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**RETAIL INVESTOR'S PERCEPTION TOWARDS INITIAL PUBLIC  
OFFERS (IPO) IN INDIA  
– A STUDY ON SELECTED CITIES**

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**ABSTRACT**

*An Initial Public Offering (IPO) is one through which an unlisted company makes either a fresh issue of securities or an offer for sale of its existing securities or both for the first time to the public. The main objective of this paper to study the opinion of retail investors on Initial Public Offers (IPOs) and its impact on them, to examine the problems facing by the retail investors during investment through IPO's and to make suggestions to get out of those problems. This study is based entirely on primary data collected through a well designed structured questionnaire from selected 500 literary retail investors as sample size from five cities in India. The opinion of the investors is taken on likert type statements. The level of agreement expressed by investors for various reasons was analyzed. Further standard deviation was used to judge the homogeneity of the mean. The study reveals that retail investor's opinion is similar on majority aspects relevant to IPOs at the same time study did find that there are some problems with IPOs, major problem out of the mentioned is 'the adequacy of 35 percent reservation for retail investors'. Retail investors are not happy with 35% reservation in IPOs. They are expecting more than this. The other problems are Refund on IPO application is received without delay, IPO allotment are credited to investor's demat account before listing of the allotted shares, Payment of 100% of the bid amount at the time of applying for IPOs. The study has stated some preventive measures to overcome the problems in IPOs investments, out of mentioned preventive measures, one measure 'Introducing mandatory rating for IPOs by credit rating agencies' has got majority acceptance...*

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*To sum up majority of the investors want SEBI to fix a greater responsibility on the merchant bankers and hold them responsible for the promoters' dubious acts. Also they want SEBI to create legal provisions to pull up the promoters for their misdeeds and proceed against them under criminal laws and confiscate all their ill gotten wealth*

## **INTRODUCTION**

Companies raise capital in the primary market by way of an initial public offer, rights issue or private placement. An Initial Public Offering (IPO) is one through which an unlisted company makes either a fresh issue of securities or an offer for sale of its existing securities or both for the first time to the public. This paves way for listing and trading of the issuer's securities. IPOs deepen the market, diversify investor's portfolios, reduce volatility in stock prices, bring domestic investors money into the market and attract Foreign Institutional Investor funds. Given the need for capital by large and small firms, IPOs also promote economic activity.

This study is an attempt to find out the perception of the retail investors towards the Initial Public Offers (IPO), and its impact on them.

## **IMPORTANCE OF IPO**

A company may choose to go for a public issue of shares because of its several advantages. The following points highlight the importance of IPO:

- IPO is an important avenue when venture capital is not available.
- Permanent capital may be provided by IPO.
- IPO makes companies easy to raise more capital by issuing additional stock in a secondary offering.
- Public companies can use their common stock to attract and retain good employees.
- An IPO provides promoters of the company and any venture capitalists invested in it, an exit opportunity for selling their ownership holdings in the business.

## **OBJECTIVES OF THE STUDY**

The study is aimed at working on the following objectives:

- To know and explain the concept of Initial Public Offers (IPOs)
- To develop the demographic profile of the retail investors

- To study the opinion of retail investors on Initial Public Offers (IPOs) and its impact on them.
- To examine the problems facing by the retail investors during investment through IPO's. And
- To make suggestions to get out of those problems

## **SCOPE OF THE STUDY**

This study covers; opinion and attitude of the retail investors towards Initial Public Offers (IPOs) and problems faced by them. And finally it gives suggestions for better understanding the IPO concept and get out of those problems, ultimately better investment decisions.

## **METHODOLOGY**

### **Primary Data:**

This study is based entirely on primary data collected through a well designed structured questionnaire. The data was collected from investors spread over four selected major cities in the country viz., Mumbai, Bangalore, Chennai, Hyderabad and Warangal. Admittedly, the sample does not represent the country's entire population but only "the universe of potential investors".

### **Secondary Data:**

The secondary data was collected from the various sources available like websites mainly SEBI, RBI, BSE and NSE, magazines, journals etc. wherever necessary.

### **Sample Size:**

I have selected 500 literary retail investors as sample size to our study from five cities namely Mumbai, Bangalore, Chennai and Hyderabad and Warangal. From each city 100 literary retail investors have selected.

