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An Analysis of Capital Issues in Indian Primary Market

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Abstract

The industrial securities market in India consists of new issue market and stock exchanges. New Issue Market facilitates transfer of resources from savers to the users and transferring them to productive purposes, which is an important requisite of economic growth. There are various methods used in the floatation of securities in the new issue market. They are public issues, offer for sale, private placement and rights issues. It has been observed that the reforms in the stock market were aimed at enhancing the efficiency, safety, integrity and transparency of the primary market. The efficiency of the market has improved through faster execution of trades. Investments in equity can be initially started at a smaller level and progressively increased by the investors as they get the experience and confidence. The primary stock market in India has shown its strength and maturity and it is comparable with any stock market in the developed countries. The investors' protection measures taken by SEBI are excellent as also the standards of corporate governance. All these make the primary market an attractive avenue for investment opportunity. The present paper focused on to analyze the resource mobilization pattern of primary market in India.

Introduction

The Indian securities market has witnessed major transformation and structural changes since 1992 as the result of ongoing economic reforms initiated by the Government of India in the wake of Liberalization, Privatization and Globalization (LPG). These reforms aimed at improving market efficiency, enhancing transparency, checking unfair trade practices and bringing the Indian capital market upto international standards. The reforms have brought about changes in the institutional character of the market, regulatory environment in which it functions and investors' profile and technology of the market. Several changes have also taken place in the operation of secondary markets such as automated on-line trading on stock exchanges, enabling trading terminals of NSE and BSE to be available across the country, reduction in the settlement period, opening of stock markets to Foreign Institutional Investors, etc.

Since the early 1990's, there has been a paradigm shift from merit based, regulated regime to disclosure based regime. Comprehensive guidelines on disclosures and investor protection are issued and amended by SEBI from time to time.

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The companies accessing the capital market through public issues have to comply with adequate disclosure norms on initial as well as on a continuous basis. India's disclosure norms are considered to be one of the best in the world and they are often cited as benchmark for global standards. Moreover, Indian accounting standards are principle- based and aligned to international accounting standards. In terms of consolation, segmental reporting, deferred tax accounting and related party transactions, the gap between India and the US is minimal. In addition to sound accounting standards, the issues relating to corporate governance have been pursued in right earnest consistent with the best international practices. In a deregulated regime, the pricing of public issues is being determined by the market, i.e either by the issuer through fixed price or by the investors through book- building process. A fair system of proportionate allotment of shares has been put in place. The foreign institutional investors have been allowed to invest in primary issues within the sectoral limits set by the Government.

An Initial Public Offering (IPO) occurs when a security is sold to the general public for the first time. If a company prospers and needs additional equity capital, at some point the firm generally finds it desirable to "go public" by selling stock to a large number of diversified investors. Once the stock is publicly traded, this enhanced liquidity (IPO) allows the company to raise capital on more favorable terms than if it had to compensate investors for the lack of liquidity associated with a privately-held company. Firms going public, especially young growth firms, face a market that is subject to sharp swings in valuations. The fact that the issuing firm is subject to the whims of the market makes the IPO processes a high-stress period for entrepreneurs. Because initial public offerings involve the sale of securities in closely held firms in which some of the existing shareholders may possess non-public information, some of the classic problems caused by asymmetric information may be present. In addition to the adverse selection problems that can arise when firms have a choice of when and if to go public, a further problem is that the underlying value of the firm is affected by the actions that the managers undertake. This moral hazard problem must also be dealt with by the market. The industrial securities market in India have in recent years, undergone significant changes keeping pace with the changing need of market participants. They facilitate the reallocation of savings from savers to entrepreneurs.

Various institutions/ intermediaries associated with primary as well as secondary markets such as merchant bankers/ registrars to issues, portfolio mangers, underwriters, bankers to issues, stock exchanges, brokers and sub- brokers, share transfer agents, depositories, FIIs, custodians, credit rating agencies, venture capital funds, collective investment schemes including mutual funds have to register with SEBI and function within the guidelines issued from time to time. SEBI also promotes self- regulatory organizations.

