INITIAL PUBLIC OFFERING UNDERPRICING PERFORMANCE IN MALAYSIA (LISTED ON MAIN MARKET)

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ABSTRACT: The purpose of this paper is to investigate the degrees of initial public offering (IPOs) underpricing in Malaysia (listed on Main Market of Bursa Malaysia). Based on 46 IPOs data collected from 2012 until 2015 in Bursa Malaysia, the degree of IPOs underpricing was calculated and factors of IPOs underpricing was determinants. A sample of 46 IPOs listed on main market (new listing) of Bursa Malaysia from 2012 until 2015 was used. The effect of determinants factors were examined in this study is issues price, offer size, and types of industries into degrees of IPOs underpricing. The preliminary results indicate that over the study period, the initial returns of Malaysian IPOs have positive returns. The results of this study found that high underpricing in the initial trading is not determined poor performance. This study only take part in IPO companies that listed in main market from 2012 until 2015 (new listing). This study provides the general insight for investors regarding IPOs performance.

Keywords: Initial Public Offering, Underpricing

1. INTRODUCTION

The Malaysian Stock Exchange (MSE) was incorporated on 14 December 1976. It has two types of markets which are the main market and the ACE market. The main market was established for companies with a profitable track record for three to five full financial years. ACE was established for high growth and technology companies in order to raise capital. The Securities Commission (SC) of Malaysia was established on March 1, 1993. The SC is a self-funding statutory body with focus on capital market regulation in Malaysia. The roles of the SC are to regulate, supervise and systematically develop Malaysia's capital market. In January 1996, the SC liberalized a new method of IPO shares issue on the Malaysian market that is based on a market-based pricing mechanism. The market-based pricing mechanism gave responsibilities to issuers and advisers for setting or making decisions regarding IPO price. Final approval from the SC is still required to ensure appropriateness (How et al., 2007; Abdul Rahim and Yong, 2010).

In Malaysia, companies are listed either on the Main Board or the Second Board of the KLSE, and are classified into range of diverse sectors reflecting their core businesses. Firms in Malaysia employ the fixed price method to go public whereby investors will specify the numbers of shares to which they wish to subscribe at the pre-announced subscription price. Following the close of applications for each issue, company board member and representative from the Malaysian Industrial Development Finance Consultancy and Corporate Services (MIDFCCS) and the SC meet to agree the basis for allotting the shares.

Studies of Asian IPOs (initial public offerings), including Malaysian IPOs, have documented that the levels of underpricing of Asian IPOs are significantly higher than those of more developed economies. Explanations regarding IPO underpricing are numerous and range from an asymmetric information hypothesis to a somewhat mixed behavioural theory (Loughran & Ritter, 2002). IPOs offer a unique situation of information asymmetry surrounding market value between IPO issuers and potential buyers. To overcome the problem associated with information asymmetries and adverse selection problems, IPO firms seek ways to signal the quality of their firms to potential investors.

Selling shares to the general public is an important process for companies to raise capital for the expansion of business. The first instance for a company to sell its shares to the general public on a stock exchange is known as an Initial Public Offering (IPO). Underpricing refers to the initial return that an investor earns if he buys shares of the IPO at the offer price and sells it at the end of the listing day at the market price. It is also refer to the significance increase of the IPO market price over the first few days after the initial listing. According to Murugesu and Santhapparaj (2009), underpricing refers to the situation where a private company seeking to list its shares on stock exchange at a discount price relative to its true value. This situation makes investors earn a negative return if they were to immediately sell their shares once trading commences.

IPO underpricing is a common phenomenon for stock markets around the world. Initial Public Offerings (IPOs) underpricing is an interesting research area that has major attention by academic scholars or researchers. Most of international studies found the existing of underpricing during initial trading at stock exchange (Boulton, et.al, 2011; 2012; Nguema and Sentis 2006). This phenomenon was generated negative return and worse perception into IPOs companies' performance. They had examined 10783 IPOs form 37 country and found that IPOs underpricing is depend on the corporate government in each countries. IPOs underpricing was depend into quality earnings information in each countries. Boulton, et. al. (2012) in the current research founded that the country-level institutional quality is positively correlated with the underpricing of IPOs. Ariff, et. al. (2007) investigates IPOs underpricing in United Kingdom, Singapore and Malaysia found that the IPOs underpricing are strongly related with government-linked companies (GLC). Dawson, (1987) examined IPO in three Asian country found the existing of underpricing during the initial trading. Summarizing the findings of various studies, that was focus on IPOs underpricing in a single country. (e.g. Agathee, et. al., 2012; Islam, et. al.,2010) confirmed the existing of underpricing during the initial trading at stock exchange. However, what determined factor that was influenced IPOs underpricing were varies in each countries and still a largely unexplored question. These underpricing phenomenon's are difficult to understand because various issues were related such as companies' performance, government policy and others issues.

