribute the right share had to approve by shareholder’s Annual General Meeting (AGM). This is very low chance that the resolution of the board of director (BOD) is disapproved by shareholders.
- Listing of the shares in the NEPSE again with increased number which must be approved by the stock exchange after which an application for listed new share could be made.

2.14 Success of Right Offering

If the company wishes to issue right shares to the public, then the company should make two basic decisions which are (1) subscription price and (2) number of rights required to purchase one new share. For the successful of right offering, subscription price is an important decision for the company. This subscription price is the price at which the company is going to subscribe to the existing shareholders, which is set below than the current market price of the stock. If the subscription price is set in such a way that the current market price is lower than the subscription price, then the existing shareholders obviously will not subscribe to the stock. And they can buy the stock in the market at a lower price. Consequently, a company will set a subscription price in such a way that it is lower than the current market price to reduce the risk of the market price's falling below it.

"Apart from the number of rights required to purchase one share the risk that the market price of stock will below the subscription price is a function of the volatility of the company's stock, the tone of the market, expectations of earnings and other factors. To avoid all risk, a company could set the subscription price so far below the market price that there is virtually no possibility that the market price will fall below it" *(Van Horne, 1998:573).* So the company should consider all the risks set the subscription price below than the current market price of the stock. The company also must set the necessary number of rights required to purchase one new share and it is also an important decision taken by the management of the company.

The cash should be submitted along with a certain number of rights for order of the shares which are going to be purchased from the company at a subscription price by the existing shareholders. The success of the right offering is manipulated by the balance between the individual and institutional investors. The success of right offering is also influenced by the size of the capital outlay in relation to a stockholders existing ownership of the stock. The current trend and the tone of the market are also influenced. If the current trend is upward and the market is relatively stable in the upward movement, the probability of the successful of right offering is high. But the current trend is downward and the market is also not so stable, in this case the probability of the successful of the right offering is very low. If the stock market is more uncertain and the under pricing is greater, then in this situation, it is necessary to sell the issue. To avoid uncertainty, an underwriting contract is very good choice which is a guarantee to take up, any of the new shares which are not purchased by existing shareholders or the buyers of their rights in the market at the issue price. So there are many risks associated with right offering which can be avoided by taking some important decisions by the management of the company.

2.15 Over and Under Subscription of Right Offerings

"Underwriting is the insurance, function of bearing the risks of adverse price fluctuations during the period in which a new security is being distributed." *(Weston & Copeland, 1992:891).* Most of the rights offerings are done by investment bankers who underwrite and issue the right shares. So the company is sure about the successful of the right offering with the help of investment bankers who underwrite the unsold portion of the issue. This investment banker agrees to be a standby arrangement. This agreement is a formal guarantee if any shares will not be subscribed, it will purchase the unsold shares. Because of this agreement, the investment banker takes high commission or fees from issuing company for making guarantee.

Oversubscription is a privilege given by the company to the stockholders that they can subscribe for their proportionate shares as well as they can also oversubscribe for any unsold shares because of having right. The numbers of unsold shares are oversubscribed on pro-rata basis by the some existing shareholders. Although the use of the oversubscription increases the chances that the issue will be entirely sold, it does not assure this occurrence, as does the standby agreement. There is possibility of falling short of the amount of the stock of the company which wants to sell because of the combination of subscriptions and oversubscription. Though the ownership proportions may change slightly, this privilege is a method of restricted ownership to the some group. If the shares cannot be sold through the oversubscription privilege, later it may offer to the public. If an investment banker is used, the character of unsubscribed shares may be in case up to the banker.

2.16 Nepalese Laws Relevant to Public

The entire corporation, who wants to issue its shares to the pubic, should follow certain rules and laws. In Nepal, the right issue guideline is not implemented yet. The public and the right offering both are the issue of shares to the public. The company can raise the capital fund by public offering or the right offering but the company should follow certain laws. So if the company is going to issue right share as well as other stocks, it should follow the given laws.

i. Company Act 2053 (1997)
ii. Securities Exchange Act 2040 (1983)
iii. Securities Exchange Regulation 2050 (1993)
iv. New Issue Management Guideline 2054 (1997)
v. Securities Registration and Issue Approval Guideline 2057 (2000)
vi. Securities Allotment Guidelines 2051(1994)
vii. Bank and Financial Intuitions Ordinance 2060 (2003)

2.17 Review of Journals/ Articles

This part deals with the review of journal and article by different expert relating to right share, published in various journals which is given below:

Pathak and Giri (2008), in their article, *"Right Share Issue Practice in Nepal"* have stated that every firm needs adequate capital to perform efficiently. Generally, firms fulfill their financial requirement by issuing equity share, preference share, debentures and long term bonds. Rights issue is one of the instruments to raise additional capital. We can describe the preemptive right or rights as the privilege offered to existing stockholders for buying specified number of additional shares of the company's stock before the stock is offered to outsiders for sale. They have value because generally they are offered at a subscription price somewhat lower than the market price of share.

In the secondary market, investors are willing to buy the share that has been attached to the preemptive right. But to buy additional number of shares, the shareholder should have his/her name in company's book before the record date. Hence before the record date, there will be a great demand of share attached with rights. Demand is increased because large numbers of people rush to secondary market in order to enlist their name in the company's book before record date so that they can enjoy the benefits of right offering. On the other hand, existing shareholders generally have no willingness to sell the shares to exercise the rights. Due to this double pressure, the price of share goes upwards.

Zurich (2009), in his study, *"Right Issues- Are They Right For You?"* has stated that in fact, rights issues don't do any favours for personal investors. Institutional shareowners have the money to take up their rights; personal investors frequently cannot afford to take up their rights, so their 'nil-paid' rights are sold or 'lapse', leaving institutional investors to take them up and further increase their holdings. So every time a company has a rights issue, the proportion of shares held by personal investors falls. If the company's share price is high (for example, when it is raising finance for an acquisition from a position of strength), that may not be so much of a concern: at least personal investors are getting a decent price for their shares. But if the share price is seriously depressed, as with the current round of banking rights issues, this dilution is a serious financial blow to personal investors and is a result of the lack of foresight by some companies' boards.

After a rights issue, distributable profits have to be shared over a greater number of shares than previously, resulting in lower earnings per share and a reduced dividend. Shareholders are therefore offered the subscription at a discount as an incentive to take up their rights and maintain their proportionate stake in the company. If they do not take up their rights their stake will be diluted and the value of their holding will be reduced.

Marisetty, Marsden and Veeraraghavan (2010), in their article, "*Price Reaction to Rights Issues in the Indian Capital Market*" have examined security price reaction to the announcement of rights issues by Indian firms. India is a large economy and a major emerging capital market. The study adds the effects on shareholder wealth of new equity announcements in an emerging market with unique institutional and regulatory features compared to more developed markets.

The price reaction to the announcement of the issue was more negative for firms affiliated to a family group. A rights issue increases the cash resources or level of a firm's financial slack. The study surmises that this provides greater opportunities for the controlling family shareholder to expropriate wealth from the firm to entities where the family group shareholder has greater comparative cash flow rights. Investors therefore react negatively to the announcement of the issue.

Higher levels of individual shareholding are associated with a more positive price reaction to the rights issue announcement. High levels of individual shareholding may expose the firm to a greater likelihood of takeover or impose greater market discipline on managers through the market for corporate control. High levels of individual shareholding may also be associated with greater public scrutiny or monitoring of the use of the proceeds of the rights issue. This ensures less investment in projects that do not enhance the wealth of all shareholders and the price reaction to the announcement of the issue is more positive.

Owen and Suchard (2010), in their article, *"The Pricing and Impact of Rights Issues of Equity in Australia"*, have investigated abnormal returns resulting from the announcement of a rights issue of equity in Australia and also examined the pricing of rights issues and the determinants of that pricing. The announcements of rights issues of equity are met with a significant abnormal return of -1.83% and this negative abnormal return continues after the announcement, although there is a positive pre-announcement effect. In terms of pricing, 84.54% of Australian rights issue of equity are priced at an average discount of 18.89% and 3.38% are priced at the previous day's closing price. Issues made at a premium have significantly higher announcement returns than issues made at a discount (4.17% versus -2.64%).

For issues made at a discount, non-renounceable offers have a significantly higher discount than renounceable issues, which is consistent with expectations that firms offer a discount to induce shareholders to take up non renounceable rights. However, there is no significant difference between the pricing of underwritten and non-underwritten rights issues, which suggests that Australian issuers do not use large discounts as an alternative to having the issue underwritten. There is a significant negative relationship between expected shareholder concentration and the discount which supports the conjecture that firms with higher shareholder concentration do not have to offer large discounts in order to have a successful rights issue.

Dolly (1934) conducted a study on the topic "The price effect of stock rights issue." In this study he uses 303 stock rights issued out of 422 privileged subscription recorded in NYSE. He classified these stock rights by various methods such as industry wise according to the years in which they were issued. In this study he defines a lot of key terms clearly with example. The result of his study seems that the possibilities of a stockholder realizing an immediate profit from a right issue are barely limited. Investors is about as likely to lose , as he is to gain if he sells his stock at the announcement date and buys back just prior to the record date. If he sells his stock ex-rights together with his rights on the record date, in two cases of out of three he will realize a slight appreciation over the value of his stock on the proceeding business day. If the stockholders decides to exercise his rights he would do well to exercise them toward the end of the subscription period, thus allowing for a possible decline in the market price of the stock ex-rights below the subscription price, which would render the stock ex-rights valueless.

