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A Study of IPO Performance in India: Influences of Market Trends, Regulatory Frameworks, and Investor's Sentiment

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Abstract

This research explores the underperformance of Initial Public Offerings (IPOs) in the Indian market, with a focus on the influence of regulatory policies, market conditions, and company-specific factors. IPO underpricing, where a stock's listing price is significantly lower than its market value, is a common trend that can lead to poor long-term returns, especially for retail investors. The study investigates how variables such as issue price, number of pre IPO shareholders, subscription rate, NSE market performance, and policy impact affect IPO outcomes across different time periods-1 day, 1 week, and 1 year post-listing. Using data from 30 Indian IPOs between 2017 and 2021, a multiple linear regression model was applied to identify patterns and correlations. The findings reveal that higher issue prices generally lead to lower underpricing in the short term, making pricing decisions a key factor in IPO success. Market trends (NSE changes) significantly affect long-term IPO performance. Policy-related factors showed a mostly negative but indirect impact, indicating that while regulations aim to protect investors, they may also affect the ease and success of public listings. This study highlights the importance of proper pricing, market timing, and regulatory balance in IPO planning. The results are useful for companies planning to go public, policymakers aiming to strengthen investor confidence, and researchers exploring IPO behavior in emerging markets like India.

Keywords: IPO, Under-pricing, NSE, Issue Price Subscription Rate, Shareholders.

1. Introduction

An Initial Public Offering (IPO) is when a private company sells its shares to the public for the first time. This helps the company raise a large amount of money without taking loans. IPOs are important for companies that want to grow, expand into new markets, develop technology, or improve their reputation. In India, which is a growing economy, IPOs are especially important. They help use domestic savings wisely, attract foreign investors, and support Indian industries. For startups in sectors like technology, pharma, and renewable energy, IPOs are often the best way to get funding because loans and venture capital are hard to get. However, IPOs also come with challenges. Many IPOs in India fail to perform well after listing. This is known as IPO underperformance, where the stock price falls below the offer price after a few weeks or months. This affects investor confidence, reduces trust in the market, and discourages other companies from launching IPOs. Several reasons cause underperformance-such as wrong pricing, weak market conditions, lack of trust in management, or too many rules. In India, the role of government policies and market regulations is especially important. SEBI (the stock market regulator) has made strict rules to protect investors and improve transparency, but sometimes these rules also increase costs and reduce flexibility for companies. This study focuses on these problems and tries to find out how regulatory and market factors affect IPO success or failure in the Indian market.

2. Objectives of the Study

This Research has the Following Objectives

i) Analyse how various factors influence IPO underpricing in the Indian market
ii) Examine the relationship between IPO underpricing and market volatility, focusing on short-term (1 day, 1 week) and long-term (1 year) performance

iii) Identifying the role of regulatory and governmental factors in IPO under-pricing in India
iv) Assessing multiple linear regression models for explaining the phenomenon of IPO under-pricing in various time intervals.

3. Review of Literature

Many researchers have studied IPO performance and underpricing in different countries, including India. This section highlights the important findings from previous studies.

Benveniste and Spindt (1989) explained the book-building process, where investment banks gather feedback from investors to set the IPO price. This method helps in better price discovery and reduces the gap between actual and expected value.

Amihud and Mendelson (1986) studied market liquidity and found that when a stock is hard to buy or sell, investors demand higher returns, which leads to underpricing. So, liquidity plays a big role in IPO pricing. Corporate governance also matters.

Studies by Alkaabin and Mostafa (2013) show that companies with good governance (like transparency and proper management) face less underpricing. Strong governance gives confidence to investors.

Jain and Kini (2008) observed that after going public, many companies face difficulties in managing growth effectively. Although sales may rise, profits and performance may suffer.

Media coverage also plays a role. Cook *et al*. (2006) found that more media attention usually increases investor interest and early returns. But hype can lead to overvaluation and later poor performance.

Baker and Wurgler (2007) discussed investor behaviour, like herd mentality and overconfidence, which can cause IPOs to be over or underpriced. In India, SEBI regulations play a huge role. La Porta *et al*. (2006) found that while regulations help protect investors, too many rules can increase IPO costs. Deb and Marisetty (2010) suggested finding a balance between regulation and market freedom.