### **Techniques for Analysis:**

The opinion of the investors is taken on likert type statements. The level of agreement expressed by investors for various reasons was analyzed. For analysis purposes, while entering the data strongly agree option was assigned a weight of five and strongly disagree option was assigned a weight of one. In between these two extremes other levels such as agree, neither agree nor disagree and disagree were assigned weights of four, three and two respectively. Further standard deviation was used to judge the homogeneity of the mean

## REVIEW OF LITERATURE

**Wan Nordin Wan-Hussin (2002):** in their paper examined (1) the valuation impact of IPO profit guarantee as an investor protection tool, and (2) the structural changes in IPO pricing before and after deregulation in 1996.

**Sourabh Ghosh (2002):** Several papers have identified the uncertainty of the investors and signaling intentions of the issuers behind IPO underpricing. This paper tests the implications of these models for the Indian IPOs over the last decade. The empirical findings show that there exists positive relationship between IPO underpricing and ex-ante measures of risk proxies.

**B. Swaminathan & Amiyatosh K. Purnanandam (2004):** This paper studies the valuation of initial public offerings (IPO) using comparable firm multiples. Study did find that the median IPO is overvalued at the offer by about 50% relative to its industry peers. Our results suggest overvaluation is the likely source of the long-run underperformance of IPO's and provide support for behavioral theories based on investor overreaction.

**Prof. V. Gangadhar & Mr. G. Naresh Reddy (2005):** They have stated that the book-building system is a part of Initial Public Offer (IPO) of Indian companies. Book-Building involves sale of securities to the public and the institutional bidders on the basis of predetermined price range. It is an innovative method of marketing securities involving price determination and quantum of securities on the basis of demand from the prospective shareholders.

**William J. Wilhelm Jr. (2005):** They have studied the future of IPO with relevance to the Internet-based IPO auction process. Their conclusion is recent advances in communications technology and auction theory will undoubtedly reshape current securities underwriting practices. In particular, Internet auctions are likely to replace book building in debt IPOs and less risky equity issues (say, IPOs of LBOs)

**Markku Kaustia and Samuli Knupfer (2008):** In their article, find a strong positive link between past IPO returns and future subscriptions at the investor level in Finland. Their setting allowed them to trace this effect to the returns personally experienced by investors; the effect is not explained by patterns related to the IPO cycle, or wealth effects. The results provide a micro foundation for the argument that investor sentiment drives IPO demand.

**S.S.S. Kumar (2010):** This paper examines the efficiency of IPO issuing mechanisms using a sample of Indian IPOs that tapped the primary market. Results showed that the issue

expenses associated with book building is more than those associated with fixed price offers after controlling for issue size and firm specific characteristics

## DEMOGRAPHIC PROFILE OF THE RETAIL INVESTORS

### Age wise distribution of investors:

The age wise distribution of investors is given in the following table. The Table 1 reveals that below 35 years age group investors dominate the sample with 42.2 percent followed by the age group of 36-50 years with 30 percent.

### Sex wise distribution of investors:

Male investors constitute a large majority 80.4 percent as compared to 19.6 percent of the female investors. In other words, male investors were more than 4 times in numbers compared to female investors.

**Table 1: Age wise distribution of investors**

Age	No. of Investors	% of Investors
Up to 35	211	42.2
36 to 50	150	30.0
51 to 60	98	19.6
61 and above	41	8.2
<b>Total</b>	<b>500</b>	<b>100.0</b>

**Table 2: Sex wise distribution of investors:**

Sex	No. of Investors	% of Investors
male	402	80.4
female	98	19.6
<b>Total</b>	<b>500</b>	<b>100.0</b>

### Income wise distribution of investors:

The distribution of investors according to their income level is presented in Table

**Table 3: Income wise distribution of investors**

Monthly Income	No. of Investors	% of Investors
Upto20000	75	15.0
20001-30000	124	24.8
30001-40000	191	38.2
40000 above	110	22.0
<b>Total</b>	<b>500</b>	<b>100.0</b>

The modal income class is above Rs.30001 to 40000 per month. This group constitutes nearly two fifth of the sample and the Rs.20001-30000 income group accounts for another 24.8% while the rest two groups (up to Rs.20,000 and Rs.40,000 above per month) accounting the balance 37%.

