

## Retail Investor's Investment Decision Criterion to Invest in IPOs - A Study



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**ABSTRACT:** Initial Public Offering is a kind of public offering by the companies to generate the funds from primary market for the first time. Individual investors are becoming rational to investment in Initial Public Offerings (IPOs) to gain from the listing and hold for short or long term profits. They use different strategies to gain from the IPOs. The present study examines the retail investor's criterion to invest in IPOs. For this purpose, a questionnaire was developed and administered to 724 sample respondents in Hyderabad and Secunderabad city. The responses are processed in SPSS - 26 version and applied few statistical tools i.e., descriptive statistics, ANOVA and Factor Analysis for interpretation of the results. The present study reveals that retail investor's investment decision is based on the quota of equity shares available to retail investors in IPO, Equity Participation by Financial Institutions & Foreign Institutional Investors and followed by Price band. Further, the researcher finds that there is a significant variation in means among retail investors on Industry and Sector that Company Issues the IPO and Terms of Issue related to IPOs. The study concludes that, most of the investor's investment decisions are based on market attractiveness and corporate image. Further the study may be useful to conduct the research in the following directions, to measure the investor's perception and behavior towards in participation of IPOs, Factors affecting investment decision of retail investors in different geographical areas in India.

**KEYWORDS:** Annual Savings, Investment Decisions, IPOs and Retail Investors.

### INTRODUCTION

Investments are the life blood of any economy. They are an important chain in the prosperity cycle (saving, investment, production, income, consumption/saving). There are a handsome number of investment options for investors in India. Some of them are driven by tax saving and low risk and the others are driven by returns. In this scenario, Capital markets investments are generally considered in the high-risk high return category. Generally, the capital markets are reflection of the economic health and growth of a country. Today, the Indian capital markets truly reflect as one of the fastest-growing economies in the world. The basic purpose of the capital markets is to match the forces of demand and supply of funds and in the process, play a vital role in channelizing saving and investments in the financial system. In simple words, capital markets facilitate the buying and selling of debt as well as equity instruments, both in the primary and secondary markets (**Hiranandani. N., 2020**). The primary market is a market for the trading of new securities is called as Fresh Public Offer (FPO) or Initial Public Offer (IPO). Its principal function is the raising of financial capital to augment new investment opportunities in developing their infrastructures and acquisition of fixed assets. Long terms funds are provided in the form of shares, debentures, securities and mortgage loan. One of the uniqueness of the primary market is that it provides an opportunity to the investor to understand about the fundraising corporate and select the best investment option (**Andrew M. Chisholm., 2002**).

**Definition of IPO:** The securities which the companies issue for the first time to the public either after incorporation or on conversion from private to public company is called "INITIAL PUBLIC OFFERING" or "IPO". Company raising money through IPO is also called as "Company Going Public."

### REASONS FOR GOING PUBLIC

- To raise funds for financing capital expenditure needs like expansion diversification etc.
- To finance increased working capital requirement

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- As an exit route for existing investors
- For debt financing
- **Investment Decision towards Initial Public Offer:**

Recent IPOs in the Indian capital markets have seen a lot of oversubscription. Although investing in initial public offerings is a risky activity, a rush has recently been noticed during the issues. Before making an investment selection, individual investors usually consider their needs, goals, and limits. However, they are unable to make an effective selection regarding investments. Investment Decisions are made on the risk and return (Srinivas, L., & Rao, P. V. (2017). Rational Investors always look for profitable investment avenues and invest according to their financial behavior. Thus, Retail investor's behavior is based on the psychological factors and market factors which influence to invest in various investment options. For investment in Initial Public Offering, most of the researchers identified the various factors such as corporate image, size and current price and market conditions, Investment by Financial Institutions and Foreign Institutional Investors, Retail Investors Quota provided by the company. In this scenario, Singh, M.(2012) carried a study intended to determine the perception of investors towards IPO and illustrate investing in IPO by the investors consider some important factors; images of corporate, corporate size, the company previous IPO performance, current price and current market condition. Further, Kunwar,A.,(2016), evaluated the awareness, perception, and investment decision of individual investors by providing a questionnaire to 116 respondents and found that there was a positive perception of investors towards IPO in Nepal.