Pokhrel (2008), in the article of *"Hakprad Share Kindai Hunuhunchha?" Aarthik Abhiyan*, writes that the flood of share has entered in our capital market at the moment. The shareholders and those who have purchased shares are getting even more shares although shares are scarce in the market to buy. Now a days, Nepalese investors have developed a new principle that is “Buy shares and get immense number of shares” where the prevailing principles propounded by experts kneeled down before them. Nepalese investors’ principle is suspiring but this principle is backed up by the decision taken in 23 April, 2004 where Nepal became the member of World Trade Organization (WTO) and committed to adopt more open and liberal economic policy after 2010. Certainly, foreign investment basically in financial sectors, will enter in our country after 2010 because our financial institutions are operating with very low capital base and are unable to invest individually even in a single hydropower project or in a big project. Considering this fact, Nepal Rastra Bank (NRB) issued a directive to increase the capital base of the financial institutions by the end of 2070 B.S. According to the directive of NRB, Commercial Banks, Development Banks and Finance Companies are required to maintain their paid-up capital of 2 billion, 640 million and 200 million respectively. Due to this reason, Nepalese financial institutions are issuing a large volume of rights share at the moment to meet the target set by NRB. Most surprisingly, the investors are purchasing shares at very high price only to get the right shares. Investors are in ignoring the performance, capacity of risk bearing, future strategies, management team, decisions of management in past, quality of human resources, etc. of concerned companies while buying shares. Even some are affording shares, having less book value then Par Value, at the price more than 240 times of their book value. In Nepalese capital market, shares of those financial institutions, which are declared in critical state by NRB, are also trading at high price.

Such institutions know that the Nepalese investors are attracted towards financial institution's share. So, taking advantage of this, they are also issuing rights shares in the market at a very large amount. If any investors are asked why they are buying such shares then they simply give the same answer that the company is going to offer rights issue. Obviously, they are bound to share the risk associated with such companies by purchasing their shares and promoters may also transfer their risk to the new investors by shifting their investment from such companies. Even some big manipulators of stock market are also selling their shares after realizing the current risk and the new ignorant investors are being trapped by them. So, its time for our investors not to run after market rumors but to invest after analyzing the financial performance and prospects of concerned companies. Otherwise knocking-out from capital market is always probable for such investors.

2.18 Review of Master's Thesis

There are many thesis conducted by different researchers in the past years relating to this topic. Many thesis were studied during the period. Among them, some of the thesis were reviewed and presented here for the analysis of literature.

Gautam (2001), had done research on *"An Analysis of Share Price Movement Attributed to Rights Offering Announcement"*. This study has set out the objectives to analyze the inadequacy of the contents of the Company Act, 2053 B.S in regard to section 21 that explains about the matters to be disclosed in the issue prospectus, to find out if there is significant change in share price after the announcement of rights offerings, etc.

To conduct the study, the researcher had used correlation analysis between share price and NEPSE index i.e. general market movement and t-statistics between share price before and after rights issue announcement. T-statistics was used to test if there was significant change in the share price before and after the issue of rights. But the researcher did not consider the value of right which is very important part of the study. It is seen that the researcher was concentrated on the company act and due to small sample size, the result may not represent the present scenario of rights share issues. The researcher founds that the company Act was not clear regarding the issue of rights offering and subsequent allotment of the right shares and has nowhere mentioned about necessity of legally transferable rights instrument called rights, which must be mailed to the stockholders for each stock held before the rights offering. The study revealed that there was sharp decline in the share price after the announcement of rights issue. The researcher pointed Nepalese security market has failed to use various capital market instruments such as warrants, convertibles, options and other various kinds of debentures.

Baral (2003), in master's thesis entitled *"Stock Price Movement in Nepalese Security Market"* sets some specific objectives. The objectives of the study were to study and analyze the stock price and volume, to study and analyze the rate of newly listed companies in NEPSE, to study and analyze the investors views regarding the decision on stock investment and to study and examine the signaling factors' impact on the stock price with the help of NEPSE index. The researcher analyzed the data of six years and concluded that Nepalese stock market is in the growth stage. Although it has crossed the initial stage but not reached in the matured stage.

The researcher also found that the international environment also affects the Nepalese stock market. But the researcher didn't consider the factors that make a direct effect on the movement of share price. From the study, the researcher founds that most of the stock prices are affected by the dividend policy of the company. The researcher found that most of the investors prefer banking sectors for investment and are not aware about the investment.

Aryal (2003), had made a study on the topic *"Equity Rights Issue; its Practice and Impact in Nepal"*. The main objectives of the study were to examine the relationship between the stock price reaction and announcement of rights issue, and to analyze the relationship between rights share and equity share, and rights share and NEPSE index.
To conduct the study, the researcher had used cross-sectional analysis by estimating the regression and concluded that the announcement of rights offering will have positive effect on share price. The researcher founds that the theoretical value of right differs from company to company and the announcement of equity rights issue are associated with a positive effect on share prices. Company issues rights share to increase equity capital for mainly two reasons. The first reason is to invest it in company's diversification and expansion, and the next reason is to increase capital to meet the level prescribed by Nepal Rastra Bank (NRB). The researcher also founds that rights share and equity share has low degree of positive correlation, and the correlation coefficient between rights share and NEPSE index has also positive correlation.

Regmi (2005), conducted a study on *"Share Price Behaviour in Nepal"*. The main objectives of the study were to test the random walk or weak form of efficient market hypothesis, to examine whether successive price changes are independent or dependent of each other, and to conduct the opinion survey of financial executives regarding various aspects of share price behavior in Nepal. From the study, the researcher concluded that both tests serial correlation and run-test analysis do not support terms of both tests, a few of price series support the random walk model. One important implication of the non random behaviour of share prices in that the Nepalese stock market may not be termed as “weakly efficient” in pricing shares where market efficiency is reflected in security prices. As regard the current trading price of share in the market, the researcher founds that the majority of the respondents felt “moderate”. In this respect when the responses of finance sector respondents, the majority of the respondents from each sector opined that the current trading price of shares in the market is moderate. The informal interview with financial executives in this respect indicated that the current trading price of shares in the market is low except for financial institutions. The researcher also concludes that Nepalese investors are not really indifferent towards making or non-making of information public.

Chongbang(2007), had done a research on *“A study on Issue of Right Share and its Impact on the Movement of Share Price with Special Reference of Nepalese Capital Market”*. The study had set out the objectives to analyze the significant change of share price after announcement of right share and to analyze the problems associated with issuing of right shares in the Nepalese capital market. To conduct the study, the researcher used the correlation analysis as a major statistical tool and t-test to test the hypotheses of the study. The researcher concluded that there were only few companies that follow the theory of rights offering. Only a little number of Commercial Banks followed the theory but in the case of Finance Companies, no one met the theory of rights offering. Although the researcher analyzed the 11 years data, the researcher failed to include other sector companies rather than banking and finance sectors in the study. But the researcher was successful in analyzing recent data which may show the present scenario of Nepalese capital market. From the study, the researcher founds that there was no uniformity in the impact of right share in different companies. A practice of right share issue in Nepal is in increasing trend in recent years where Nepalese investors mostly prefer the banking and finance sectors to invest rather than other sectors. Subscription price of rights share is too low as compared to market price of share. The researcher also found that Most of the right issues were undersubscribed in Nepalese capital market and there is lack of clear and easy provision regarding the sales of under subscribed shares.

Paudel (2008), in master's thesis entitled *"Rights Share Issue Practice in Nepalese Market and its Impact on Market Price of Share"*, focuses the study in rights share practice and its impacts. The main objectives of the study were to find out the impact on changes in market price of stock, before and after the announcement of rights offering, to examine the theoretical value of right and its practical effect of right on stock price, and to analyze the inadequacy of existing law on the matter of rights share. The researcher analyzed the primary data as well as secondary data to conduct the study. Run test, t-test and Chi-square test were used as statistical tools to test the hypotheses. The researcher concluded that the majority of the companies followed the rule of rights issue which can be observed through the decreased price of stock after rights issue. The study had taken the whole companies as sample that had issued rights share in a single year to explore the facts of rights offering practices in Nepalese capital market. The researcher founds that Nepalese equity market is dominated by financial sector companies and the participation of the real sector is quite low or negligible. Rights offering have some impact on the price of share either positive or negative, and mostly, market price of shares are found decreased after the rights issue. Under subscription of rights issue is common phenomena as right is not transferable in Nepal. So existing legal provisions are not adequate and needs to be amended as soon as possible.

2.19 Research Gap

Looking at the fifteen- year old history of the issue approval from the Securities market there are many studies conducted which are related to the capital market and share price behaviour in Nepal but this study especially focuses on an issue of rights share and its impact on the movement of share price in Nepalese capital market. Different studies showed that the capital market is the essential sector in order to develop the nation because the nation will be strong and developed only if each and every sector is capable and strong. Rights share is also one of the major instruments for raising additional equity capital from the capital market. After reviewing some thesis and other related sources, it is found that various studies were done on the topic of share price and its determinants. Some of the studies were conducted based on financial performance, some were based on dividend policy, some were based on bonus share and nominal researches were based on right shares. Similarly, only few Nepalese writers have written articles directly based on the rights share and some of those studies are also conducted several years ago. Therefore, there is a gap of time period which will be fulfilled by this study. Though, some researches were conducted on right share issues, but they were especially concerned with the rights offerings of listed Commercial Banks and Finance Companies ignoring the rights offering of other sectors. Therefore, those studies couldn't cover the whole sector in Nepalese capital market. More precisely at present context, Development

Bank sector has covered a major portion of rights share issues in Nepalese capital market. But none of the studies on rights shares issues have covered this sector and Insurance sector till the date in their studies. So, this study tries to show the issue of rights share and its impact on movement of share price of Banking, Finance, Development Bank and Insurance sectors. It is hoped that it will give more detailed information about the rights share. Samples from the Banking, Finance, Development Bank and Insurance sectors are taken to be considered because these sectors are issuing largest amount of shares in Nepalese capital market. Moreover, the earlier studies on rights share have become old and need to be updated and validated because of the rapid changes taking place in capital market. This research provides clear vision on the right shares which have not given by the other researchers. Other research works which have done on the right offering which are being old in the context of rapid changes in the capital market. So this research is essential to provide fresh study on the right offering because of the rapid changes in the capital market. At last we can say that this research is being useful as information for related bodies like SEBON. NEPSE, NRB, investors, managers etc.