#### **Education (Qualification) wise Classification of Investors:**

The distribution of investors according to the levels of education is given in Table 4. It reveals that half of the investors are post graduates, around 40% are graduates and others about 16%. Thus it can be said that 8 out of 10 investors are educated enough to understand the ongoing trends in the capital market and they can acclimatize themselves with the changing capital market environment.

#### **Occupation Wise Classification of Investors**

The distribution of investors according to their occupations is given in Table 5. A cursory view of the Table 5 reveals that little more than one fourth (26.8%) of the investors comprises of non-government service investors and a little less than one fourth (24.2%) of the investors comprises of retired investors. Nearly 12% of the investors were practicing professionals, one fifth was in Government service and 14% of the investors had their own business.

**Table 4: Education (Qualification) Wise Classification of Investors**

**Table 5: Occupation Wise Classification of Investors**

Qualification	No. of Investors	% of Investors
Graduation	190	38.0
Post Graduation and a Above	229	45.8
Others	81	16.2
Total	500	100.0

Occupation	No. of Investors	% of Investors
Government services	116	23.2
Non Government services	158	31.6
Own business	121	24.2
Professional Practices	44	8.8
Retired	27	5.4
Others	34	6.8
Total	500	100.0

### SEBI ROLE IN AN IPO ISSUE

Any company making a public issue or a listed company making a rights issue of value of more than Rs.50 lakhs is required to file a draft offer document with SEBI for its observations. The company can proceed further on the issue only after getting observations from SEBI. The validity period of SEBI's observation letter is three months only *i.e.*, the company has to open its issue within three months period. SEBI does not recommend any issue nor does take any responsibility either for the financial soundness of any scheme or the project for which the issue is proposed to be made or for the correctness of the statements made or opinions expressed in the offer document. It is to be distinctly understood that submission of offer document to SEBI should not in any way be deemed or constructed that the same has been cleared or approved by SEBI.

The lead manager certifies that the disclosures made in the offer document are generally adequate and are in conformity with SEBI guidelines for disclosures and investor protection in force for the time being. This requirement is to facilitate investors to take an informed decision for making investment in the proposed issue. The investors should make an informed decision purely by themselves based on the contents disclosed in the offer documents. SEBI does not associate itself with any issue/issuer and should in no way be construed as a guarantee for the funds that the investor proposes to invest through the issue. However, the investors are generally advised to study all the material facts pertaining to the issue including the risk factors before considering any investment. They are strongly warned against any *tips*' or news through unofficial means.

## IPOS' CAPITAL CONTRIBUTION

The India's growth story is a best seller and the equity market is hot. There are no second thoughts about it. And India Incorporated's promoters have capitalized on this fact. The following table presents the number of IPOs made and the amount of capital raised during the years from 2000-01 to up to April 2009-10.

**Table 6: Amount of Capital Raised and Number of IPOS during the years  
2000-01 to April 2009-10**

Fiscal year	Number of IPOs	Capital Raised (Rs. In Crore)
2000-01	124	6,618
2001-02	19	6,423
2002-03	14	5,732
2003-04	35	22,145
2004-05	34	25,526
2005-06	101	23,632
2006-07	8	3,820
2007-08	85	42,595
2008-09	21	2,083
2009-10	39	24,696

Source *www.entintelligence.com*

### Application Supported by Blocked Amount (ASBA):

Application Supported by Blocked Amount (ASBA) is an application containing an authorization to block the application money in the bank account, for subscribing to an issue. If an investor is applying through ASBA, his application money shall be debited from the bank account only if his/her application is selected for allotment after the basis of allotment is finalized, or the issue is withdrawn/failed.

SEBI has been specifying the investors who can apply through ASBA. In public issues w.e.f. May 1, 2010 all the investors can apply through ASBA.



Investors were asked whether they are aware of ASBA or not? For this 68 percent of the investors said 'no' and remaining nearly 32 percent investors said 'yes', as shown in the Table 7.