This paper was to examine the degree of IPOs underpricing for the first day trading at MSE (listed in main market). This study provides the general insight for investors regarding IPOs performance and which IPOs shares were generated high returns. As the investors, they need information to evaluate future IPOs performance in order to decide whether to buy or sell that share.

This study is organized in the following manner. Section 2 is a discussion of important and relevant literature on this area while Section 3 outlines the study methodology. Section 4 discusses the results and highlights the findings while Section 5 provides conclusion and implication of the study.

2. LITERATURE REVIEW

2.1 Overview of IPO process in Malaysia

In Malaysia, the statutory body that was responsibility with investment and new listing companies at stock exchange is known as Malaysian Stock Exchange (MSE). Before changes the name on 14 April 2004, stock exchange in Malaysia is known as Kuala Lumpur Stock Exchange (KLSE) that was incorporated on 14 December 1976. MSE contains 3 boards that are Main Board, Second Board and The Malaysian Exchange of Securities Dealing and Quotation Berhad (MESDAQ). The Main Board is

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provided for bigger capitalized companies whilst smaller companies will seek to be listed on the Second Board. MESDAQ was provided for high growth and technology companies in order to raise capital. In August 2009, the Main and Second Boards merged and were renamed the Main Market, and the MESDAQ board was renamed the ACE Market which is the acronym for "Access, Certainty, Efficiency." The main aim of the ACE Market is to provide greater certainty and efficiency in the listing process and to make it easier for issuers to tap the capital market. The ACE Market is a sponsor-driven market and is open to companies of all sizes and from all sectors. The sponsors, who are mostly investment bankers, essentially evaluate the suitability of applicants seeking listing, conduct due diligence process for the ACE Market companies' documents as well as maintain regular contact with the companies for at least three years after listing. In conjunction with the new market structure, Bursa Malaysia also revamped its listing requirements for the Main Market and the ACE Market. One key reform to the ACE Market, apart from its being sponsor-driven and open to all companies of all sizes from all sectors, is that there is no prescribed minimum operating history or profit track record requirement for entry into this market. This factor empowers the sponsors to assess the suitability of listing applicants.

2.2 IPO Underpricing in Malaysia

There is extensive evidence of IPO underpricing in many developed and emerging markets. Underpricing occurs when the firm's agreed-upon offer price is less than the market price at the close of the trading on the first day. Empirical studies show that IPOs was underpriced during the initial trading in Malaysia. The significant study that attempts to measure IPO underpricing performance in Malaysia based on initial return is Dawson, (1987). IPOs data collected from 1978-1984 show that IPOs in Malaysia was underpriced (offering price compared with closing price on the first day trading) at 166.7% compare with Hong Kong 13.8% and Singapore 39.4%. While, Yong and Isa, (2003) found the average initial return (offer price to open price) is 94.91% over the entire January 1990 – December 1998 period. Murugesu and Santhapparaj (2009) found that IPO was underpriced (closing price and offering price was deflated by Net Asset Value) at 81% from 1999-2004. The offer price is determined by the underwriters in concert with the company, while the market price is determined by investors.

The aggregate amount of underpricing is colloquially referred to as "money left on the table" which is a transfer of wealth from IPO firm owners to investors including underwriters and their clients. In almost every country, IPOs are underpriced. A study by Islam, Ali, and Ahmad (2010) reports a very high average degree of IPO underpricing in Bangladesh (480.72 percent) for the period 1995 to 2005.

The study from Prasad, et. al. (2006) regarding the short-run and long-run performance in Malaysian IPOs was founded that Malaysian IPOs are highly underpricing compared to IPOs in developing countries. The data consist of the IPOs of various firms that went public for first time during the period 1968-1992. This study was investigating the impact of IPOs policy that was implementing since 1976 in Malaysia. The policy is at least 30% of an new shares on an IPO offer be sold to the indigenous Bumiputra population or to mutual funds owned by them. The result show that, the average of IPOs underpricing is 61% during the period after the regulatory economic policy was instituted. This study was used data from 2012 until 2015.