CHAPTER- III
RESEARCH METHODOLOGY

3.1 Introduction

Research methodology indicates the methods and processes employed in the entire aspects of the study. It refers to the various subsequent steps to be adopted by a researcher in studying a problem with certain objectives in a view. So, it is the method, steps, and guidelines, which are to be followed in analysis and it is a way of presenting the collected data with meaningful analysis. This section highlights the methodology adopted in the process of present study. It also focuses about sources and limitations of the data, which are used in the present study. Research methodology is a way for systematically solving the research problem *(Kothari, 1990: 127).*

Research Methodology refers to the various steps that are generally adopted by a researcher in studying his research problem along with logic behind it. Thus, research methodology is a systematic and organizes effort to investigate a specific problem that needs a solution *(Wolf and Plant, 1999: 131).*The main objective of the study is based on primary and secondary data. The basic objective of primary data analysis is to survey the opinions of rights shareholder and rights share issuing company management body. Secondary data were used on analyze the relationship between stock price reaction and announcement of rights issues, correlation coefficient between rights share and equity shares, correlation coefficient between rights shares and NEPSE Index, number of issue approval of rights share etc. The methodology consists of Research Design, The Selection of Sample, Source of Data, and Coverage of the Data, Data Analysis Tolls, Others Statistical Tools and Valuation of Rights.

3.2 Research Design

In simple language, planning for research is research design. It is a purpose full scheme of action proposed to be carried out in a sequence during the process of research. Research Design is a conceptual framework within which a research is conducted. It helps the researcher to enable him to keep tack of action and to know whether he is moving the right direction to achieve his goal. Kothari (2000), states that research design is a plan, structure and strategy of investigation concerned so as to obtain answer to researcher question and to control variance. This research is based on the analytical and descriptive design as well. "A research design is the agreement of condition for collection and analysis of data in a manner that aims to combine relevance to the research purpose with economy in procedure" *(Bhurtel; 2002:43).* " In other words, research design is the plan structure and strategy of investigation conceived so as to obtain answer to research questions and to control variances" *(Kerlinger; 1978:300).* The primary objective of this research is to analyze the right share and its role on the stock price movement of the stock. Therefore, to conduct the study, analytical descriptive approaches has been made to evaluate the role of right offering (shares) on the stock price movement of the sample firms and logical conclusion could be made. All the data used in this study, are secondary as well as some are primary in nature.

3.3 Population and Sample

The data collection activities consist of taking order information from reality and transferring into same recording system. So, that it can be examined and analyzed from pattern. Population or universe refers to the entire group of people events, or things of interest that the researcher wishes to investigate. In most of cases, we cannot collect data of whole population. Therefore, sample in the best technique of the research study. A sample is the collection of items from population or universe and comprises some observations selected from the population. Sampling method is the scientific procedure of selection those representative units which would provide the required elements with associated margin of uncertainty arising from examining only a part and no to the whole. The corporate firms which issued right shares are given below.

Table 3.1

Right Share of Corporate Firms in Nepal

Fiscal Year	Number of Rights Offering companies
2052/53	2
2053/54	3
2054/55	3
2055/56	1
2056/57	3
2057/58	2
2058/59	5
2059/60	4
2060/61	3
2061/62	6
2062/63	11
2063/64	16
2064/65	42
2065/66	50
2066/67	33
Total	**184**

Source: Annual Report of SEBON 2066/67

For simplicity and unbiased result, 16 companies are taken as samples.

Name of sample Companies

Finance Companies
Ace Finance Company Limited
Annapurna Finance Company Limited
Nawa Durga Finance Limited
Capital Merchant Banking & Finance Limited
Kist Merchant Banking & Finance Limited
Alpic Everest Finance Limited
Yeti Finance Limited
Pokhara Finance Limited
People Finance Limited
Development Bank
Nepal Development Bank Limited
Paschimanchal Development Bank Limited
Business Development Bank Limited
Chhimek Development Bank Limited
Banks
Siddhartha Bank Limited
Laxmi Bank Limited
Lumbini Bank Limited

Note: Ace Finance Company Ltd. & Kist Merchant Banking & Finance Ltd. is converted as Bank till now.

3.4 Sources for Data

This research is mainly based on secondary sources for reference as well as primary sources. Secondary sources used in this research are Annual report of SEBON, NEPSE, respective companies and some related information are taken from economic survey. Other data have been collected from newspapers, books, magazines and journals. Primary data is taken as personal interview with the official of SEBON, NEPSE, mangers and officers of issue managing companies, issuing companies, investors and exports.

In order to bring out the answer, the research questions are put to managers and officers (concerned with the issue of rights share) of the issuing companies, regulatory bodies, investors issue, managing companies and experts for the primary source of data. Questionnaires are sent out to a sample of 60 people and 60 responses are obtained. The table below shows the sample and response of the primary source of data. Questionnaire is presented in the appendix II.

Thus here the some of responds from sample and response as a primary source of data. Out of total 60 responses, commercial bank 10, Development Bank 10, Insurance company 2, finance 2 and from managers and officer of issuing manager and regulatory office 20 and investor and experts 15.

3.5 Data Processing Technique and Procedure

The collected data from NEPSE, SEBON etc need to be aggregated into a form that presents the summary of answers from respondents. Data presenting and analyzing tools are trend bar and Hypothesis test.

In this research work, theoretical market price will be used to measure the role of right share issue on market price of share. Theoretical market price of share after right share issue is given by

Theoretical Value of Stock after right share issue = $\frac{P_0 \# \Gamma P^s}{\# \Gamma 1}$

Pre right issue stock price =P_0

Subscription price =P^s

No. of general shares required to purchase one right share = #

3.5.1 Percentage change in MPS

Percentage change in MPS provides the deviations of the share price due to right share issue phenomenon on the share price before right share issue. If the percentage changes become positive, it points out that the MPS has increased after right share issue. Likewise, if the percentage of change comes negative, it points out that the MPS has decreased after right share issue. And if the percentage change come zero, it specifies that there is no change in MPS before and after right issue. The percentage that has been changed in MPS after right share issue is computed by using the following formula.

Change in Price (%) = $\frac{P \quad R.I: \quad P \quad - P \quad R.I: \quad P}{P \quad R.I: \quad P}$

3.5.2 Percentage Change in Actual Market Price and Theoretical Price

This provides the percentage deviation of actual price on theoretical price after right share issue. If the percentage change comes negative, it indicates that the theoretical price is greater than actual price after right share issue. Similarly, if the percentage change comes positive, it specifies that theoretical price is less than actual market price after right share issue. And if the percentage change comes to be zero, it indicates that the theoretical price and actual price are same after right share issue. This has been calculated given by the formula.

Percentage (%) Change = = $\frac{A \quad P \quad - T \quad P}{T \quad P}$

3.5.3 Hypothesis Test

"Hypothesis is a statement about the relationship between two or more variables which need to be investigated for its truth" (Wolf and Pant, 2003:62). It is a reasonably assumed relationship between two or more variables said in the form of testable statements. Following hypothesis are put in this research paper.

Null Hypothesis H0:

$\upuparrows_x = \upuparrows_y$, that actual market price after right share issue and theoretical price after right share issue are same. In other words, there is no significance difference between theoretical price and actual market price after right share issue.

<u>Alternative Hypothesis H1:</u>

⥣x| |⥣y that is actual market price after rightly share issue is not equal to theoretical market price. In other words, there is significance difference between theoretical market price and actual market price after right share issue. (Two tail test)

Test Statistics are

$$\bar{d} \ \mathrm{X} \frac{d}{n}$$

$$s \ \mathrm{X} \sqrt{\frac{1}{n \ \mathrm{Z} 1} \quad d^2 \ \mathrm{Z} \frac{(\quad d)^2}{n}}$$

$$t \ \mathrm{X} \frac{\bar{d}}{\frac{sd}{\sqrt{n}}}$$

I. Arithmetic Mean

The sum of all the observations divided by number observations is called arithmetic mean or simple average. In equation:

$$X = \frac{X}{n}$$

Where, $X \ \mathrm{X} \ X_1 \ \Gamma \ X_2 \ \Gamma \ X_3 ....X_n$ X given set of observations

n = Number of items observed.

II. Standard Deviation (±)

Standard deviation was first suggested by Karl Pearson in 1893 A.D. as a measure of dispersion. It is usually denoted by sigma (±). The measurement of the scatterings of the mass of figures in a series about an average is known as dispersion and standard deviation measures the absolute dispersion. Greater the amount of dispersion greater will be the standard deviation and vise versa. A small standard deviation means high degree of uniformity of the observation as well as homogeneity of a series. A large standard deviation refers low uniformity and homogeneity of the series.

Symbolically,

$$SD\ (\pm)\ X \sqrt{\frac{(X\ Z\ \overline{X})^2}{n}}$$

II. Coefficient of Variation (C.V.)

The relative measure of dispersion based on standard deviation is known as coefficient of standard deviation. Coefficient of dispersion based on standard deviation multiplied by 100 is known as coefficient of variation (C.V.).

Symbolically,

$$C.V. = \frac{\pm}{\overline{X}} \mid 100$$

The coefficient of variation reflects the relationship between standard deviation and mean. Since C.V. is independent of unit, two distributions can bitterly be compared with the help of it for their variability. Higher C.V. denotes higher variability i.e. lesser uniformity and consistency and vise versa.

CHAPTER- IV

DATA PRESENTATION AND ANALYSIS

This chapter mainly represents the presentation and analysis of data. The data obtained from both primary and secondary sources are analyzed. The primary data mainly consists of the responses to questionnaires and personal interview with experts, investors, officers and other related persons. In the same way, the secondary data are obtained from annual reports of SEBON, NEPSE, sample companies etc. This chapter of this research work helps to achieve the objective of the study.