### REVIEW OF LITERATURE

Initial Public Offers are widely discussed and researched topic by many of the researchers and experts, Most of them related to the performance of Initial Public Offers with various factors either to measure long term or short term profit.

Pande A, Vaidyanathan R. – "A study of Initial Public Offerings on the National Stock Exchange of India". The researchers' main objective was to study the pricing of IPOs in the NSE. The study focused to empirically explain the first day under pricing in terms of the demand generated during the book building of the issue, the listing delay between the closure of the book building and the first day listing of the issue and the money spent on the marketing of the IPO by the firms. The researchers also attempted to study any emerging patterns in Indian IPO market with reference to the previous studies and seek to find the post IPO returns for one month in the NSE. The researchers concluded that the demand generated for an issue during book building and the listing delay positively impact the first day under pricing whereas the effect of money spent on the marketing of the IPO is insignificant. The researchers also concluded that the post IPO performance in one month after the listing for the firms under study is negative.

Mittal, S., Gupta, N., & Sharma, S. K. (2012), has evaluated the Investor Preference and Promoter's Ownership Pattern in Graded IPOs of India. Their main objective of the study is to find the grading of IPOs is used as a basis of investment decisions by the retail investors. The results shows that proportion of issued share capital of an IPO is negatively (inversely) correlated with IPO grading.

Saravanan, S., & Satish, R. (2018) has studied the exploration into the Determinants of Retail Investors Investment Behaviour about Initial Public Offers in Indian Scenario. Their paper main objective of the study is to identify constructs involved in Retail Investors Investment Behaviour towards Initial Public Offers and suggest a model to understand the relationship between various construct considered. Data was collected through structured questionnaire from selected sample size and finally 504 responses were used to justify the structure. The study finds that Information Asymmetry had an indirect relationship with Intention by modifying the perception of investors either through the Representativeness and Familiarity or through the Market and Company Perception.

Jignesh B. Shahet et al.(2013)in their research, concluded that, the recent IPO Scam indicates that even a highly automated system will not prevent malpractices. But steps should be taken by SEBI to restrict such IPO Scam by applying know your customer (KYC) and unique identification number to market players and investors.

### RESEARCH GAPS

Thorough study of literature provides the research gap and frames the methodology of the study. The following are the research gap under the study.

- Most of the studies available are done with the market data available from the technical point of view related to their performance. Performance is assessed either in short or long run based on the return the IPOs provided in the period considered. Our research is aimed at behavioural view not technical.

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- From the Behavioural point of view reviews available were huge enough to know about the factors but not the specific items that constitute the factors since most of the reviews were either related to secondary market investment or in the non-financial areas.

**Research Objectives:** The following are the research objectives framed under the study.

1. To measure the investment criterion to invest in IPOs
2. To analyse the factors influencing retail investor's investment decision towards IPO

**Scope of the study:** The present study is limited to Hyderabad and Secunderabad city only. The scope of the study is confine to assess the investment criterion and factors influence the investment decision of retail investors in Hyderabad and Secunderabad city only.

**Methodology of the study:** The present study is based on the mixed research method by using qualitative data from respondents and quantitative data (published journals and articles) for identifying research gaps and research frame work.

**Research Design:** A research design is the arrangement of conditions for collection and analysis of data in a manner that aims to combine relevance to their search purpose with economy in procedure. Research design is broadly classified into three types:

- Exploratory Research Design
- Descriptive Research Design
- Causal Research Design

The present study is Descriptive in nature. Some characteristics of descriptive research are:

- Quantitativeness: Descriptive research uses a quantitative research method by collecting quantifiable information to be used for statistical analysis of the population sample.
- Qualitativeness: It can also be carried out using the qualitative research method, to properly describe the research problem. This is because descriptive research is more explanatory than exploratory or experimental.
- Uncontrolled variables: In descriptive research, researchers cannot control the variables like they do in experimental research.

**Research Instrument:** A structured questionnaire is developed and administered to the sample of respondents.

### DATA COLLECTION METHODS

- *Primary Data:* The Primary data collected from the individual investors on the basis of well designed questionnaire framed and administered to collect responses.
- *Secondary Data:* The secondary data collection pertaining to the concept of FMCG, sales promotion techniques, consumer behaviour and review of literature are collected from quality Journals, Books, Websites and Blogs, News Papers, Published and Unpublished Theses from various university libraries. The quality journals are accessed through popular databases such as Emerald, JSTOR, Taylor and Francis, Indian Journal Marketing, EBSCO, Pro Quest, and Google Scholar.