2.3 Reason for Underpricing

Underpricing is estimated as the percentage difference between the price at which the IPO shares were sold to investors (the offer price) and the price at which the shares subsequently trade in the market. In well-developed capital markets and in the absence of restrictions on how much prices are allowed to fluctuated by from day to day, the full extent of underpricing is evident fairly quickly, certainly by the end of the first day of trading, and so most studies use the first-day closing price when computing initial underpricing returns. Using later prices, say at the end of the first week of trading, typically makes little difference. In less developed capital markets, or in the presence of 'daily volatility limits' restricting price fluctuations, aftermarket prices may take some time before they equilibrate supply and demand.

Much of the theoretical research on IPOs has focused on explaining IPO underpricing. Possible reasons for underpricing include self-interested investment bankers (Baron and Holmstrom, 1980; Baron, 1982), the "winner's curse" (Rock, 1986), lawsuit avoidance (Tinic, 1998), signaling (Allen and Faulhaber, 1989), market incompleteness (Mauer and Senbet, 1992), bookbuilding (Benveniste and Spindt, 1989), and informational cascades (Welch, 1992). Evidence also suggests that in some countries IPO underpricing may be due to the regulatory environment or because the allocation of IPO shares can be used as a bribe. One possible explanation for the strong fluctuations in IPO volume is that the cost of issuing for a survey of the research on initial public offerings.

Attempts were made to examine the reasons for the initial high returns of these new issues. Some theoretical work suggests that the underpricing of IPOs is associated with asymmetric information and investors' concerns that the decision to issue equity is an attempt to expropriate wealth from outsiders. Empirical studies have found evidence that the underpricing for IPOs of financial institutions is related to proxies for asymmetric information.

Offer size, age of the firm (Barry & Brown, 1994; Megginson & Weiss, 1991; McDonald & Fisher, 1972), and the volatility of the post-offer return have all been associated with IPO underpricing. Recently Taufil Mohd (2004) conducted empirical tests on the relationship between regulations and underpricing using 546 initial public offerings on the Kuala Lumpur Stock Exchange from 1990 to 2002 and finds that the length of time from price setting to listing date is negatively related to underpricing. However the fraction of shares set aside for indigenous investors and the concerns of ethnic associations that leads to lower offering prices do not seem to affect underpricing. Finally, it was found that the protective mechanisms lead to more underpricing for firms that went public between 1996 and November 6, 1997 or those that went public after the Asian financial crisis.

2.4 Underwriter Reputation

Premarket activities undertaken by the underwriter can signal to the public the significant demand for the IPO shares. Most empirical studies find a significant relationship between underwriter reputation and the average degree of IPO underpricing. It shows that an underwriter plays a significant role in determining IPO underpricing performance. An empirical study conducted by Carter et al. (1998) suggested that the underperformance of IPO stocks relative to the market over a three-year holding period is less severe for IPOs handled by more reputable underwriters. Yip et al. (2009) found that investors can earn above-market returns by investing in IPOs that are underwritten by leading investment banks and backed by venture capitalists and divest before the expiration of the lockup period.

Kirkulak and Davis (2005) investigate underwriter reputation and IPO underpricing for the Japanese IPO market. They find that the relationship between underwriter reputation and IPO underpricing depends on when the IPO is priced, reflecting the level of demand for the issue. A study from Neupane and Thapa (2013) regarding underwriter reputation and the underwriter-investor relationship in IPO markets in India found that high reputation and low reputation underwriters have strong relationships with different sets of investors. While large institutional investors participate early in IPOs managed by high reputation underwriters, high net worth investors appear to do the same in IPOs managed by low reputation underwriters.

The varying nature of relationships with investors also has important consequences for IPO pricing. The analysis of setting the offer price shows that reputation matters greatly for high reputation underwriters. Low reputation underwriters, on the other hand, appear to price aggressively and set high offer prices even when institutional participation is negligible.

Jelic et al. (2001) extend the sample period of Paudyal et al. (1998) study to include IPOs in the Main Board since 1980 and examine the role of underwriter reputation and earnings forecast in IPO prospectus on underpricing. They document that both underwriter reputation and the accuracy of earnings forecast do not influence IPO underpricing. Results from a study by Jelic et al. (2001) do not provide evidence that offers underwritten by more prestigious underwriters are better long-term investments as compared to those underwritten by less prestigious underwriters in the Malaysian market. However, market sentiment prior to IPO and oversubscription rate positively affect the level of underpricing.