As a part of study the investors were asked a question that did they purchase securities through book buildings or not for this question 33.6 percent of the retail investors said 'yes' and 66.4 percent of the total investors are said 'no', as shown in the Table 8. It means that majority of the investors are away of using the book building method

**Table 7: Investors awareness on ASBA**

Response	No. of investors	% of investors
Yes	158	31.6
No	342	68.4
<b>Total</b>	<b>500</b>	<b>100.0</b>

**Table 8: Investors awareness on book Building method of application**

Response	No. of Respondents	% of investors
Yes	168	33.6
No	332	66.4
Total	500	100.0

## RESERVATION FOR RETAIL INVESTORS IN IPO

The reservation for retail investors was set at 25 percent earlier. It was found to be inadequate. The investors were not able to cash in on good investment opportunities as the portion reserved for them in IPO is low.' In this context the Primary Market Advisory Committee's (PMAC's) of SEBI recommended hiking of the allocation for retail investors to 35% and the bid amount defining a retail investor to Rs.1 lakh. These have been accepted by SEBI and at present 35 percent of the public issue portion in a book built issue is reserved for retail investors. The Securities Exchange Board of India has thus allocated up to 50 percent of issue size to Qualified Institutional bidders, minimum 15 percent of issue size to Non-Institutional Bidders and 35 percent of issue size to Retail individual bidders in a public issue.

## PROBLEMS IN IPO SUBSCRIBING

The investors were asked whether they did purchase the shares through IPO or Not? The response shown in the Table 9, for this question 51.2 percent of the investors have said 'yes' of the total respondents and remaining 48.8 percent of the investors have said 'no'

The investors were further asked to specify the problems faced by them in IPO subscribing. The response is mentioned in the Table 10. Nearly 61 percent of the investors surveyed have said they have faced problems in subscribing to IPO's. 39 percent of the investors said they have no problems.

**Table 9: Investors participation in IPOs**

Response	No. of Respondents	% of investors
Yes	256	51.2
No	244	48.8
Total	500	100.00

**Table 10: Investor response on problems**

With IPO's

Response	No. of Respondents	% of investors
Yes	156	60.93
No	80	39.07
Total	256	100.00

Table 11 presents, of those who said they face problems in IPO subscribing, a large number have specified the problems. Of them, above 60 percent were related to Reservation of 35% of IPO for Retail Investors is not adequate and Payment of 100% of the bid amount at the time of applying for IPOs is a problem. 28 percent of the investors said that IPO allotment is credited to their D-mat account before listing of the allotted shares. Surprisingly only 8.97 percent of the investors complained that Refund on IPO application is received with delay. They have even suggested that refund money should be credited to the bank account. The next major problem identified by the investors was high levels of premium charged and the payment of the entire bid amount at the time of applying for IPOs.

**Table 11: Response towards the problems faced while IPO**

Problem	No. of Respondents	% of investors
Refund on IPO application is received with delay	14	8.97
IPO allotment are credited to my D-mat a/c before listing of the allotted shares	44	28.20
Reservation of 35% of IPO for Retail Investors is not adequate	50	32.05

Payment of 100% of the bid amount at the time of applying for IPOs is a problem	48	30.78
Total	156	100.00

The investors' opinion relating to Initial Public Offer was analyzed using mean values. Table 12 presents the mean value and standard of deviation of values from the mean values. The table reveals that the investors agree with all the statements except that of 35 percent reservation for retail investors in an IPO is adequate.

**Table 12: Mean & Standard Deviation of Investors' Opinion Regarding IPOs**

Statements	N	Mean	Std. Deviation
Refund on IPO application is received without delay	500	3.66	0.943
IPO allotment are credited to my demat account before listing of the allotted shares.	500	3.72	0.890
Reservation of 35% of IPO for retail investors is adequate.	500	3.27	1.214
Payment of 100% of the bid amount at the time of applying for IPOs is a problem.	500	3.62	0.990

The investors' level of agreement on all these statements is above the level of indecisiveness moving towards the level of agreeing. This can be interpreted that the investors receive the refunds of application money without delay and the allotted shares are also credited to their demat accounts before they are listed in a stock exchange. The mean value of their opinions reflects that this may not be case all the times and they might have faced some odd situations too. Earlier the investors used to pay a small amount at the time of applying for shares towards application money. Later if allotted they paid the balance in one or more installments. Now under the book building method of IPOs, they have to pay 100 percent of the bid amount at the time of applying which is not agreeable. The only statement relating to

IPO on which investors expressed disagreement is regarding the adequacy of 35 percent reservation for retail investors. The Standard Deviation of values for the agreed statements from their mean values is small indicating the high level of uniformity in investors' views on the subject.