**Sampling Technique:** A convenient sampling method adopted due to large population in the defined geographical area i.e., Hyderabad & Secunderabad (twin) cities of Telangana state.

**Sample Size:** The study is based on Primary data collected from the respondents by administering a structured questionnaire through Online (Google Form) as well as off – line (Physical). For this purpose, a suitable sample size of Investors is carefully designed. In this process, alpha level a priori at .05, has been set which plans to use a proportional variable, setting the level of acceptable error at 5%, and has estimated the standard deviation of scale as .5. William Cochran's (1977) sample size formula for categorical data used to find out the appropriate sample size for the study.

$$n_0 = \frac{(t)^2 * (p)(q)}{(d)^2}$$
$$n_0 = \frac{(1.96)^2 (.5)(.5)}{(.05)^2}$$

Where t = value for selected alpha level of .25 in each tail = 1.96. (The alpha level of .05 indicates the level of risk the researcher is willing to take that true margin of error may exceed the acceptable margin of error).

Where (p) (q) = estimate of variance = .25 (Maximum possible proportion (.5)\*1-maximum possible proportion (.5) produces maximum possible sample size).

Where d+ acceptable margin of error for proportion being estimated = .05 (error researcher is willing to except).

$$= (1.96)^2 0.5 0.5 / (0.05)^2 = 384$$

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The minimum required sample size is determined as 384 but, 1000 Investors are selected for the study which is more than the minimum sample required. From that, 800 questionnaires are returned and 724 are found valid and considered as final sample. The response rate is 72.4% under the study.

**Geographical Area:** The city of Hyderabad, Telangana State covers an area of 625 square kilometers (241 sq mi), has a population of 68, 09,970 making it the fourth most populous city in India. The male population consists of 35, 00,802, female population consists of 33, 09,168 and the total population consists of 68, 09,970 (**According to CENSUS - 2011**).

**Table No – 1.1: Spread of Sampling Distribution**

Brokerage Firm	Hyderabad		Secunderabad	
	Questionnaire Distributed / Mailed	Response Recieved	Questionnaire Distributed / Mailed	Response Recieved
ICICI DIRECT	50	41	50	29
HDFC SECURITIES	50	43	50	21
SBI CAPITAL	50	44	50	26
KOTAK SECURITIES	50	47	50	27
ANGEL ONE BROKING	50	46	50	24
SHAREKHAN	50	46	50	32
MOTILAL OSWAL	50	48	50	31
5PAISA	50	47	50	32
IIFL	50	47	50	21
UPSTOX	50	48	50	24
<b>Total</b>	500	457	500	267
<b>Grand Total</b>	<b>1000</b>	<b>724</b>	<b>Response Rate</b>	<b>72.4%</b>

Source: Researcher Compilation

## DATA ANALYSIS AND INTERPRETATION

In recent times over 115 IPOs are infested in Indian Capital Market (2019 - 2021) by various companies and retail investor's participation is also very high in these IPOs. Because, investors always look for profitable investment avenues to get maximum return or gain. In this scenario, it is important to measure and analyze the criterion for investment. Under the present study, the below criterion is considered for investment in Initial Public Offering by sample respondents belongs to Hyderabad and Secunderabad city.

**Table No – 1.2: Demographic Profile of the respondents**

Demographic Variable	Category	Frequency	Percent
Gender	Male	406	56.1
	Female	318	43.9
	<b>Total</b>	<b>724</b>	<b>100.0</b>
Age	<30	420	58.0
	31-40	275	38.0
	41-50	27	3.7
	Above 50	2	0.3
	<b>Total</b>	<b>724</b>	<b>100.0</b>
Marital Status	Single	328	45.3
	Married	388	53.6
	Widowed	5	0.7
	Divorced	3	0.4
	<b>Total</b>	<b>724</b>	<b>100.0</b>