3. METHODOLOGY

3.1 Sample

The data used in this study is comprised of 46 IPOs companies listed in main market from 2012 to 2015. The data from this study are compiled from the Bursa Malaysia, Prospectus, and listed company websites.

Table 1: Number of IPOs from 2012 to 2015 and Number of IPOs selected in this study

IPO Year	No. of IPOs selected in study		No. of IPOs not selected		Total	%
	n	*%*	*n*	*%*	*n*	
2012	13	28.26	4	25.00	17	27.42
2013	15	32.61	2	12.50	17	27.42
2014	12	26.09	3	18.75	15	24.19
2015	6	13.04	7	43.75	13	20.97
Total	**46**	**100**	**16**	**100**	**62**	**100**

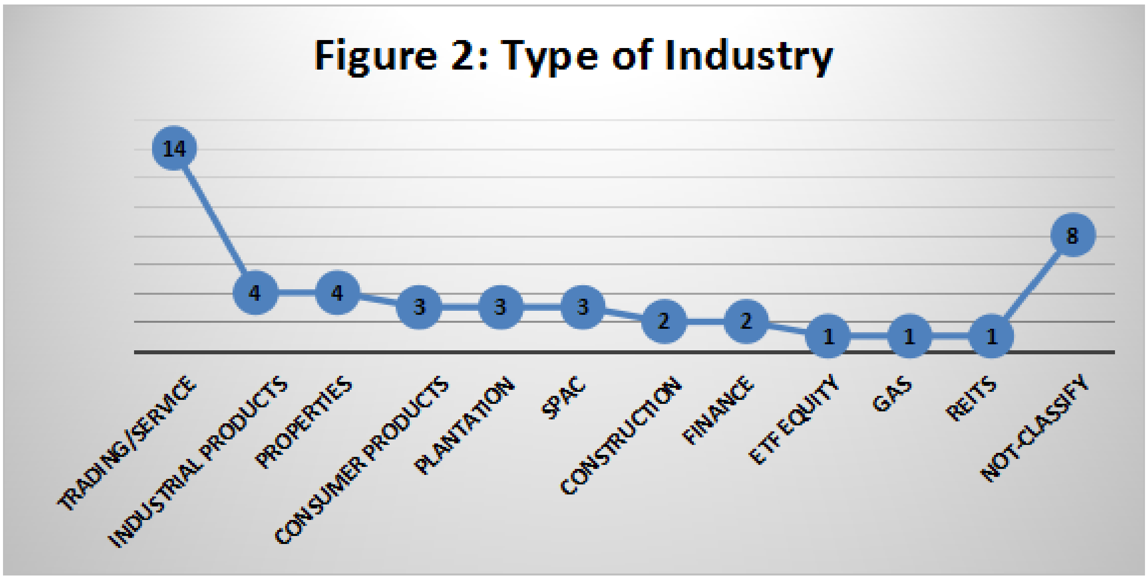
Note: This table reports the number of 46 IPOs (selected in this study), while 16 IPOs not selected.
Source: Bursa Malaysia (2012 - 2015).

Table 1 above shows number of IPOs from 2012 to 2015 listed in Bursa Malaysia. There are only 46 (74.19%) of IPOs companies listed in main market from 2012 to 2015 was selected in this study.

Table 2: Type of Industry Include in this study

Type of industry	*n*	*%*
Trading/service	14	30.43
Industrial products	4	8.70
Properties	4	8.70
Consumer products	3	6.52
Plantation	3	6.52
SPAC	3	6.52
Construction	2	4.35
Finance	2	4.35
ETF equity	1	2.17
Gas	1	2.17
REITS	1	2.17

Not-classify	8	17.39
Total	**46**	**100**



This study includes IPOs issues in all types of industry such as trading/service, industry product, property, consumer product, plantation, Special-Purpose Acquisition Company (SPAC), construction, finance, ETF equity, gas and Real Estate Investment Trusts (REITs). (see Table 2/Figure 2).