#### Age Wise Opinion on Initial Public Offers

The investors' opinion on IPOs was further analyzed based on their age; the mean values of investors' opinions on this basis are given in the following table number 13. The table reveals that age wise mean value of investors' IPO related opinions almost go with the opinion of the overall investors with one exception. The above sixty age group neither agrees nor disagrees with the statement '*reservation of 35 percent of IPO for retail investors is adequate*'. In that, the group differs from the overall investors' slightly disagreement with that statement.

#### Income Wise Opinion on Initial Public Offers

The mean values of investors' level of agreement with opinion statements on IPOs were further classified based on their income. This classification is given in the following table 14. Table reveals that investors classified on the basis of their income does not differ significantly among themselves in their opinions regarding IPOs. However, the investors with monthly income up to Rs.20,000 even though neither agree nor disagree with the statement that 35 percent reservation for retail investors in IPOs is adequate, they seem to slightly lean towards agreeing to the statement as per the mean value.

**Table 13: Age wise opinion on Initial Public Offers**

Age in Years	Reservation of 35% of IPO for Retail Investors is not adequate	Refund on IPO application is received with delay	PO allotment are credited to my D-mat a/c before listing of the allotted shares	Payment of 100% of the bid amount at the time of applying for IPOs is a problem
Below 35	3.13	3.57	3.67	3.53
36 to 50	3.55	3.79	3.84	3.73
51 to 60	3.32	3.62	3.62	3.60

61 and above	2.88	3.73	3.73	3.73
Total	3.27	3.66	3.72	3.62

*Mean values of investor's IPO related opinions*

**Table14: Income Wise Opinion on Initial Public Offers**

*Mean values of Investors' IPO Related Opinions*

Monthly Income in Indian Rupees	Reservation of 35% of IPO for Retail Investors is not adequate	Refund on IPO application is received with delay	PO allotment are credited to my D-mat a/c before listing of the allotted shares	Payment of 100% of the bid amount at the time of applying for IPOs is a problem
Up to 20000	3.29	3.76	3.79	3.67
20001-30000	3.37	3.61	3.74	3.65
30001-40000	3.16	3.62	3.68	3.58
Above 40000	3.35	3.72	3.72	3.64
Total	3.27	3.66	3.72	3.62

#### **CityWise Opinion on Initial Public Offers:**

Is the opinion of investors from various cities remaining the same with regarding to IPOs?

The curiosity led to the classification of the mean values of opinions based on the city of dwelling of investors.

**Table 15: City Wise Opinion on Initial Public Offers**  
*Mean values of Investors' IPO Related Opinions*

<b>City of the Respondents</b>	<b>Reservation of 35% of IPO for Retail Investors is not adequate</b>	<b>Refund on IPO application is received with delay</b>	<b>PO allotment are credited to my D-mat a/c before listing of the allotted shares</b>	<b>Payment of 100% of the bid amount at the time of applying for IPOs is a problem</b>
Bombay	3.27	3.64	3.70	3.67
Bangalore	2.75	3.57	3.67	3.56
Hyderabad	3.32	3.65	3.69	3.64
Chennai	3.64	3.74	3.76	3.65
Warangal	3.38	3.70	3.77	3.59
Total	3.27	3.66	3.72	3.62

The city wise classification of the mean value of investors' opinion reveals that over all investors are towards agreeing to the opinion that payment of 100 percent of the bid amount while applying for IPO is a problem. The investors' level of agreement on all these statements is above the level of indecisiveness moving towards the level of agreeing

It is further asked retail investors opinion about the prevention of manipulators in capital markets with reference to IPOs. Their opinion is shown in the Table 16

**Table 16: Investors' Opinion on Prevention of Manipulators from approaching capital**

Opinion Statements	Number of Investors	% to Total
Fixing a greater responsibility on merchant bankers and penalizing them if found guilty.	150	30
Creating provisions to personally pulls up the promoters for their acts and punishes them.	145	29
Introduce mandatory rating for IPOs by credit rating agencies.	205	41

Market

Out of the response, 30 percent of investors want SEBI to fix a greater responsibility on merchant bankers and penalize them in case of wrong doing. More than one fourth of investors want the authorities to create necessary provisions to personally pull up the promoters for their wrong doings and punish them. And 41 percent of investors want introduction of compulsory rating of IPO's by credit rating agencies.