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EQs	Below Graduation	30	4.1
	Graduation	293	40.5
	PG & Above	370	51.1
	Professional Degree - CA/CMA/DOCTOR	31	4.3
	<b>Total</b>	<b>724</b>	<b>100.0</b>
Occupation	Business	206	28.5
	Self Employee	151	20.9
	Private Employee	250	34.5
	Professional	70	9.7
	Student	29	4.0
	House Wife	6	0.8
	Govt Employees	12	1.7
	<b>Total</b>	<b>724</b>	<b>100.0</b>
Annual Income	Below Rs.150,000	254	35.1
	Rs.1,50,001 - Rs.3 Lakh	155	21.4
	Rs.3,00,001 - Rs.5 Lakhs	212	29.3
	Rs5,00,001 - Rs.700,000	86	11.9
	Above Rs. 7 Lakhs	17	2.3
	<b>Total</b>	<b>724</b>	<b>100.0</b>
Annual Savings	Less than Rs.50,000	321	44.3
	Rs.50,001 - Rs.1 Lakh	129	17.8
	Rs.1,00,001-Rs.3 Lakhs	192	26.5
	Above Rs.3,00,000	82	11.3
	<b>Total</b>	<b>724</b>	<b>100.0</b>

Source: Primary Data

Demographic variables identified under the study are Gender, Marital Status, Family Structure, Annual Income and Annual Savings. Considering the Gender, Majority of the respondents i.e., 56.1% is Male and remaining is Female. Age wise distribution, most of the respondents 58% are less than 30 age. Marital Status wise, most of the respondents i.e., 53.6% are married. According to Educational Qualification, most of the respondents i.e., 51.1% are Post Graduate. Occupation wise – 34.5% of the respondents are Private Employees. Annual Income wise respondents distribution, most of them 35.1% comes under below Rs.1, 50, 000 and 44.3% of the respondent's annual savings are less than Rs.50, 000.

### Hypothesis Statement:

Null Hypothesis ( $H_{01}$ ): There is no significant variance in the means on investment criterion for participating in Initial Public Offerings between male and female investors.

Alternative Hypothesis ( $H_{1a}$ ): There is a significant variance in the means on investment criterion for participating in Initial Public Offerings between male and female investors.

**Table No -1.2: Descriptive Statistics**

Criterion	N	Minimum	Maximum	Mean	Std. Dev	Rank
Retail investors Quota	724	1	8	3.83	1.917	1
Equity participation by FI / FIIs	724	1	8	3.59	1.759	2
Price bands of the issues	724	1	8	3.49	2.011	3
Board of directors - Management	724	1	8	3.44	1.649	4
Promoter's track record	724	1	8	2.98	1.603	5

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Nature and type of products & services offered by the company	724	1	8	2.88	1.675	6
Terms of issues	724	1	8	2.68	1.621	7
Industry / Sector to which the company belongs	724	1	8	2.62	1.610	8

Source: Primary Data |

Descriptive statistics is used to analyze the data collected from sample respondents. Ranking method is also adopted to assign the ranks to the statements. High mean – High rank is assigned against the statement and vice – versa.

Majority of the sample investors reveals that they invest in the Initial Public Offering based on retailer's quota with a mean of 3.83. After that, Foreign Institutional Investors or Financial Institution's participation (Mean-3.59) is considered to follow the investment decision related to Initial Public Offering. Price band is also important parameter (Mean – 3.49) to investment in Initial Public Offering under the study. Board of Directors (Mean - 3.44) and Promoter's track record (Mean - 2.98) are moderately acceptable criterion for investing in Initial Public Offering. Nature and type of product (Mean - 2.88), Terms of issues (Mean - 2.68), Industry / Sector to which the company belongs (Mean - 2.62) are low level acceptable criterion by investor's investment decision on Initial Public Offerings.

Further, the means variation is measured by applying ANOVA – One way classification among various levels of income of respondents. Table 1.3 depicts the results of Anova test.