4.1 Right Shares Issued by Nepalese Corporate Firms in Nepal

The detail information of the right offering from fiscal year 2052/53 to 2066/67 is given below:

Table 4.1

Right Shares Issued by Nepalese Corporate Firms in Nepal

(Rs. In Million)

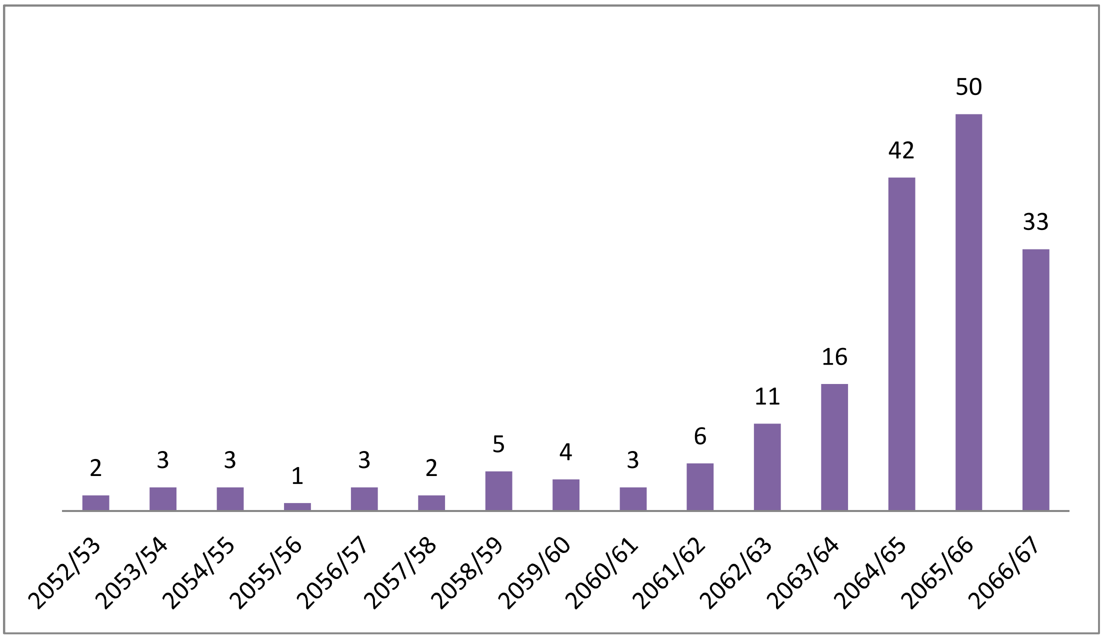
Fiscal Year (A)	Total Public Floatation (B)	Number of Rights Offering (C)	Total Amount Raised Through Rights Offering (D)	% of Right offering
2052/53	293.74	2	69.00	23.49%
2053/54	332.20	3	275.20	82.84%
2054/55	462.36	3	249.96	54.06%
2055/56	258.00	1	30.00	11.63%
2056/57	326.86	3	184.60	56.48%
2057/58	410.49	2	131.79	32.11%
2058/59	1441.33	5	885.45	61.43%
2059/60	556.54	4	162.24	29.15%
2060/61	1027.50	3	70.00	6.81%
2061/62	1476.82	6	949.34	64.28%
2062/63	2443.28	11	1013.45	41.48%
2063/64	2295.50	16	1265.30	55.12%
2064/65	10668.20	42	6093.4	57.11%
2065/66	16828.50	50	14262.8	84.75%
2066/67	10822.41	33	8173.04	75.5%
Total	**49643.73**	**184**	**33815.57**	**68.11%**

Source: Annual Report of SEBON 2066/67

Most of the companies issue right share in order to increase paid up capital as directed by NRB.

Figure 4.1

The Companies Who Issued Right Shares from Fiscal Year 2052/53 to



2066/67

As stated above, the figure 4.1 gives the clear picture of the number of companies that issued right shares, are increasing every year since FY 2052/53 to FY 2065/66. This figure indicates that the Nepalese Corporate Firms are being interested to issue right shares for raising capital funds. Therefore, the issuance of right shares by the Nepalese Corporate Firms is in increasing trend. However in FY 2066/67 only 33 companies issued right share.

4.2 Contribution of Rights Issue on the Total Public Flotation

The given table shows the contribution of right share issue in the total public flotation in each fiscal year in which the right offering has made.

Table 4.2

Right Shares Issued by Nepalese Corporate Firms in Nepal

(Rs. In Million)

Fiscal Year (A)	Total Public Floatation (B)	Number of Rights Offering (C)	Total Amount Raised Through Rights Offering (D)	% of Right offering
2052/53	293.74	2	69.00	23.49%
2053/54	332.20	3	275.20	82.84%
2054/55	462.36	3	249.96	54.06%
2055/56	258.00	1	30.00	11.63%
2056/57	326.86	3	184.60	56.48%
2057/58	410.49	2	131.79	32.11%
2058/59	1441.33	5	885.45	61.43%
2059/60	556.54	4	162.24	29.15%
2060/61	1027.50	3	70.00	6.81%
2061/62	1476.82	6	949.34	64.28%
2062/63	2443.28	11	1013.45	41.48%
2063/64	2295.50	16	1265.30	55.12%
2064/65	10668.20	42	6093.4	57.11%
2065/66	16828.50	50	14262.8	84.75%
2066/67	10822.41	33	8173.04	75.5%
Total	**49643.73**	**184**	**33815.57**	**68.11%**

Source: Annual Report of SEBON 2066/67

It is clear from above table that in the preliminary stage, the trend of rights offering in Nepalese share market was quite low. In the fiscal year 2052/53, there were two cases of rights offering in which the share of rights offering was 23.49% of the total public floatation. Similarly in the fiscal year 2053/54, 3 companies issued rights share amounting Rs. 275.20 million out of Rs. 332.20 million of total public floatation. Observing the above data, we can easily conclude that the share of rights offering on total public floatation was highest during the fiscal year 2053/54. In the fiscal year 2054/55, out of Rs. 462.36 Million of total public floatation, Rs. 249.96 million was raised through rights offering. In the fiscal year 2055/56, the contribution of rights share on total public floatation was just 11.63% i.e. Rs. 30 million out of Rs. 258 million of total public floatation. In FY 2056/57, three companies issued right share. The proportion of rights share was 56.48% i.e 184.60 million out of Rs 326.86

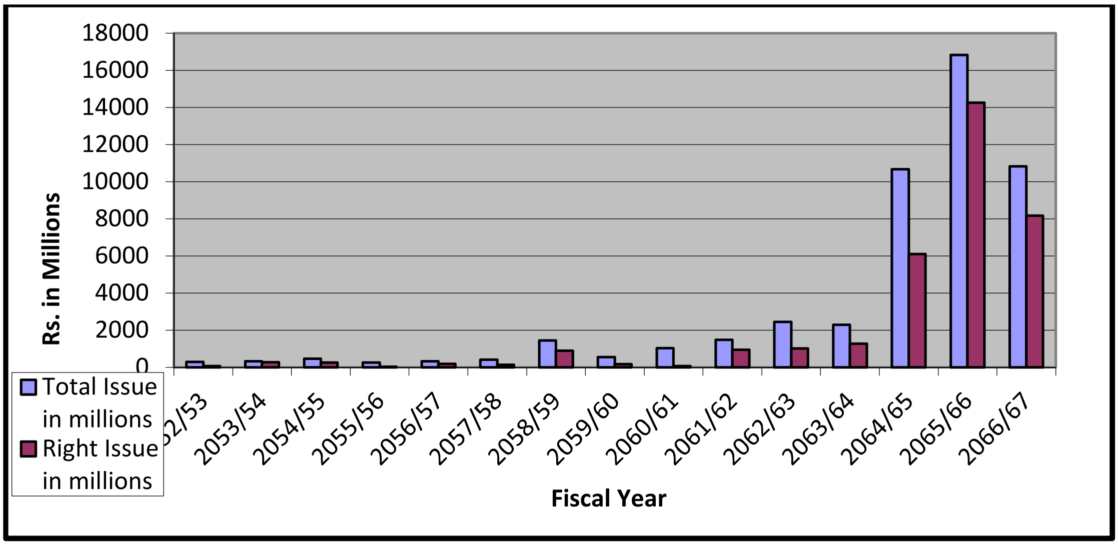
million of total public floatation. In that fiscal year, Necon Air, Paschimanchal Finance Company Ltd and Ace Finance Co. Ltd issued right share. Similarly Narayani Finance Ltd and Everest Bank Ltd issued right share in the FY 2057/58. The proportion of right share was 61.43% in the FY 2058/59. In the FY 2059/60, there were 4 cases of rights offering of Rs. 162.24 million which covers 29.15% of total public floatation of Rs. 556.54 Million.

In the FY 2060/61, three companies namely Alpic Everest Finance Ltd, Siddhartha Finance Ltd, NB Finance and Leasing company issued rights share of Rs. 70 million i.e 6.81% of Rs. 1027.50 million of total public floatation. The issuance of right share seems quite low in this fiscal year. Altogether 6 companies issued right share in FY 2061/62 amounting Rs. 949.34 million which is 58.36% of total public floatation of Rs. 1626.82 million. In FY 2063/64, 16 companies issued right share. The proportion of rights share was 55.12% i.e. Rs. 1265.30 million out of Rs. 2295.5 million of total public floatation. In FY 2064/65, 42 companies issued right share. The proportion of rights share was 57.11 % i.e. Rs.6093.4 million out of Rs.10668.20 million of total public floatation. In FY 2065/66, 50 companies issued right share. The proportion of rights share was 84.75% i.e. Rs. 14262.8 million out of Rs. 16828.5 million of total public floatation. In FY 2066/67, 33 companies issued right share. The proportion of rights share was 75.5% i.e. Rs. 8173.04 million out of Rs. 10822.41 million of total public floatation.

After analyzing the table, it is clear that during the period, there is lower percentage of rights offering i.e. 6.81% and highest percentage of rights offering i.e. 84.75% in FY 2060/61 and FY 2065/66 respectively. This was because of the NRB directives that the financial institutions have to maintain optimal capital adequacy ratio. So most of the financial institutions had to raise their capital and they issued right share.

Figure 4.2

Contribution of Right Issue on Total Public Flotation



Source: Table 4.1

The above figure 4.2 shows the growing trend of the issue of right shares to increase the additional funds in five fiscal years. Whatever the total amount of flotation, the amount of right share issue is increasing.

4.3.Contribution of Rights Issue in Total Public Flotation in FY 2066/67

The following table and figure shows the contribution of rights issue in total public flotation in the fiscal year 2066/67.