## CONCLUSION

Above study reveals that retail investor's opinion is similar on majority aspects relevant to IPOs at the same time study did find that there are some problems with IPOs, major problem out of the mentioned is 'the adequacy of 35 percent reservation for retail investors'. Retail investors are not happy with 35% reservation in IPOs. They are expecting more than this. The other problems are Refund on IPO application is received without delay, IPO allotment are credited to investor's demat account before listing of the allotted shares, Payment of 100% of the bid amount at the time of applying for IPOs.

The study has stated some preventive measures to overcome the problems in IPOs investments, out of mentioned preventive measures, one measure 'Introducing mandatory rating for IPOs by credit rating agencies' has got majority acceptance.

To sum up majority of the investors want SEBI to fix a greater responsibility on the merchant bankers and hold them responsible for the promoters' dubious acts. Also they want SEBI to create legal provisions to pull up the promoters for their misdeeds and proceed against them under criminal laws and confiscate all their ill gotten wealth.

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## ANNEXURE

### Questionnaire to Retail Investors

#### Guidelines for Filling up the Questionnaire:

For a majority of questions readymade answers are provided. Please tick (✓) the appropriate response from among the answers given, as applicable to you. Proper instructions are given along with question wherever necessary; respondents are requested to follow those instructions while answering the questions

1. Name of the Investor \_\_\_\_\_
2. Address: \_\_\_\_\_
3. Age (in years):
  - a) Below 35 ( )
  - b) 36 - 50 ( )
  - c) 51 - 60 ( )
  - d) 61 and above ( )
4. Educational Qualification: \_\_\_\_\_
5. Sex: Male/Female.

6. Occupation:
- a) Government Services ( )
  - b) Non Government Services ( )
  - c) Own Business ( )
  - d) Professional Practices ( )
  - e) Retired ( )
  - f) Others ( )
7. Monthly total Income (in Rs.):
- a) Up to 20,000 ( )
  - b) 20,000 --30,000 ( )
  - c) 30,000-- 40,000 ( )
  - d) 40,000 and above ( )
8. Did you purchase shares through IPO Yes/No
9. Do you feel, are there any problems with IPO subscription Yes/No
10. If your answer is 'Yes', kindly opinion about the following statements regarding Initial Public Offers (IPOs), Please indicate your opinion in respect of the following statements by ticking '1' Strongly Agree, '2' Agree, '3' Neither Agree nor Disagree, '4' Disagree, and '5' Strongly Disagree
- a) Refund on IPO application is received without delay  
1 2 3 4 5
  - b) IPO allotment are credited to my D-mat account before listing of the allotted shares  
1 2 3 4 5
  - c) Reservation of 35% of IPO for Retail Investors is adequate  
1 2 3 4 5
  - d) Payment of 100% of the bid amount at the time of applying for IPO's is a problem  
1 2 3 4 5
11. Are you aware of Book Building method Yes/No
12. Did you purchase the securities through Book building method Yes/No
13. Do you purchase the securities using ASBA (2008) Yes / No

14. If you have purchased securities from the primary market, kindly indicate the problems you have faced.
- a) Non-availability of prescribed application form ( )
  - b) Misleading advertisement ( )
  - c) Misleading market rumors and gossip ( )
  - d) Lack of reliable investment counseling facilities ( )
  - e) Delayed/Non-receipt of Refund Order ( )
  - f) Delayed/Non –receipt of Certificates ( )
  - g) Delayed listing of the securities with stock exchanges ( )
  - h) Offering securities under promoters quota or as firm allotment on payment of unofficial premium ( )
15. How can we prevent manipulators from capital markets?
- a) Fixing a greater responsibility on merchant bankers and penalizing them if found guilty ( )
  - b) Creating provisions to personally pull up the promoters for their acts and punish them ( )
  - c) Introduce mandatory rating for IPOs by credit rating agencies ( )