Reasons for Going Public

The companies opt for the IPO to raise funds to financ capital expenditure programs like expansion, diversificatio modernization, etc, financing of increased working capit requirements, and financing acquisitions like a manufacturin unit, brand acquisitions, tender offers for shares of anoth firm.

Advantages of Going Public

1. Initial Public Offerings facilitate the future fundin by means of subsequent public offerings;
2. It provides liquidity to existing shares and increase the visibility and reputation of the company; and
3. Enables the company to offer its shares as purchas consideration or as an exchange for the shares another company.

Disadvantages of Going Public

1. Dilution of ownership stake makes the compan potentially vulnerable to future takeovers;
2. IPO involves substantial expenses ranging betwee 4% to 15% of the size of the issue;
3. The companies going for IPO need to mak continuous disclosures and increased regulator monitoring; and
4. Listing fees and documentation for public issue an cost of maintaining investor relations is high.

Structure of the New Issue Market (NIM)

While New Issue Market, as a channel for corporat investments, has grown over the years, the pattern of growth o the NIM varies through the various phases of its growth, i terms of both financial instruments and channels of marketin used by private corporate firms. The choice of NIM as a instrument was substantially influenced by economi conditions and policy changes. Equity and debentures wer the two main instruments issued through NIM because thes instruments show a growing degree of complementarity ove the years. Equity issues showed a consistent trend i correspondence with the growth in NIM. The intermediatio phase witnessed a greater reliance on equities than o debentures, pointing to the influence of the intermediatio activities by banks and FIIs.

Objectives of the Study

The main objective of the study is to analyze the resourc mobilization pattern of primary market in India. The broa objectives can be grouped in the following manner.

a) To analyze mobilized resources component- wise t highlight the domination of each component in th total resources from year to year, and
b) To study the sector wise and region wise distributio of capital mobilized.

Period of the Study

The study covers the period from 1995-96 to 2005-06.

Development of Primary Market in India

Table 1 brings out aggregate pattern of capital issues in India from 1995-96 to 2005-06. The total number of public issues over a period of eleven years stood at 3,337 with an average of 303.36 issues and the value of public issues was Rs.1, 49, 685 corers with an average of Rs.13, 607, 73 cores per annum. It is clearly understood from the table that the companies have raised an amount of Rs.13, 607, 73 cores every year from the public. The number of issues was highest in 1995-96 with 1725 issues. The year 2002-03 accounted for the lowest number at 26 issues. The year 2004-05 recorded Rs.28, 256 cores from the public claiming the highest amount of capital raised during the study period. The number of issues were in fluctuation during the period from 1995-96 to 1998-99 and from 2000-01 to 2002-03 and later it continuously increased year after year.

Table 1
Aggregate Pattern of Capital Issues in India

Years	No of Issues	Amount (Rs.crore)
1995-96	1725	20804
1996-97	882	14276
1997-98	111	4570
1998-99	58	5587
1999-00	93	7817
2000-01	151	6108
2001-02	35	7543
2002-03	26	4070
2003-04	57	23272
2004-05	60	28256
2005-06	139	27382
Total	3337	149685

Source: www.sebi.gov.in

Table 2 represents the components of capital issues in order to bring out type of securities that are predominately popular in the total capital issues in India from 1995-96 to 2005-06. Further, it is also aimed to highlight whether a particular type of issue of securities was continuously popular during the study period or there was any change in this pattern. The total capital issues are being grouped into equity and debt. For the past few years i.e. from 1997-98 to 2002-03, debentures have been predominant in the public issues.

However, since 2003-04 there has been a reversal in this trend. The share of debt in resource mobilization through public issues was only 16.1 % in 2004-05.

The year 2005-06 has seen a striking phenomenon of complete elimination of the share of debt in resource mobilization through public issue. The amount raised through equity issues has been the highest ever in the history, so far, of the Indian capital market accounting for 100 % of resource mobilisation.