4. DATA ANALYSIS AND FINDINGS

When the offer price is lower than the price of the first trade, the stock is considered to be underpriced; that is, the stock experiences a high initial return. The offer price and the closing price of the first day of public trading for each IPO stock are obtained from the firm's prospectus and from the DataStream database. Following the lead of previous empirical work (Certo et al., 2001; Yong et al., 2001; Jelic et al., 2001), underpricing. To analyze degree of IPOs underpricing in first day trading at MSE, this study was calculated initial return (underpricing) using this formula:

$$R = \frac{(P_i - P_o)}{P_o}$$

Where:
Pi = the closing price on the first day of trading for a newly listed stock; and
Po = the offer or issue price of the firm's stock

Issue prices of listing day for 46 selected IPOs have been collected from Bursa Malaysia and IPOs offering share price (unadjusted price) have been collected from data-stream. Collected data on listing date show the IPO’s initial return.

Table 3: First day Return of IPOs

Return	**Year**			
	2012	**2013**	**2014**	**2015**
Mean initial return	4.11%	20.38%	15.26%	12.81%

Standard deviation	9.31	42.93	28.46	17.40
Highest return	16.48%	160.0%	78.98%	43.86%
Lowest return	-12.50%	-24.00%	-25.38%	0.01%

According to Table 3, all the years yield have positive initial return for IPOs on the first day of trading. The highest initial return is achieved in year 2013 with 20.38% on the first listing day. In fact, most of the stocks which have been issued in IPOs during these four years were underpriced.
It means that the closing prices of stocks on the first day of listing were higher than their offering prices. The highest return of firms' stock is observed in year 2013 with 160.00% return while the lowest with -25.38% is found in year 2014.

Table 4 show the IPOs was underpriced for issues price below than RM1.00 that is 67.62%. There were high underpriced for issues price over than RM1.00 that is 197.93%.

Table 4: Issues price below than RM1.00 and over than RM1.00

	n	**Mean**	**Std. Deviation**
Underpricing	Below RM1.00 ***n = 17***	67.62%	.2013
	Over RM1.00 ***n = 29***	197.93%	.9311
Total/Overall	***n = 46***	**149.77%**	**.9789**

4.1 Size of Firms and Total Unit Offered

The size of firms in IPO stage shows that average size of IPO – firms between 2012 and 2015 is 290,346,654 units offered where the greatest firm-value between firms is 1,800,000,000 units offered (went public in 2012) and the lowest firm-value is 12,880,000 units offered (went public in 2012).

Table 5: Unit Offered

	Year			
	2012	**2013**	**2014**	**2015**
High Offer Size	1,800,000,000	1,100,000,000	1,065,174,516	1,000,000,000
Low Offer Size	12,880,000	20,250,000	14,694,000	37,782,000

4.2 Initial Return by Sector

In this study find that IPO companies categorized under Properties, Consumer products and Plantation sectors have an average of underpriced at 24.64%, 24.48% and 24.52% respectively. Overall mean is 13.46%. While, in the SPAC sector show that the IPOs was overpriced with initial return of -13.67%. Table 5 shows mean of initial return sector of listed companies by type of industry from 2012 to 2015.

Table 5: Initial Return by Sector

Type of industry	**No.**	**MEAN**
Trading/service	14	18.43%
Industrial products	4	2.01%
Properties	4	24.64%
Consumer products	3	24.48%
Plantation	3	24.52%
SPAC	3	-13.67%
Construction	2	16.97%

Finance	2	18.93%
ETF equity	1	-
Gas	1	10.0%
REITS	1	11.20%
Not-classify	8	6.93%
Total	**46**	**13.46%**

5. CONCLUSION

This study was to investigate the degrees of initial public offering (IPOs) underpricing in Malaysia (listed in Main Market of Bursa Malaysia). The overall performance of the market showed a positive return which is high return in 2013. Consistent with past Malaysian studies, the results of marked-adjusted initial returns show that IPO companies are significantly underpriced. According to this study, all the years yield have positive initial return for IPOs on the first day of trading. Therefore, investor's loyalty into IPO companies is important in determined good performance of IPO. IPOs in Malaysia are associated with high underpricing (i.e: Dawson, 1987). However, this study found that high underpricing in the initial trading is not determined poor performance in 4 years after IPO shares are issued. Although, this study was contributes to understand the IPOs underpricing in Malaysia main market with limited to investigate the companies' performance effect into degrees of IPOs underpricing. The companies' performances were investigating in this study is issues price, offer size, and types of industry. Moreover, further research should seek enlarge determine factor were influence the degrees of IPOs underpricing. Besides that, the research should make comparison methods use by company for issues IPOs.

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+ Numbers followed by same letters in each column are not significantly ($P<0.05$) different according to the DMR test