**Table No – 1.3 ANOVA One Way Classification – Criterion for Investment in IPO and Annual Savings.**

Criterion for Investment in IPO	Annual Savings	Mean	S.D	F	p-value	Remarks
Nature and type of products & services offered by the company	Less than Rs.50,000	2.83	1.721	0.937	0.422	Not Significant, Accept the H01
	Rs.50,001 - Rs.1 Lakh	2.91	1.691			
	Rs.1,00,001-Rs.3 Lakhs	2.83	1.593			
	Above Rs.3,00,000	3.16	1.652			
	Total	2.88	1.675			
Industry / Sector to which the Company Belongs to	Less than Rs.50,000	2.82	1.767	5.796	0.001	Significant- Reject the H01
	Rs.50,001 - Rs.1 Lakh	2.26	1.332			
	Rs.1,00,001-Rs.3 Lakhs	2.42	1.419			
	Above Rs.3,00,000	2.91	1.642			
	Total	2.62	1.610			
Terms of Issue	Less than Rs.50,000	2.81	1.681	3.001	0.03	Significant- Reject the H01
	Rs.50,001 - Rs.1 Lakh	2.72	1.634			
	Rs.1,00,001-Rs.3 Lakhs	2.38	1.482			
	Above Rs.3,00,000	2.78	1.61			
	Total	2.68	1.621			
Promoter's track record	Less than Rs.50,000	3.01	1.701	0.285	0.836	Not Significant- Accept the H01
	Rs.50,001 - Rs.1 Lakh	2.93	1.453			
	Rs.1,00,001-Rs.3 Lakhs	3.04	1.563			
	Above Rs.3,00,000	2.87	1.538			
	Total	2.98	1.603			
Board of Directors and Management	Less than Rs.50,000	3.41	1.62	0.429	0.732	Not Significant- Accept the H01
	Rs.50,001 - Rs.1 Lakh	3.59	1.81			

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	Rs.1,00,001-Rs.3 Lakhs	3.42	1.587			
	Above Rs.3,00,000	3.38	1.66			
	Total	3.44	1.649			
Equity Participation by Financial Institutions and Foreign Institutional Investors.	Less than Rs.50,000	3.58	1.677			
	Rs.50,001 - Rs.1 Lakh	3.3	1.857			
	Rs.1,00,001-Rs.3 Lakhs	3.74	1.857	1.775	0.155	Not Significant- Accept the H0
	Above Rs.3,00,000	3.71	1.652			
	Total	3.59	1.759			
Retail Investors Quota	Less than Rs.50,000	3.83	1.929			
	Rs.50,001 - Rs.1 Lakh	3.6	2.063			
	Rs.1,00,001-Rs.3 Lakhs	3.9	1.902	1.038	0.375	Not Significant, Accept the H0
	Above Rs.3,00,000	4.05	1.64			
	Total	3.83	1.917			
Price bands of the issues	Less than Rs.50,000	3.64	1.983			
	Rs.50,001 - Rs.1 Lakh	3.36	1.972			
	Rs.1,00,001-Rs.3 Lakhs	3.63	2.055	0.752	0.521	Not Significant, Accept the H0
	Above Rs.3,00,000	3.71	2.082			
	Total	3.59	2.011			

Source: Primary Data |

Table – 1.3 shows the ANOVA – One way classification results. The results are interpreted on the basis of p-value. Criterion for investment in IPO has 8 statements i.e., Nature and type of products & services offered by the company, Industry / Sector to which the Company Belongs to, Terms of Issue, Board of Directors and Management, Equity Participation by Financial Institutions and Foreign Institutional Investors, Retail Investors Quota and Price bands of the issues.

From the above statement, Industry / Sector to which the Company belongs to and Terms of Issue are statistically significant as computed value of p is less than significant value ( $p < 0.05$ ). Further, the criterion for investment in IPOs is analyzed by using factor analysis.

### Hypothesis Statement:

Null Hypothesis ( $H_0$ ): There is no significant relationship between different factors and investment decision of investors.

Alternative Hypothesis ( $H_a$ ): There is a significant relationship between different factors and investment decision of investors.

### Table No – 1.4: KMO and Bartlett's Test

<b>Kaiser-Meyer-Olkin Measure of Sampling Adequacy.</b>		<b>0.783</b>
<b>Bartlett's Test of Sphericity</b>	<b>Approx. Chi-Square</b>	<b>2598.751</b>
	<b>df</b>	<b>28</b>
	<b>Sig.</b>	<b>0.000</b>

Source: Primary Data |

The Bartlett's test of sphericity was used to determine the appropriateness of factor analysis by testing the magnitude of the correlations of the entire correlation matrix (Hair et al., 1998). Results from the Bartlett's test indicated significant correlations among measurement variables considered for the study, which are exhibited in table below. Kaiser (1974) has recommended KMO value of greater than 0.7 is acceptable and if stated value is between 0.7 and 0.7 is good. Value of our test 0.783 confirmed the adequacy of sample size that is considered for the purpose. Significance value of 0.000 indicates existence of relationship between



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the variables used in the study. Varimax rotation is used in this study since it has higher generalizability and replicability power on comparison with oblique rotation.