Table 2
Resource Mobilized Through Debt and Equity

Year	Percentage Share	
	Equity	Debt
1995-96	72.39	27.61
1996-97	55.99	44.01
1997-98	41.17	58.83
1998-99	15.34	84.66
1999-00	58.41	41.59
2000-01	52.79	47.21
2001-02	16.88	83.12
2002-03	18.00	82.00
2003-04	80.47	19.53
2004-05	83.96	16.04
2005-06	100.00	0.00

Source: www.sebi.gov.in

The ownership pattern of capital issues is exhibited in Table 3. The ownership pattern of capital issues is classified into two categories viz. government sector and private sector. It is further classified into four regions- north, south, east and west. The Table clearly indicates that number of public issues by public sector was high during the years 1996-97 and 2003-04 when compared to rest of the study period. It is evident from the data of the table that out of the total number of 139 public issues with a value of Rs.27,382 crores in the year 2005-06, private sector contributed with 131 issues for a value of Rs.20,199 crores, whereas the public sector accounted for only 8 number of issues with Rs.7,183 crores of capital. The ownership pattern of capital issues clearly indicates that during the study period, the maximum number of public issues of 680 issues was recorded in 1995-96 while 56 issues were recorded in 2005-06. It is interesting to note that the portion of capital from public issues increased from Rs.10,811 crores in 1995-96 to Rs.14,963 crores in 2005-06. Southern Region contributed a total number of 40 issues, representing a value of Rs.5,535 crores, next to Western Region. According to the public issues wise comparison, Western Region took the first place, Northern, Southern and Eastern Region obtained second, third and forth place respectively during the study period. The overall analysis explains that private sector were dominant in number and amount of capital issued from 1995-96 to 2005-06. In respect of region wise comparison, Western Region dominated the study period.

The amount of capital issue relating to industry wise classification is presented in Table 4. For the purpose of analysis, the total number and the amount of capital issues are classified into banking, cement and construction, finance, chemical, information technology etc. The IT sector accounted for 22 to 89 number of capital issues from 1993-94 to 2000-01. It is important that IT sector has come out with a large number of public issues. The number of issues in the finance sector accounted for 113 issues in 1993-94 to 527 issues in 1995-96. There were no issues during the period 2000-01 to 2002-03 in

Table 3
Ownership Pattern of Capital Issues

(Rs. crore)

Year	Sector-wise				Total		Region -Wise							
	Private*		Public				Northern		Eastern		Western		Southern	
	No.	Amount	No.	Amount	No	Amount	No	Amount	No	Amount	No	Amount	No	Amount
1995-96	1718	16639	7	4165	1725	20804	467	5109	168	1416	680	10811	410	3467
1996-97	872	10241	10	4035	882	14276	221	3381	114	767	360	9041	187	1087
1997-98	105	3852	6	718	111	4570	18	302	26	1164	46	2391	21	713
1998-99	57	5516	1	70	58	5587	10	171	10	266	29	4856	9	293
1999-00	91	7617	2	200	93	7817	13	1900	7	106	46	5235	27	577
2000-01	148	5893	3	215	151	6108	10	207	9	240	43	4105	89	1555
2001-02	30	6601	5	942	35	7543	3	1002	2	180	23	5942	7	419
2002-03	18	1897	8	2173	26	4070	1	78	3	117	13	3358	9	588
2003-04	39	4612	18	18660	57	23272	15	14576	7	636	21	6782	14	1234
2004-05	55	17162	5	11094	60	28256	8	8725	7	204	34	17951	11	1377
2005-06	131	20199	8	7183	139	27382	30	5389	13	1495	56	14963	40	5535

NA: Not Available.
Source: www.sebi.gov.in
** Joint sector issues, if any, have been clubbed with private sector for the respective period.*

industries like food processing, paper & pulp and power sectors. It is understood from the analysis that the post economic reforms period was dominated by banking and financial institutions with the highest amount of capital issues. The banking and FIIs mobilized significantly greater proportion of funds of the total capital issues. This may be on account of the reforms triggered by the Narshimham Committee recommendations introduced in banking sector. Further, many banks came out with mega public issues and launched variety of innovative schemes of mutual funds in order to mobilize resources from the primary capital market.