Overall, these studies show that IPO pricing and performance are influenced by market conditions, company factors, investor psychology, media, and government policies.

4. Methodology

The first aim was to examine the behaviour of underpricing of the IPOs under various time horizons. In this case we can use multiple linear regression analysis because it enables one to estimate the relationship between Underpricing at one day, one week and one year on one side while on the other side we have multiple independent variables. The other independent variables are issue price, number of pre-IPO shareholders, subscription rate, policy impact, and NSE percentage change on the issue date, after 1 week and 1 year. Because of high multicollinearity the variables of debt to equity ratio is excluded from the regression equation. Multiple linear regression is applied to estimate the direct effect of these variables on underpricing, but at the same time, controls for the effects of the other variables included in the model. Multiple linear regression is used because underpricing cannot be explained by one factor but by several factors and with several predictor variables hence insuring a reliable and accurate analysis of the determinants of IPO underpricing.

5. Analysis & Interpretation

Based on the objectives of the study the analysis has been done in which the antecedents of IPO underperformance and failures in the context of the Indian market with particular reference to regulatory factors and market forces. This has helped the analysis to uncover a number of factors about the nature and interconnectedness of different macroeconomic, firm-specific, and market-related factors of IPO performance. This study has also focused on the issue price, subscription rate, the number of shareholders, and the scenarios which have deliberately or inadvertently affected the success and failure of IPOs in India through paying attention to the impact of government policies. The information derived from these results will be useful for not only theoreticians but also legislators, supervisory authorities, and potential future IPOs.

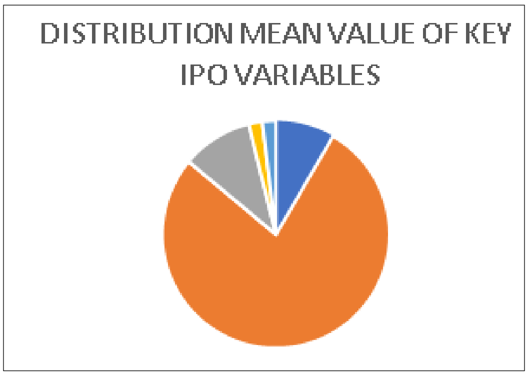

Fig 5.1: Variables Group

Figure 5.1 shows the proportion of mean values of key IPO variables such as Issue Price (IP), Number of Shareholders (NS), Debt- to-Equity Ratio (DE), Subscription Rate (SR), and Policy Impact (PI).

The highest proportion comes from the number of shareholders.

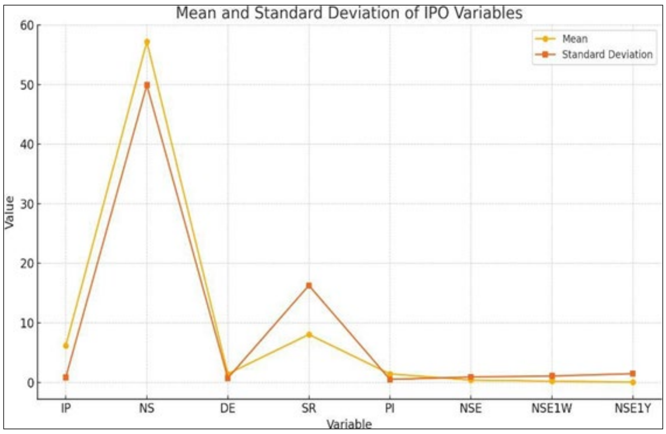

Fig 5.2: Variables Group

Figure 5.2 shows graph compares the mean and standard deviation of each variable. It clearly shows that:

i) NS (Number of Shareholders) has the highest variability.
ii) SR (Subscription Rate) also shows wide spread due to market demand differences.
iii) Market performance values like NSE, NSE1W, and NSE1Y have lower means but larger standard deviations, indicating volatility.