Table 4.3

Contribution of Rights Issue in Fiscal Year 2066/67

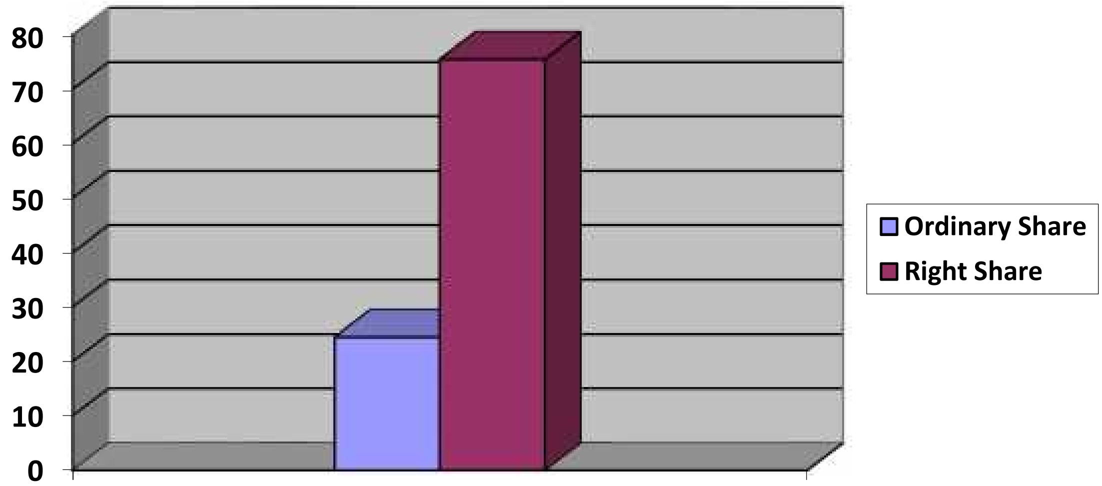
(Rs. in million)

Securities	No of Issues	Issued Amount	Percentage (%)
Ordinary share	28	2649.37	24.48
Rights share	33	8173.04	75.52
Debenture	0	0	0
Total	**61**	**10822.41**	**100**

Source: Annual Report of SEBON (2066/67)

Figure 4.3

Contribution of Rights Issue in Fiscal Year 2066/67



From the above table and figure securities wise contribution in total public flotation in the fiscal year 2066/67 can be clearly seen. In this fiscal year, only Ordinary share and right shares were issued by the firms to public announcement Rs. 10822.41 million in total. Out of them, 28 companies issued ordinary shares to public amounting 2649.37 million which contributes 24.48% in total public issue. Similarly 33 companies issued right shares to their existing shareholders which contributes 75.52% in total public issue and the mount of right issue was 8173.04 million. So it is clear that right issue contributes the highest in total public issue in the fiscal year 2066/67.

4.4 Sector wise contribution in right Issue in Fiscal Year 2066/67

The following table and figure shows the sector wise contribution in rights issue in the fiscal year 2066/67

Table 4.4

Sector wise contribution in right Issue in Fiscal Year 2066/67

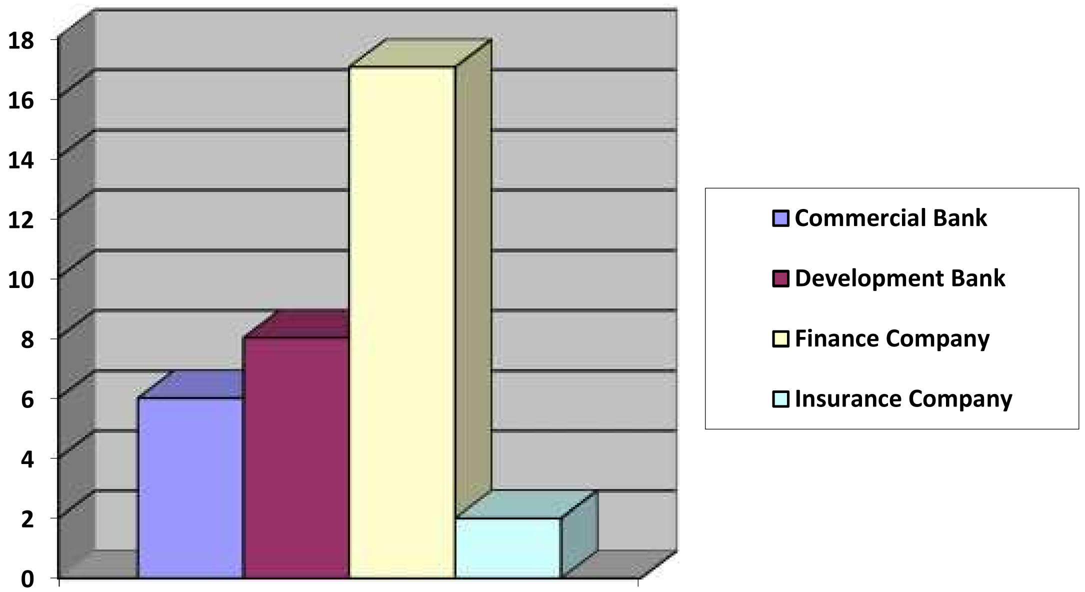
(Rs. in million)

Sector	**Number of Companies**	**Right Issued Amount**	**Percentage %**
Commercial Bank	6	2551.49	31.22
Development Bank	8	1695.40	20.74
Finance Company	17	3791.20	46.39
Insurance Company	2	134.95	1.65
Total	**33**	**8173.04**	**100**

Source: Annual Report of SEBON 2066/67

Figure 4.4

Sector wise contribution in right Issue in Fiscal Year 2066/67



The above table and figure shows the contribution of each sector in right issue in the fiscal year 2066/67. Only four sector viz. commercial Bank, Development Bank, Finance and Insurance sectors issued right shares in the fiscal year. Among them 6 commercial Banks issued right shares amounting

2551.49 million which contribute 31.22% in total amount of right shares amounting Rs. 8173.04 million. The contribution of Development banks was 20.74%in total where 8 Development banks issued right share of amount Rs. 1695.40 Million. Similarly 17 Finance companies issued right shares of Rs. 3791.20 million which covered 46.39% in total rights issue amount and finally, 2 Insurance companies issued Rs. 134.95 million of rights shares which contribute 1.65% in total amount of right issue. Beside these, other sectors didn't issue right share in the fiscal year. From the above table and figure, it is clear that only banking and financial institutions issued rights share in the fiscal year 2066/67.

4.5 Comparison of Stock Price Before and After Right Share Issue

The role of right share issue on the stock price movement is calculated here. So, the impact of right share issue on market price per share is calculated here. Theoretically, it is said that the price of the share decreases after right share issue. The given table shows that the market price per share before right share issue and after right share issue and their percentage difference. Pre right issue price is the closing market price 1 month prior to right share issue and post right issue price is the closing market price after 1 month of right share issue.

The positive change in price indicates that the post right issue price is greater than pre right issue price. Similarly, the negative change in price indicates that the post right issue price is less than the pre right issue price. The zero change in price indicates that the post right issue price and the pre right issue price are equal.

Theoretically, the negative change in price shows that the post right issue price is smaller than the pre right issue price and this is the theoretically correct phenomenon. If the positive change in price shows that the post right issue price is higher than the pre right issue price and this is the theoretically incorrect phenomenon. And also, the zero change in price between post and pre right issue5011 price shows that this is also theoretically incorrect phenomenon.

Table 4.5

MPS of Sample Companies before and after Right Share Issue

S. No.	Name of Companies	Pre. Right Issue Price (Rs.)	Post Right Issue Price (Rs.)	Change in Price (Rs.)	Change in Price (%)
1	PFL	410	400	-10	-2.44
2	PEOFL	137	130	-7	-5.11
3	AEFL	150	150	0	0.00
4	NFCL	115	120	+5	+4.35
5	AFCL	448	357	-91	-20.31
6	ANPFL	500	500	0	0.00
7	YFL	230	230	0	0.00
8	CMBFL	196	179	-17	-8.67
9	KMBFL	400	560	+160	+40.00
10	LBL	172	167	-5	-2.91
11	LAXBL	520	660	+140	+26.92
12	SBL	546	778	+232	+42.49
13	PDBL	103	105	+2	+1.94
14	BDBL	381	365	-16	-4.20
15	CDBL	100	105	+5	+5
16	NDBL	133	145	+12	+9.02

Source: Annual Report of SEBON and Trading Report of NEPSE

From the above table, we can say that there is majority case of changes in price which is in positive. It indicates that the market price per share of the most of the companies is not followed the theory. The theory implies that the market price of the share decreases after the right share issue. Among 16 cases of the companies, there are seven cases of the companies whose market price of the stock increases in the NEPSE's annual report. There are six cases of the companies whose market price per share after right share issue have decreased. Similarly, there are three cases of the companies that their market price per share before and after right share issue remains same.

.From the above table and study we can say that generally the market price per share should be decreased after the right share issue. But through this study, the market price per share of the majority portion of the companies is increased. This may happen because of various factors such as political environment, economic environment, investors, trading environment in the stock market etc.

4.6 Comparison of Theoretical and Actual Market Price after right share issue

To find out the role of the right offering on the stock price movement, we have to compute the theoretical market price per share. That means the impact of the right share issue on the market price per share can be found with the help of the theoretical market price per share. For the measurement of the impacts of the right share issue, the theoretical market price per share will be compared with the market price per share after the ex-right date. These comparison outcomes of the share evaluate the impact of the right offering on the market price per share. Through this result the role of the right offering on the stock price movement can be found out. If the market price per share is higher than the theoretical market price per share, then it should be taken as positive change in share price. And this is the good sign for shareholders as well as the company. But if the market price per share is lower than the theoretical market price, then it is taken as negative sign and this sign discourages the shareholders as well as the company.

The percentage change in actual market price and theoretical price of share after right share issue. Theoretically, actual market price per share should be equal to theoretical price of the share after right share issue. But above table shows that actual market price per share is not equal to theoretical price after right share issue. Actual market price after right share issue is collected from the trading reports of NEPSE and theoretical price of the share after right share is calculated in the table.