**Table -1.5 Total Variance Explained**

Component	Initial Eigenvalues			Extraction Sums of Squared			Rotation Sums of Squared		
	Loadings			Loadings			Loadings		
	Total	% of Variance	Cumulative %	Total	% of Variance	Cumulative %	Total	% of Variance	Cumulative %
1	3.564	44.551	44.551	3.564	44.551	44.551	2.861	35.761	35.761
2	1.809	22.613	67.164	1.809	22.613	67.164	2.512	31.403	67.164
3	0.837	10.460	77.623						
4	0.468	5.846	83.470						
5	0.434	5.422	88.892						
6	0.376	4.694	93.585						
7	0.268	3.354	96.939						
8	0.245	3.061	100.000						

Extraction Method: Principal Component Analysis.

Source: Primary Data |

Table 1.5 shows the total variance explained from the eight statements. From total eight components, two iterations are extracted. The total variance explained by these two iteration 67.164%. First component explains the total variance is 35.761% and second component explains the total variance is 31.403%.

**Table No – 1.6 Rotated Component Matrix**

Statements	Component	
	1	2
Nature and type of products & services offered by the company		0.855
Industry / Sector to which the company belongs		0.880
Terms of issues		0.800
Promoter’s track record		0.533
Board of directors	0.707	
Equity participation by FI / FIIs	0.846	
Retail investors Quota	0.864	
Price bands of the issues	0.783	

Extraction Method: Principal Component Analysis.  
Rotation Method: Varimax with Kaiser Normalization.

Source: Primary Data |

There are 8 statements in Investment Criterion to investment in Initial Public Offerings. Dimension reduction technique is applied and two iterations are extracted and labeled as Factor -1: Market Attractiveness and Factor -2: Corporate Image.

**Factor-1: Market Attractiveness** consists of 4 Statements i.e., Board of directors loading of 0.707, Equity participation by Financial Institutions or Foreign Institutional Investors loading are 0.846, Retail Investors Quota is loading is 0.864 and Price bands of the issues is 0.783.

**Factor -2: Corporate Image** is included of 4 statements i.e., Nature and type of products & services offered by the company with loading factor of 0.855, Industry or Sector to which the company belongs to as 0.880, Terms of Issues are 0.800 and Promoter’s track record is 0.533.

Therefore, the null hypothesis – H02 is rejected due to computed value of p i.e.,  $p < 0.05$ .

**Discussion of Results:** The growth of the capital market attracts the retail investors to participate in both primary market and secondary market. Retail Investors may buy the equity shares in the form of Initial Public Offering (IPO) or they trade at stock exchanges. The present study reveals that retail investor’s investment decision is based on the quota of equity shares available in IPO, Equity Participation by Financial Institutions and Foreign Institutional Investors and followed by Price band. Further, there is a significant variation in means among retail investors on Industry and Sector that Company Issues the IPO and Terms of Issue to



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the public for participation in IPOs. The study concludes that, most of the investor's investment decisions are based on market attractiveness and corporate image. The study may be useful to conduct the research in the following directions to measure the investor's perception and behavior towards in IPOs, Factors affecting investment decision of retail investors in different geographical areas in India.

### LIMITATIONS OF THE STUDY

The study is focused on the assessment and measuring individual investor's perception towards capital market investment. These individual investors are the bottom of the pyramid in stock market and their share of trading, investment is too small compared to FIIs and DIIs. Under the present study, the following are major limitations:

- Majority of the sample respondents are new generation investors and in their responses some personal bias may be recorded under the study.
- The study is confined to Hyderabad and Secunderabad City only. The sample respondents are more from Hyderabad city as compared to Secunderabad city.
- The study is confined to Individual investors only as they are in bottom of the pyramid and top & middle level of pyramid are ignored under the study.
- The study is qualitative in nature and the sampling technique (convenient sampling method) used under the study may have its own limitation.

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