

Initial Return of Initial Public Offerings (IPOs) and IPOs Underpricing: Evidence from Sri Lanka

Dias, D. S. M.¹, Wijesinghe, M. R. P.² and Madhushani, P. W. G.³

Initial public offering is an essential milestone for a company. It has been identified that past studies have not captured the time lag between the end date of the subscribing period, the first trading day and account for the opportunity cost of the investors as well as other market changes. Furthermore, there are limited studies available in the Sri Lankan context. This study aims to identify the factors affecting IPOs initial return and examine the level of underpricing prevailing in the Colombo stock Exchange (CSE). We considered 68 IPOs in CSE from 2006 to 2018 and employed regression analysis. ASPI Return, Sector Price/Earnings ratio, Age, Earnings Per Share, Debt Ratio, Net Asset Value, Return on Asset, Price/Earnings Ratio, Debt/Equity Ratio, Offer Price and Over Subscription Rate were the variables of the study. The results revealed that ASPI return, and oversubscription rate positively influence the market adjusted initial return (MAIR) and offer price is negatively affected. According to the level of underpricing analysis, the prevailing level of underpricing is equal to 14% and 18% for Raw Initial Return (RIR) and MAIR, respectively. Moreover, the Beverage, Food and Tobacco sector, Banking, Finance and Insurance sector and diversified holding sectors are identified as highly underpriced sectors of CSE. The study becomes novel by investigating the time lag between the end date of subscribing period and first trading day and accounting for the investors' opportunity cost and other market changes. The findings are helpful for potential investors, regulators and those who are interested in IPO investment decisions.

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¹ Department of Finance, Faculty of Commerce and Management Studies, University of Kelaniya, Sri Lanka [suleka104@gmail.com]

² Department of Finance, Faculty of Commerce and Management Studies, University of Kelaniya, Sri Lanka [ruwanmrp@kln.ac.lk]

³ Department of Finance, Faculty of Commerce and Management Studies, University of Kelaniya, Sri Lanka [gangam@kln.ac.lk]