Table 4
Industry Wise Classification of Capital

(Rs.crore)

Industry	1995-96		1997-98		1998-99		1999-00		2000-01		2001-02		2002-03		2003-04		2004-05		2005-06	
	No	Amount	No	Amount	No	Amount	No	Amount	No	Amount	No	Amount	No	Amount	No	Amount	No	Amount	No	Amount
Banking/FIs	17	6118	8	2242	15	4738	15	4039	13	3139	14	5142	13	3443	11	5428	12	11311	12	12439
Cement& Construction	NA	NA	5	22	4	199	3	337	2	82	2	27	1	30	1	8	2	169	11	1020
Chemical	101	1129	7	226	2	37	4	181	5	32	3	187	1	16	7	522	4	128	2	128
Electronics	NA	NA	3	62	4	204	3	213	4	69	0	0	0	0	4	238	2	61	2	54
Engineering	NA	NA	7	108	6	27	2	10	2	23	4	760	2	10	1	993	3	133	6	1124
Entrainment	*	*	*	*	*	*	2	129	13	458	0	0	2	24	2	153	3	154	7	710
Finance	527	2562	22	74	8	75	3	124	10	440	1	33	1	30	2	71	3	116	7	824
Food processing	135	1339	4	85	2	21	3	71	0	0	0	0	0	0	1	8	6	317	9	427
Health Care	NA	NA	6	28	0	0	7	575	4	48	0	0	2	74	1	329	2	109	10	651
Information Technology	NA	NA	1	9	5	47	36	1547	89	804	6	38	3	227	9	804	5	5095	15	902
Paper & Pulp	NA	NA	3	16	0	0	1	14	0	0	0	0	0	0	9	0	1	60	4	182
Plastic	NA	NA	1	12	0	0	1	7	1	4	0	0	1	218	0	0	0	0	0	0
Power	NA	NA	0	0	1	13	1	15	0	0	0	0	0	0	0	0	2	5854	6	2164
Printing	*	*	*	*	*	*	*	*	*	*	0	0	0	0	0	0	1	130	1	43
Telecom	NA	NA	1	5	0	0	1	75	2	922	1	834	0	0	0	0	2	25	0	0
Textile	159	1118	12	418	4	122	4	68	0	0	2	126	0	0	4	61	0	0	13	771
Others	104	1680	31	763	4	105	7	387	5	4	2	397	0	0	14	14954	12	4595	34	5944
Total	1043	13945	111	4570	58	5586	93	7817	151	6108	35	7543	26	4070	57	23272	60	28256	139	27382

Source: www.sebi.gov.in
Data pertaining to above variables may have been clubbed into the 'others' category.
**NA: Not Available.*

Size wise classification of capital raised from the primary market from 1993- 94 to 2003-04 is presented in Table 5. For this purpose of analysis, the total capital issues are grouped into the following sizes.

i) Below Rs. 5 crores,
ii) Rs.5 Crores- Rs.10 crores
iii) Rs.10 crores- Rs.50 crores
iv) Rs. 50 crores- Rs. 100 crores
v) Rs. 100 crores and above

The average number of capital issues during the study period were 50.41 % in the size group below Rs. 5 crores, followed by the size group of Rs. 100 crores (2.42 %) in the year 1994- 95. The mega size capital issues moved between 2.42 % to 43.86 % from 1994-95 to 2003-04 with fluctuations. The capital issue size group of Rs. 50 crores- Rs.100 crores moved from 3.01 % in 1994-95 to 8.77 % in 2003-04. However the capital issue size group of below Rs. 5 crores have attributed for maximum number over the period under review. In respect of the capital issue size of Rs. 10 crores- Rs.50 crores, it decreased from Rs. 6356 crores in 1994-95 to Rs 199 crores in 2001-02. The capital issue size group below 5 crores claimed highest number, though its share in total amount of capital issues was very insignificant and moved between Rs 2569 crores in 1994-95 to Rs. 16 crores in the year 2003-04. The size group above 100 crores mobilized Rs. 12090 crores in 1994-95 to Rs. 22539 crores in 2003-04 from the primary market.