Table 4.6

Comparison between Actual Market Price and Theoretical Price after Right Share Issue

S. No.	Name of the Companies	Actual MPS after right issue	Theoretical Price after right issue	Actual MPS-Theoretical Price	% Change
1	PFL	400	306.67	93.33	+30.43
2	PEOFL	130	118.50	11.50	+9.70
3	AEFL	150	133.33	16.67	+12.50
4	NFCL	120	110	10	+9.09
5	AFCL	357	237.09	119.91	+50.58
6	ANPFL	500	300.50	199.50	+66.39
7	YFL	230	204	26	12.75
8	CMBFL	179	143.54	35.46	+24.70
9	KMBFL	560	250	310	+124
10	LBL	167	160	7	+4.38
11	LAXBL	660	450	210	+46.67
12	SBL	778	471.67	306.33	+64.95
13	PDBL	105	101.25	3.75	+3.70
14	BDBL	365	240.50	124.50	+51.77
15	CDBL	105	100	5	+5
16	NDBL	145	116.50	28.50	+24.46
					539.41

Source: Annual Report of SEBON and Trading Report of NEPSE

The above table indicates that the actual market price of sixteen companies is greater than the theoretical price. The actual market price of Pokhara Finance Ltd and Peoples Finance limited are Rs. 400 and Rs. 130 and their theoretical price are Rs 306.67 and Rs 118.50 respectively. The % changes between the two prices are +30.43% and +9.70% respectively. Similarly, the actual market price of Alpic Everest Finance limited and Nawa Durga Finance Company Limited are Rs.150 and Rs. 120 and their theoretical price are Rs. 133.33 and Rs 110 respectively. The % change between two prices are +12.50% and + 9.09% respectively. The actual market price of Ace Finance Company

Limited, Annapurna Finance Company Limited and Yeti Finance Limited are Rs. 357, Rs. 500 and Rs. 230 and their theoretical price are their theoretical prices are Rs. 237.09, Rs. 300.50 and Rs. 204 respectively. Their percentage change between three prices is +50.58, +66.39 and +12.75 respectively. In the same way, the actual market price of Capital Merchant Banking And Finance Limited and Kist Merchant Banking And Finance Limited are Rs. 179 and Rs. 560 and their theoretical prices are Rs. 143.54 and Rs. 250 respectively. Their percentage change between two prices are +24.70% and +124% respectively. Similarly, the actual market price of , Lumbini Bank Limited, Laxmi Bank Limited and Siddartha Bank Limited are Rs.167, Rs 660 and Rs.77and their theoretical prices are Rs. 160, Rs. 450 and Rs. 471.67 respectively.

Their percentage change is +4.38, +46.67 and +64.95 respectively. Likewise, the actual market prices of Pashchimanchal Development Bank limited, Business Development Bank Limited, Chhemek Development Bank limited and Nepal Development Bank Limited are Rs. 105, Rs. 365, 105 and Rs. 145 and their theoretical prices are Rs. 101.25, Rs. 240.50, Rs. 100 and Rs.116.50 respectively. Their percentage change is +3.70, +51.77, +5 and +24.46 respectively.

From the above analysis, it is found that out of 16 sample companies, all companies' actual market prices are higher than the theoretical price showing positive change. The average percentage change between the actual market price and theoretical price is 33.71%.

4.7 Testing of Hypothesis

The testing of Hypothesis is a process of drawing conclusion about characteristics relating to a large number of events (population characteristics) on the basis of sample observations. A hypothesis is defined by Webster as "A tentative theory or supposition provisionally adopted to explain certain facts and to guide in the investigation of others." However in statistics, hypothesis means a statistical statement about the values of one or more parameters of the population.

In testing of Hypothesis, statistics calculated from samples drawn are taken as for examination whether the samples drawn belong to the parent population with certain characteristics. The computed values of statistics are likely to differ from the reality or population parametric value. This difference occurs simply because of the sample fluctuation or operation of chance. The testing of hypothesis releases the fact whether the difference between the calculated statistics and hypothetical parameter is significant.

4.7.1 Testing of difference in Actual Market Price and Theoretical Price

Testing of hypothesis includes the following systematic steps in order to make precise decision about the value which has to be tested.

Step I: Null hypothesis H_0 : $\mu_x = \mu_y$, i.e**.** there is no significance difference between Actual Market price after Right share issue and Theoretical Price after Right Share Issue. This means the Actual Market Price after Right Share Issue and the Theoretical Price after Right Share Issue are same.

Step II: Alternative Hypothesis H_1 : $\mu_x \div \mu_y$ i.e. there is significance difference between Actual Market Price after Right Share Issue and Theoretical price after Right Share Issue. This means Actual Market Price after Right Share Issue is not equal to Theoretical Market Price.

Step III: Test Statistics

$$t \text{ X } \frac{\bar{d}}{sd/\sqrt{n}}$$

Calculation of $\bar{d}$ and sd:

Table 4.7

Testing of Difference in Actual Market Price and Theoretical Price

S. No.	**Name of the Companies**	**Actual Market Price per Share after Right Share Issue (x)**	**Theoretical Price after Right Issue (y)**	**d (x- y)**	**d ^{2}**
1	PFL	400	306.67	93.33	8710.4889
2	PEOFL	130	118.50	11.50	132.25
3	AEFL	150	133.33	16.67	277.8889
4	NFCL	120	110	10	100
5	AFCL	357	237.09	119.91	14378.4081
6	ANPFL	500	300.50	199.50	39800.25
7	YFL	230	204	26	676
8	CMBFL	179	143.54	35.46	1257.4116
9	KMBFL	560	250	310	96100
10	LBL	167	160	7	49
11	LAXBL	660	450	210	44100
12	SBL	778	471.67	306.33	93838.0689
13	PDBL	105	101.25	3.75	14.0625
14	BDBL	365	240.50	124.50	15500.25
15	CDBL	105	100	5	25
16	NDBL	145	116.50	28.50	812.25
	Total			$\sum d = 1507.45$	$\sum d^2 = 315771.3289$

$$\bar{d} = \frac{\sum d}{n} = \frac{1507.45}{16} = 94.22$$

$$sd = \sqrt{\frac{1}{n-1}\left[\sum d^2 - \frac{(\sum d)^2}{n}\right]} =$$

$$\sqrt{\frac{1}{16-1}\left[315771.3289 - \frac{1507.45^2}{16}\right]} = \sqrt{0.0667 \times 173745.9850} = \sqrt{11588.8572} = 107.65$$

$$t = \frac{\bar{d}}{sd/\sqrt{n}} = \frac{94.22}{107.65/\sqrt{16}} = 3.501$$

Step IV: Level of Significance, Degree of Freedom & Critical Value

Let level of significance (α) = 5%=0.05

Degree of freedom $(d.f.) = n-1 = 16-1 = 15$

Since, Tabulated $t(\alpha, d.f.) = t(0.05,15) = 2.131$

Step V: Decision

Since, calculated "t" is greater than tabulated "t" at 5% level of significance and 15 degree of freedom, so we reject null hypothesis and accept "H_1". This means there is significance difference between Actual Market price after Right share issue and Theoretical Price after Right Share Issue. It means Actual Market Price after Right Share Issue is not equal to Theoretical Market Price.

4.7.2 Testing of Hypothesis

Step I: Null hypothesis H_0 : $\mu_1 = \mu_2$ i.e. Right share is not responsible for the stock price movement.

Step II: Alternative Hypothesis H_1 : $\mu_1 \neq \mu_2$ i.e. Right share is responsible for the stock price movement.

Step III. Test Statistics: Two tail test

$$t = \frac{\bar{d}}{sd/\sqrt{n}}$$

S. N.	Name of the Companies	Pre. Right Issue Price (Rs.)	Post Right Issue Price (Rs.)	Change in Price (Rs.) “d”	$(d \ Z \overline{d})^2$
1	PFL	410	400	-10	1269.4969
2	LBL	172	167	-5	938.1969
3	PDBL	103	105	+2	558.3769
4	PEOFL	137	130	-7	1064.7169
5	AEFL	150	150	0	656.8969
6	CDBL	100	105	+5	425.5969
7	NDBL	133	145	+12	185.7769
8	NFCL	115	120	+5	425.5969
9	AFCL	448	357	-91	13602.5569
10	AFCL	500	500	0	656.8969
11	LBL	520	660	+140	13080.4969
12	CMBFL	196	179	-17	1817.3169
13	YFL	230	230	0	656.8969
14	BDBL	381	365	-16	1733.0569
15	KMBFL	400	560	+160	18055.2969
16	SBL	546	778	+232	42588.5769
	Total			d X410	$(d \ Z \overline{d})^2$ X 97715.7504

Source: Annual Report of NEPSE

$$\bar{\bar{d}} \, X \frac{d}{n} \, X \frac{410}{16} \, X 25.63$$

$$sd \, X \sqrt{\frac{(d \ Z \overline{d})^2}{n \ Z 1}} \, X \sqrt{\frac{97715.7504}{16 \ Z 1}} \, X 80.7117$$

$$t \text{ X} \frac{\bar{d}}{sd/\sqrt{n}} \text{ X} \frac{25.63}{80.7117/\sqrt{16}} \text{ X} \frac{25.63}{20.1780} \text{ X} 1.2702$$

Step IV: Level of Significance, Degree of Freedom & Critical Value:

Level of Significance (~) = 5%=0.05

Degree of Freedom ($d.f.$) = n-1=16-1=15

…Tabulated $t_{(0.05,15)}$ X2.131

Step V: Decision: Since, calculated t is less than the tabulated t (i.e.1.2702 2.131), We accept null hypothesis H_0 at 5% level of significance. This means the right share is not responsible for the stock price movement.

4.8 Analysis of Primary Data

In Nepal, now a day's people are being so much interested for investing in the shares. It may happen because of the awareness in those people about the shares, high interest (getting more benefit than other investment) or lack of better investment alternatives though the history of capital market is not so long. People are eagerly interested to invest in the capital market. So, the performance of the capital market is being strong than before. Because of this strength, the expectation of growth of the Nepalese corporate firms is increasing in positive trend. In the context of Nepalese stock market, it is also growing from the point of view of the investment in the stocks as well as turnover though it is very back as compared to the world's capital market. For this research work, the personal interview and questionnaire are taken as the primary sources. Results and views are given below:

1. **Practicing the right share of Nepalese corporate firms**

Table No. 4.8

Option	No	%
Slightly Agree	36	60
Agree	10	18.33
Neutral	8	13.33
Disagree	6	8.34
Total	60	100

Source: Field Survey, 2011

Out of 60 total responses, 60% of them agree that the Nepalese Corporate Firms agree about the practices of right share issue are in increasing trend to raise the additional capital fund, while 18.33% of them, slightly agree about the practices of right share issue are in increasing trend to raise the capital fund. However 13.33% of them disagree and 8.34% of them are neutral in the context of the practices of right share issue to raise the capital fund.

