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Impact of Subscription on Structure on Short Run Volatility of IPOs in India

AMIT KUMAR SINGH*
SHIVANI KALRA**

Abstract

The listing day returns as well as post listing day returns of an IPO are impacted by a lot of factors such as age of the firm, market adjusted average returns, debt-equity ratio, price-earnings ratio, offer size, etc. The study first analyses the nature of impact of various firm specific and issue specific factors on the short run volatility of the IPO returns using OLS regression technique. One of the most significant factors that play a role in impacting the underpricing of stocks is the total subscription rate of the IPO reflecting its overall demand in the market. In this study; impact of subscription structure has been analysed using individual subscription rate of different categories of investors namely QIBs, NII, and RIIs. The results are indicative of negative relationship of subscription rate of QIBs with the volatility of the stock and positive relationship between subscription rate of NIIs and RIIs and the stock volatility.

I. Introduction

IF THE PRICE of the IPO on the listing day is higher than the price at which it was offered, the IPO is said to be underpriced. And the return offered by a stock on the day it is listed reflects the listing day return. There is enormous literature (Ritter and Welch (2002); Sehgal andSingh (2008); Sehgal and Sinha (2013); Handa and Singh (2017); Anandand Singh (2019))based on the identification of factors affecting the listing day returns of an IPO along with their association with such returns. However, there is dearth of studies whichtake into account the listing as well as post listing period returns of an IPO to study the impact of various factors on them. And out of the factors investigated, a comparatively less researched area is the impact of subscription rate as well as subscription pattern on the volatility of IPO returns.

* Associate Professor, The University of Delhi, Department of Commerce, Delhi School of Economics, University Enclave, Delhi 110007, INDIA
** Research Scholar, The University of Delhi, Department of Commerce, Delhi School of Economics, University Enclave, Delhi 110007, INDIA

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The possible reason for such conclusion is that investors invest more during hot deals (more demanded deals) because they know they would be allotted less than they have asked for. Hence demand does not always end up making the stock volatile. In the second case, instead of taking Total subscription rate as one of the indicators, we took individual subscription rates by Qualified Institutional Buyers, Retail Individual Investors and Non-Institutional Investors along with other variables, to test their association with volatility. The results indicated that subscription rate of qualified buyers is inversely related to volatility which means that if the subscription by qualified buyers is more; there are less chances of volatility in the aftermarket adjusted returns. This is because of their maximum share in allotment ratio of the three categories, often indicative of quality IPOs. The qualified buyers are known to have better knowledge and expertise with respect to investing in stocks, which retail investors lack. As a result, subscription rate by retail (and non institutional investors) is directly related to volatility.

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