Findings of the Study

The following are the findings on the basis of analysis of the study.

1. The number of capital issues and volume of issue companies increased from the year 2003-04.
2. Debentures played a dominant role in the public issues in the years 1998-99 and 2001-03.
3. In the year 2005-06, Indian capital market completely eliminated the share of debt in mobilization through public issue.
4. Private sectors dominated the public issues in respect of number of issues and amount of capital.
5. Western region dominated in the capital mobilization among four regions of the country.
6. Banking, Finance and IT industries raised the highest amount of capital during the study period.
7. The lowest number of public issues was recorded in Plastic, Printing and Telecommunication industries.
8. The capital issue size group below Rs.5 crores attained minimum number over the study period.
9. The capital issue size group Rs.100 crores and above claimed highest number and volume of capital issues during the study period.

Table 5
Size- wise Classification of Capital Raised

(Rs. crore)

Year	Total		<5 cr.		> 5cr.- <10cr.		> 10cr.- <50cr.		>50cr.- <100cr.		>100cr.	
	No	Amount	No	Amount	No	Amount	No	Amount	No	Amount	No	Amount
1995-96	1725	20804	1066	3183	418	2833	175	3344	43	2934	23	8511
1996-97	882	14276	547	1760	215	1473	87	1671	14	908	19	8465
1997-98	111	4570	52	122	26	177	15	368	6	420	12	3484
1998-99	58	5587	15	35	9	63	14	297	9	581	11	4611
1999-00	93	7817	19	53	15	105	26	629	14	997	19	6034
200-01	151	6108	66	186	25	165	34	764	8	507	18	4486
2001-02	35	7543	3	7	3	20	8	199	3	177	18	7140
2002-03	26	4070	2	6	1	8	10	255	0	0	13	3801
2003-04	57	23272	6	16	5	36	16	330	5	351	25	22539
2004-05	60	28256	2	3	5	44	17	461	11	723	25	27025
2005-06	139	27382	6	20	4	32	47	1325	33	2189	49	23815

Source: www.sebi.gov.in
NA: Not Available

Suggestions of the Study

On the basis of the findings of the study, important suggestions are put forwarded for consideration.

1. The investors should approach the primary market with a medium to long- term perspective. It should not be looked upon by investors as a means to reap windfall profit or quick returns.
2. The investors should do their homework and evaluate the IPOs based on company's fundamentals, quality of management etc, before grabbing every IPO with the same fervor.
3. The IPO companies should come up with effective price mechanism like Green Shoe Option (GSO), in order to control underpricing in IPO issues.
4. The companies with good image of disclosures alone should be allowed to issue the IPO.
5. The aggressive pricing strategy based on the temporary stock market buoyancy should be discouraged and SEBI should evolve some measures to discourage this practice.
6. Investor education is the need of the hour. Regional exchanges, stock brokers, investor associations etc should provide services to the investors like informed advice to investors on evaluation, selection of IPOs, distribution of forms, etc.
7. The SEBI should establish separate system to monitor the post listing performance of a company.
8. The price rigging before issue of securities should be strictly controlled.
9. Prompt action should be taken against companies which are involved in complaints.
10. The SEBI should ensure the confidence of new investors in the primary market in order to encourage more companies to enter into the IPO.
11. In order to help the investors, SEBI should maintain proper information about post listing activities and it should be made available at the stock exchanges.

Conclusion

From the above discussion, it is clear that the reforms in the stock market were aimed at enhancing the efficiency, safety, integrity and transparency of the primary market. The efficiency of the market has improved through faster execution of trades. Investments in equity can be initially started at a smaller level and progressively increased by the investors as they get the experience and confidence. The primary stock market in India has shown its strength and maturity and it is comparable with any stock market in the developed countries. The investors' protection measures taken by SEBI are excellent as also the standards of corporate governance. All these make the primary market an attractive avenue for investment opportunity.

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