2. **Reliable and Sufficient information from the company**

Table 4.9

Option	No	%
Yes	25	41.67
No	35	58.33
Total	60	100

Source: Field Survey, 2011

Out of 60 total responses, 41.67% of them say “Yes” about the reliable and sufficient information available from the company to the shareholders/ investors regarding the right share issue, while 58.33% of them say “No” about the reliable and sufficient information available from the company to the shareholders/ investors regarding the right share issue.

3. The awareness of the shareholders about the phenomenon of right share issue

Table 4.10

Option	No	%
Yes	34	56.67
No	26	43.33
Total	60	100

Source: Field Survey, 2011

Out of 60 total responses, 56.67% of them say “Yes” about awareness of the shareholders that they have knowledge of right shares, cause of the issuing right shares, impact of right share issue on their wealth position etc. while 43.33% of them say “NO” about awareness of the shareholders that they have knowledge of right shares, cause of the issuing right shares, impact of right share issue on their wealth position etc.

4. Motivation of issuing right shares

Table 4.11

Option	No.	%
Increase capital	39	65
increase the no. of outstanding shares	6	10
Market price of the stock	15	25
Total	60	100

Source: Field Survey, 2011

Out of 60 total responses, 65% of them give their views on (a) the issuing of right shares to increase capital fund and get more respectable size, while 10% of them give their views on (b) the issuing of right shares to increase the numbers of outstanding shares for promoting the active trading in the stock market and 25% of them give their views on (c) the issuing of right shares to bring out the market price of the stock with in most popular range.

5. Impact of right share on the stock price movement

Table 4.12

Option	No	%
Increase	18	30
Decrease	27	45
Constant	6	10
Don't Know	9	15
Total	60	100

Source: Field Survey, 2011

Out of 60 total responses, 30% of them agree that (a) the stock price should be increased while 45% of them agree that (b) the stock price should be decreased after right share issue. Similarly, 10% of them give their opinion that (c) the stock price remains same before and after right share issue and 15% of them give their opinion that (d) don’t know about the effect of right share issue on the stock price movement.

6. The role of the right offering on the stock price movement

Table 4.13

Option	No	%
Increased	20	33.33
Decreased	23	38.33
Remain constant	10	16.67
Don't Know	7	11.67
Total	60	100

Source: Field Survey, 2011

Out of 60 total responses, 33.33% of them (i.e. 20 responses; 6 from issuing company, 7 from managers & officers of issuing manager and regulatory office and 7 from investors and experts) agree that the stock price should be increased because the right share plays an important role on the stock price movement. While 38.33% of them (i.e.23 responses; 12 from issuing company, 8 from managers & officers of issuing manager and regulatory office and 3 from investors and experts) put their view that the stock price should be decreased because the right share does not play an important role on the stock price movement. Similarly, 16.67% of them (i.e. 10 responses; 4 from issuing company, 3 from managers & officers of issuing manager and regulatory office and 3 from investors and experts) put their view that the stock price should remain constant and right share does not affect the stock price movement and 11.67% of them (i.e. 7 responses; 3 from issuing company, 2 from respondents issue manager and regulatory office and 2 from investors and experts) don't know about the effect of stock price movement by the cause of right share issue.

7. The "Right" that it should be legally transferable

Table 4.13

Option	No	%
Transferable	34	56.67
Not to be transferable	5	8.33
Don't want to say	11	18.33
Don't know	10	16.67
Total	60	100

Source: Field Survey, 2011

Out of 60 total responses, 56.67% of them (i.e.34 responses; 15 from issuing company, 14 from issue manager and regulatory office and 5 from investors and exports) agree that the "right" should be transferable. While 8.33% of them (i.e. 5 responses; 2 from issuing company, 2 from issue manager and regulatory office and 1from investors and exports) give their opinion that right should not be transferable. Similarly, 18.33% of them (i.e.11 responses; 5 from issuing company, 1 from issue manager and regulatory office and 5from investors and exports) give their opinion that they don't want to say about the current laws while 16.67% of them (i.e. 10 responses; 3 from issuing company, 3 from issue manager and regulatory office and 4from investors and exports) give their opinion that they don't know about it.

8. Why right shares of the companies are not fully subscribed

Table 4.14

Option	No	%
Lack of knowledge	40	66.67
Insufficient legal provision	15	25
Insufficient money	5	8.33
Total	60	100

Out of 60 total respondents, 66.67% of them (i.e. 40 respondents) give their view that rights are not fully subscribed because of lack of the knowledge of right shares in investors while 25% of them give their view that rights are not fully subscribed because of the insufficient legal provision. Similarly 8.33% of them say that the investors/ shareholders may have insufficient money.

9. The affects the issuance of the right shares

Table 4.15

Option	No	%
political environment	34	56.67
economic environment	16	26.67
legal provision	10	16.67
Total	60	100

Source: Field Survey, 2011

Out of 60 total respondents, 56.67% of them give their view that political environment affects the issuance of the right shares. While 26.67% of them give their opinion that the economic environment affects the issuance of the right shares. Likewise, 16.67% of them give their opinion that legal provision plays affects the issuance of the right shares.

10. the action that should be taken for maximum subscription of right share

Table 4.16

Option	No	%
A	27	45
B	15	25
C	18	30
Total	60	100

Source: Field Survey, 2011

Out of 60 total respondents, 45% of them agree that the legal provision should be modified for maximum number of subscription of rights whereas 25% of them agree that agree that the company should be promoted in such a way that the investors/shareholders will be ready to subscribe the rights. While 30% of them give their opinion that the investors should be aware about the right shares.

11. That which one they prefer

Out of 60 total respondents, most of them choose the option (a) Subscribed the rights to purchase the new shares and very few of them choose the option (b) sell the right to others. Some of them in less number choose the option (c) partially sell and partially exercise and at last there is nobody who choose the last option (d) do no thing at all, let the right expire.

12. The investing in the right shares is profitable

Out of 60 respondents, most of them put their opinion that the investing in right shares is profitable. Very few of them say that it is non-profitable.

13. Any experiences about the right share issue

Out of total 60 respondents, 60% of them have experience about the right shares, it means, they had invest in the right shares whereas 40% of them have no experience about the right shares at all.

Source: Field Survey, 2011

4.9 Major Findings

From the analysis of data and other information, the findings of the study are as pointed below:

1. Nepalese stock market is dominated by financial sector companies, the participation of the real sector i.e. manufacturing, hotels, etc is quite low or negligible.
2. It is found that the policy of Nepal Government on stock market is not clear, perfect and transparence.
3. It is found that the trading of common stock, right share and very little extent to debenture, preference shares and few mutual funds have taken place. There is no any practice of option, warrants and convertibles.
4. The contribution of Right Share is being the second largest among various issues to raise the capital of the corporation approved by SEBON
5. It is found that the practice of right share issue is in increasing trend per year.
6. The maximum contribution of right offering in total public flotation 58.36% and minimum is 6.81% within the fiscal year 2052/53 to 2066/67.
7. It is found that out of 16 sample companies, all companies' actual market prices are higher than the theoretical price showing positive change. The average percentage change between the actual market price and theoretical price is 33.71%.
8. It is found that there is significance difference between actual market price and theoretical price of the share after right share issue through t-test.

9. Among 16 cases, the majority of the cases i.e. 7 cases, MPS after right share increases and 6 cases are found that MPS after right share decreases. And 3 cases are found that MPS of Alpic Everest Finance Ltd, Annapurna Finance Ltd and Yeti Finance Ltd remain the same after the right share issue showing no effects of right share issue.
10. According to the two tailed t-test, it is found that the right share is not responsible for the stock price movement.
11. Company Act has not mentioned about necessity of legally transferable rights instruments called right, which must be mailed to the stockholders for each stock held before the rights offering.
12. Declaration of inappropriate holders of record date has caused dilution of wealth position of existing shareholders if they do not exercise the rights with in the ex-right date. The theme of Right share issue is to protect the wealth position of the existing shareholders which is not happened because of Declaration of inappropriate holders of record date.
13. Company Act is silent on the topic of the issue of right offering and its transferability.
14. According to the field survey, it is found that the investors are not aware about the right share issue.
15. Regarding procedural aspects of rights offering, all the other procedures are same as IPO. But rights issuing company (Issue Manager) should be mailed a document called a ‘right’ to the existing shareholders.
16. There is common of the under subscription of rights issue as right is not transferable in Nepal. But it is found that rightn shares of t Lumbini Bank Ltd is fully subscribed because it made two rights issue according to annual report of SEBON. And right shares are nearly to be fully subscribed (i.e. 99%) of Pokhara Finance Ltd, Nawadurga Finance Company Ltd, Ace Finance Company Ltd, Kist Merchant Banking and Finance Ltd and Siddhartha Bank Ltd according to annual report of SEBO/N..

17. Promotional role played by the issuing company and issue manager regarding to the rights offering is not sufficient.
18. Seti Cigarette Factory Ltd., Nepal United Co. Ltd., Nepal Bank Ltd. and Necon Air Ltd. are the four companies that have issued rights share and are currently de-listed from NEPSE.
19. At present, most of the banking and financial institutions are issuing rights share to increase their capital base to comply with the policy directive given by NRB.
20. Due to low flotation cost, easy process to collect fund and maintaining control position in management, are also the causes to prefer rights share by Nepalese Corporate firms.

CHAPTER –V

SUMMARY, CONCLUSION AND RECOMMENDATIONS

The last chapter of this study presents the summary, conclusion and recommendation. Summary passes on the form of the whole study. Similarly, conclusion is drawn from the analysis and recommendation is drawn to suggest for the improvement to the activities of right offering which causes the stock price movement.

5.1 Summary

Capital market is the backbone of the national economy. It plays an important role for the development of the industrial sectors. Under the capital market, the stock market has played the crucial role for the proper balance of the country.

In the capital market, the right offering is being popular to raise the additional capital fund for the long-term purpose. In Nepal, the trading of securities started with the establishment of Biratnagar Jute Mill Ltd and Nepal Bank Ltd. in 1937. So the history of Nepalese stock market is not very old. The establishment of Security Exchange Centre Ltd. in 1976 can be taken as the most remarkable event in the history of securities market in Nepal. It was converted into Nepal Stock Exchange Limited (NEPSE) in 1993. The regulatory body was established known as Securities Board of Nepal (SEBON) in 1993, 7^{th} of June under the provision of security exchange act 1983.