One of the main findings is about issue price. It was seen that IPOs with higher issue prices had lower chances of underpricing. This means when a company sells its shares at a higher price, the difference between the IPO price and the market price on the first day is smaller. So, higher priced IPOs tend to perform better in the short term (1 day or 1 week after listing).
Next, it was found that IPOs that followed a fixed price system showed less underpricing. The fixed price method seems to offer more stability. A test called the Likelihood Ratio Test was used to confirm this result, and it showed strong evidence with a p-value of 0.05 or lower, meaning the result is reliable.
When looking at the long-term performance (after 1 year), the study found that there is a positive relationship with NSE performance. If the NSE index rises, IPOs launched during that period are more likely to perform better over time. This shows that market conditions affect IPO returns in the long run.

6. Findings of the Study

The empirical analysis of IPOs in the Indian market between 2017 and 2021 yielded several notable findings regarding the factors influencing underpricing across various time horizons-specifically, 1 day, 1 week, and 1 year post-listing.

1. Issue Price and Under-pricing

One of the most consistent and statistically significant findings across both short-term models (1-day and 1-week) was the negative correlation between the issue price and IPO underpricing. IPOs with higher issue prices tended to experience less underpricing. This suggests that well-valued IPOs, particularly those using fixed price methods, are less likely to leave excess gains on the table for early investors, reducing volatility and investor speculation. This finding supports the hypothesis that pricing strategy is a pivotal determinant of short-term IPO performance.

2. Subscription Rate

Contrary to common assumptions, the subscription rate showed a minimal and statistically insignificant effect on underpricing across all time frames. While high subscription rates are typically interpreted as indicators of strong investor demand, this study suggests that subscription enthusiasm does not reliably translate into better post-listing returns. It indicates that market sentiment, investor psychology, and broader market factors might overshadow mere subscription volume.

3. Number of Shareholders(Pre-IPO)

The number of pre-IPO shareholders exhibited a positive but statistically weak relationship with underpricing, particularly in the long term. Though not strongly significant, this trend implies that firms with a broader shareholder base prior to going public may experience slightly improved long-term price stability, possibly due to more diversified investor confidence and institutional backing.

4. Policy and Regulatory Impact

The variable reflecting policy impact, which included significant events like the introduction of GST (2017) and the corporate tax reduction (2019), showed a negative but statistically insignificant relationship with IPO underpricing. While regulatory frameworks are designed to promote transparency and protect investors, they may indirectly deter IPO performance by increasing compliance burdens and limiting operational flexibility for firms. These findings align with prior studies that recommend a balanced approach to regulation that fosters investor trust without stifling market efficiency.

5. NSE Market Performance (NSE,NSE1W,NSE1Y):

The NSE index performance showed minimal impact in the short-term (1 day and 1 week) underpricing models. However, a positive and statistically notable correlation emerged in the 1- year model, suggesting that market timing plays a crucial role in long-term IPO success. IPOs launched during bullish periods were more likely to yield positive long-term returns. This confirms the need for companies to strategically time their market entries.

6. Regression and Robustness Results

Multiple linear regression models confirmed these trends with R^2 values ranging from 0.18 to 0.21, indicating a moderate explanatory power. Variance Inflation Factor (VIF) values were all below 5, and Durbin-Watson statistics were close to 2, confirming the absence of multicollinearity and autocorrelation, respectively. These results affirm the robustness and reliability of the regression models used.

Conclusion

This research studied the reasons behind IPO underperformance in India. It focused on how market trends, company-related factors, and government policies affect IPO results. The main finding was that higher issue prices usually result in lower underpricing, especially in the short term (1 day after listing). This means that setting the right price is very important. A well-priced IPO can raise good money for the company and give investors a fair return. The number of shareholders before the IPO showed a small positive effect on long-term performance. More shareholders may bring stability and trust, but the impact was not very strong. Surprisingly, subscription rate (how much people apply for the IPO) did not strongly influence performance. This shows that market mood and other outside factors may be more important than just demand during IPO. Government policy impact was mostly negative but not significant. This means rules and regulations may influence IPOs indirectly by affecting investor trust or company costs. Flexible and transparent rules could help reduce underpricing. There was also a positive link between NSE performance and long- term IPO success. This means market conditions at the time of IPO matter a lot. IPOs done during strong markets perform better over time. This study helps companies, investors, and policymakers understand how to improve IPO planning and reduce risks. Firms should choose the right timing, pricing, and prepare well for listing. Policymakers should make IPO rules supportive but not too strict.

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