In Nepal, the issuing of rights share was started from fiscal year 2052/53 B.S. and the issuing company is Nepal Finance and Saving Company Ltd. It is just being 15 years of the issuing of rights share in Nepal. So it is still a new and emerging concept for both organizations and investors.

In Nepal, the trend of right offering is increasing every year. Right offering have been started from fiscal year 2052/53 by Nepal Finance and Saving Company Limited. In fiscal year 2059/60, there were four cases of right offerings which collect Rs.162.24 million out of the total public flotation, Rs.556.54 millions. Similarly, in fiscal year 2060/61- three cases, 2061/62- six cases, 2062/63- 11 cases and 2063/64-16, cases, 2064/65 – 42 cases, 2065/66 – 50 cases and 2066/67 - 33 cases of right offerings has made. Since 2052/53 to 2066/67 184 cases of right offerings has made.

The main objective of this study is to find out the ole of the right offering in the stock price movement. According to the nature and objective both primary and secondary sources of data are collected from Annual Reports of NEPSE, SEBON related companies. Questionnaires were distributed and interviews were made to collect information which was tabulated and presented as per requirement of the study.

Finally, major findings based on primary as well as secondary data have been presented and following conclusion is drawn.

5.2 Conclusion

It is found that the policy of Nepal Government on stock market is not clear, perfect and transparence. And the trading of common stock, right share and very little extent to debenture, preference shares and few mutual funds have taken place. There is no any practice of option, warrants and convertibles.

The contribution of Right Share is being the second largest among various issues to raise the capital of the corporation approved by SEBON. The maximum contribution of right offering in total public flotation 84.75% and minimum is 6.81% within the fiscal year 2052/53 to 2066/67.

It is found that out of 16 sample companies, all companies' actual market prices are higher than the theoretical price showing positive change. The average percentage change between the actual market price and theoretical price is 33.71%. There is significance difference between actual market price and theoretical price of the share after right share issue through two tailed t-test. According to the two tailed t-test, it is found that the right share is not responsible for the stock price movement.

Among 16 cases, the majority of the cases i.e. 7 cases, MPS after right share increases and 6 cases are found that MPS after right share decreases. And 3 cases are found that MPS of Alpic Everest Finance Ltd, Annapurna Finance Ltd and Yeti Finance Ltd remain the same after the right share issue showing no effects of right share issue.

The result of run test is positive i.e. market price per share before 1 month of right share issue and after right share issue is found to follow randomness in price fluctuation.

Company Act is silent on the topic of the issue of right offering and its transferability. It has not mentioned about necessity of legally transferable rights instruments called right, which must be mailed to the stockholders for each stock held before the rights offering.

Declaration of inappropriate holders of record date has caused dilution of wealth position of existing shareholders if they do not exercise the rights with in the ex-right date. The theme of Right share issue is to protect the wealth position of the existing shareholders which is not happened because of Declaration of inappropriate holders of record date.
There is common of the under subscription of rights issue as right is not transferable in Nepal. But it is found that rights share of Lumbini Bank Ltd is fully subscribed because it made two rights issue according to annual report of SEBON. And right shares are nearly to be fully subscribed (i.e. 99%) of Pokhara Finance Ltd, Nawadurga Finance Company Ltd, Ace Finance

Company Ltd, Kist Merchant Banking and Finance Ltd and Siddhartha Bank Ltd according to annual report of SEBON.

Promotional role played by the issuing company and issue manager regarding to the rights offering is not sufficient. And generally investors are driven to invest on securities whether that may be rights share or the other upon their own interest.

5.3 Recommendation

After analyzing the data obtained from primary as well as secondary sources, the researcher has got various findings. These findings are directly and indirectly related with the rights issue practice, its difficulties and its impact on market price of stock. The researcher has provided some recommendations to concerned personals, authorities and regulatory bodies. The given recommendations, if they are implemented properly, will help us to make rights issue more easy, effective and efficient. On the basis of findings, some recommendations are presented as follows:

1. Company act 2053 is not clear about the rights shares which are not subscribed by the existing shareholders. The current practice is made by distributing the unsubscribed rights shares among the employees of the respective companies and underwriting. So this act should be amended to make position about the issue of rights shares and subsequent allotment of the rights issue.
2. Those rights which were not exercised by the existing shareholders that will be exercised by the employee of the respective company. It is not good practice. If the rights can be transferred that means the unsubscribed rights can be sold by existing shareholders separately to new investors in the securities market, then this activity will help for the full subscription. So the issuing company should think about it and problem of under subscription of rights issue can be reduced simultaneously.

3. In order to attract the investors to invest, the issue prospects should provide some motivates reasons for rights offering.
4. Infrastructure like good communication, banking facilities, postal services and margin trading should be developed to encourage investors for investing in the securities especially right shares.
5. The company should be very careful for the right offering and it should play promotional role for the full subscription of rights share. Because there are so many large number of rights which are not exercised by the existing shareholders. This may happen because of insufficient information, misconception and rumors about rights share. This situation can be minimized by awareness program for general investors, using mass and through program via seminars, training, and workshops..
6. Still a right issue guideline does not come yet. Because of lack of it, there is some problems. So, it must come soon, which is base and key to support the right share issue.
7. The role of market players in the stock market should be made effective in promoting Nepalese capital market by giving proper training and adopting changed environment with modern tools and techniques.
8. Regulatory offices, issues managers, issuing company and government should jointly brought awareness program for the investors to invest on stocks, especially rights share because large no of investors are ignorant about it.
9. In order to improve the right offering's problem, regulation and their implementation should be sound and strict for capital market and its related sectors. Because of lack of implementations of good rules and regulations, there will be no improvement and work.
10. The development of all sectors like capital market, industrial market or other economic market depends upon political stability. So it should be maintained in our country. Then after only our country can be developed.

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www.nepalstock.com

www.nrb.org.com.np

www.sebonp.com

APPENDIX

APPENDIX: 1

Calculation of Ex-right value of the Stock after Right Share Issue

Ex-right value Pe = $\frac{P0\ \# + Ps}{\# + 1}$

Right on price of the stock =P_0

Subscription price =P_s

No. of rights required to purchase a new share of stock.

S. N.	Name of the Companies	P_0	P_s	Ratio	#	P_e
1	PFL	410	100	2:1	2	306.67
2	PEOFL	137	100	1:1	1	118.50
3	AEFL	150	100	2:1	2	133.33
4	NFCL	115	100	2:1	2	110
5	AFCL	448	100	1:1.53	0.6536	237.09
6	ANPFL	500	100	1:1	1	300.50
7	YFL	230	100	4:1	4	204
8	CMBFL	196	100	1:1.2	0.8333	143.54
9	KMBFL	400	100	1:1	1	250
10	LBL	172	100	5:1	5	160
11	LAXBL	520	100	5:1	5	450
12	SBL	546	100	5:1	5	471.67
13	PDBL	103	100	1:1.4	0.7143	101.25
14	BDBL	381	100	1:1	1	240.50
15	CDBL	100	100	1:2	0.5	100
16	NDBL	133	100	1:1	1	116.50

APPENDIX: 2

Questionnaire

Dear respondent,

This Questioner is prepared for my research on "**ROLE OF RIGHT OFFERING ON THE STOCK PRICE MOVEMENT**" which, I am doing for the partial fulfillment for the degree of Master of Business Studies (M.B.S.).I humbly request you to fill at the best knowledge. Your cooperation in this regard will be huge value for me.

I assured that the information collected from you will be exclusively used for the research purpose and will not be published in any media.

I shall be highly obliged for your response as for as possible.

Thank You.

ANJANA ADHIKARI
Researcher
T.U. Registration No.7-1-274-192-98
Campus Roll No. 477/061
Shanker Dev Campus
Putalisadak, Kathmandu.

Name: - Date:-
Organization: - Designation:-
Address: - Occupation:-

Instruction: Please tick [ ] in an appropriate place and put your views in opened ended Question.

1. Do you think that Nepalese corporate firm increasingly practices the right share?

   a) Slightly Agree ( ) c) Neutral ( )

   b) Agree ( ) d) Disagree ( )

2. Do you think that the shareholders get reliable and sufficient information from the company in the context of right share issue?

   a) Yes ( ) b) No ( )

3. Do you think that the shareholders are aware about the phenomenon of right share issue and their successive involvement in it?

   a) Yes ( ) b) No ( )

4. What is the motivation of issuing rights share by the corporate firms?

   a) To increase capital fund and get more respectable size. ( )

   b) To increase the numbers of outstanding shares for promoting the active trading in the stock market ( )

   c) To bring out the market price of the stock with in most popular range. ( )

5. What do you think about the right share issues and its impact on stock price movement?

   a) Should increase ( ) c) Remains constant ( )

   b) Should decrease ( ) d) Don't know ( )

6. What do you think about the role of the right offering on the stock price movement?

   a) The stock price should be increased because the right share plays an important role on the stock price movement ( )

   b) The stock price should be decreased because the right share does not play an important role on the stock price movement. ( )

c) The stock price should remain constant and right share does not affect the stock price movement. ( )

d) Don’t know about the effect of stock price movement by the cause of right share issue. ( )

7. What is your opinion about the “rights” should be legally transferable?

a) Should be transferable ( )

b) Should not be transferable ( )

c) Don’t want to say about the current laws ( )

d) Don't know ( )

8. Why Rights of the companies are not being fully subscribed?

a) Lack of the knowledge of right shares in investors. ( )

b) Insufficient legal provision. ( )

c) The investors/ shareholders may have insufficient money. ( )

9. What is the thing which affects the issuance of the right shares?

a) Political environnent.

b) Economic environnement.

c) Legal provision

10. What is the action that should be taken for maximum subscription of right share?

a) Legal provision should be modified. ( )

b) The company should be promoted to attract the investors/shareholders to subscribe the rights. ( )

c) Investors should be aware about the right shares. ( )

11. In your opinion which of the following options mostly prefer?

A) Subscribe to the new share. ( )

B) Sell the rights. ( )

C) Partially sell and partially exercise. ( )

D) Do nothing at all. ( )

12. In your opinion, is it profitable to invest in rights share?

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13. Do you have any experience about right offering, you want to share with us?

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