

Share Subscription Ratio In Primary Markets –An Important Determinant For Identifying Good Stocks In Secondary Markets

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INTRODUCTION

Over the past few years, Securities and Exchange Board of India (SEBI), through implementation of several measures and regulations has tried to ensure that only good companies can access funds from the primary market. Though under such regulations, fly by night operators have been prevented from raising funds, but the problem of proper pricing of Initial Public Offerings still remain visible in the system.

When a company comes out with an Initial Public Offering, it ensures proper distribution of shares among various classes of investors such as Individuals, Non- Institutional Investors and Qualified Institutional Buyers or Institutional Investors. The investors, particularly retail investors, invest on the basis of recommendations given by friends and different analysts and the return on such investments are subject to high uncertainty.

This study has been done with a view to assess the returns from the Initial Public Offering market on the basis of the response shown by different class of investors mentioned above. There is a general perception in the market that sometimes the companies not having sound profitability record or management and those which have aggressively priced their issues try to ensure subscription by luring their friends, relatives and other retail investors.

The study has been conducted to broadly assess the following aspects:

- The price movement of the shares immediately after listing in the secondary market.
- The long term return and short term return offered by Initial Public Offerings and their relationship to the subscription pattern.

RESEARCH METHODOLOGY

The price pattern of some of the Initial Public Offerings which have been listed at different points of time over the last three years have been taken. The data has been collected for twelve companies which are as follows:

- **Cinemax India Limited**
- **Alpa Laboratories Limited**
- **Koutons Retail India Limited**
- **Nissan Copper Limited**
- **Burnpur Cement Limited**
- **Info Edge India Limited**
- **Aries Agro Limited**
- **Binani Cement Limited**
- **Allied Computers International (Asia) Limited**
- **Tulsi Extrusions Limited**
- **Omaxe Limited**
- **Educomp Solutions Limited**

All the companies mentioned above have been analysed in a uniform manner and then compared on the basis of certain measures to arrive at a conclusion. The subscription pattern data of each company on the basis of which their prices have been analyzed and the correlation between the subscription pattern and the returns offered by these companies have been studied.

In order to find whether the stock has underperformed or outperformed the market, charts have been prepared

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between the movement of the share vis-à-vis the market during the three months from the date of listing of the share. The price pattern has also been studied, taking the movement of the share price vis-à-vis its issue price.

Daily return of the stock as well as the market has been calculated to draw other statistical inferences. The returns have been calculated using the formula

$$\text{Return} = \{(\text{Closing}_n - \text{Closing}_{n-1}) / (\text{Closing}_{n-1})\} * 100$$

The first parameter that has been calculated was the Coefficient of Correlation between the closing price of the stock and the closing value of the market so as to assess how well do they move in tandem with one another. The next step was to calculate the Probable Error in order to check whether the value of Coefficient of Correlation is appropriate for interpretation or not. As per the statistical rule, the Coefficient of Correlation is significant for interpretation if its value is six times or more than that of the Probable Error. The Probable Error is calculated using the formula:

$$\text{Probable Error} = \{(0.6745 * (1 - (\text{Coefficient of Correlation})^2)) / \text{Square Root of } n\}$$

The next set of statistical figures which have been calculated to further substantiate various analytical aspects of the study include the Mean Price, Mean Return and Standard Deviation. The Mean Price is calculated using the Average function along with the closing prices of the stock and it has been calculated so that it can be compared with the Issue Price so as to be able to conclude whether the issue is Over Priced or Under Priced. The Mean Return is calculated on the stock by taking the Average of the Daily Returns that has been calculated earlier so as to establish the relation between the risk and return for each stock. The Standard Deviation has been calculated using the function to assess the level of risk the stock carries. All this is followed by the calculation of the Coefficient of Variation which helps to compare the level of risk among the stocks, even if all of them have different levels of return. It is calculated using the formula:

Average Return/ Standard Deviation

The last set of figures include the Standard Deviation, Standard Error and Test of Significance which have all been calculated for a period of 15 days in order to eliminate the impact of the market factors to a great extent. The Standard Deviation has been calculated using the same formula. The Standard Error is calculated for the computation of the test of significance and the formula for the same is:

Standard Deviation/ Square Root of 15 (As it is for a period of n days and n=15)

The Test of Hypothesis helps to establish whether there is a significant difference between the Issue Price and the Mean price. And to ascertain the same, the value for the formula below should be greater than or equal to the value of 2.58. The formula for the Test of Hypothesis is:

$$\{ \text{Absolute Value (Issue Price-Mean Price)} \} / \text{Standard Error}$$

And the last figure that has been calculated is the Beta which just shows how responsive the stock is to the movements in the market. A high Beta represents that the stock will respond efficiently if the market moves efficiently and vice-versa. It has been calculated using the formula:

$$[\{ n (\text{Sum of } (X * Y)) \} - \{ (\text{Sum of } X) * (\text{Sum of } Y) \}] / [\{ n (\text{Sum of } (x^2)) \} - \{ (\text{Sum of } X)^2 \}]$$

where X represents the Return on the Market and Y represents the Return on the Stock and n represents the number of values being considered.

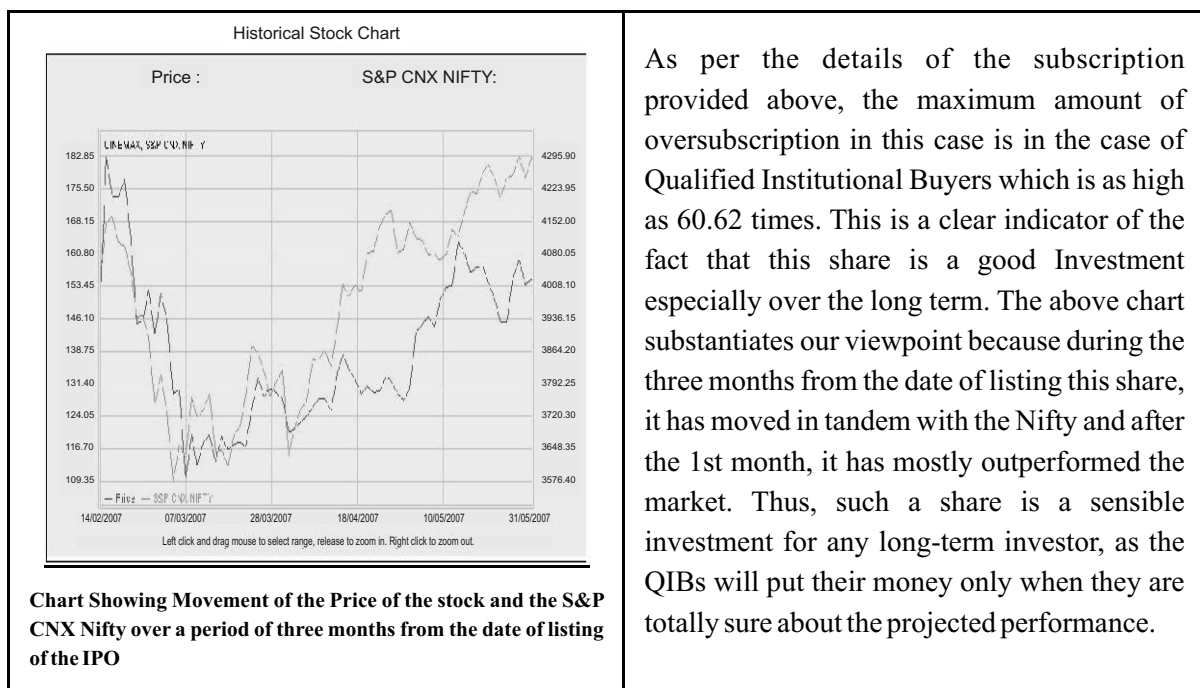
The entire methodology explained above has been used to arrive at the conclusion set to be achieved.

ANALYSIS OF THE COMPANIES

CINEMAX INDIA LIMITED (CIL)

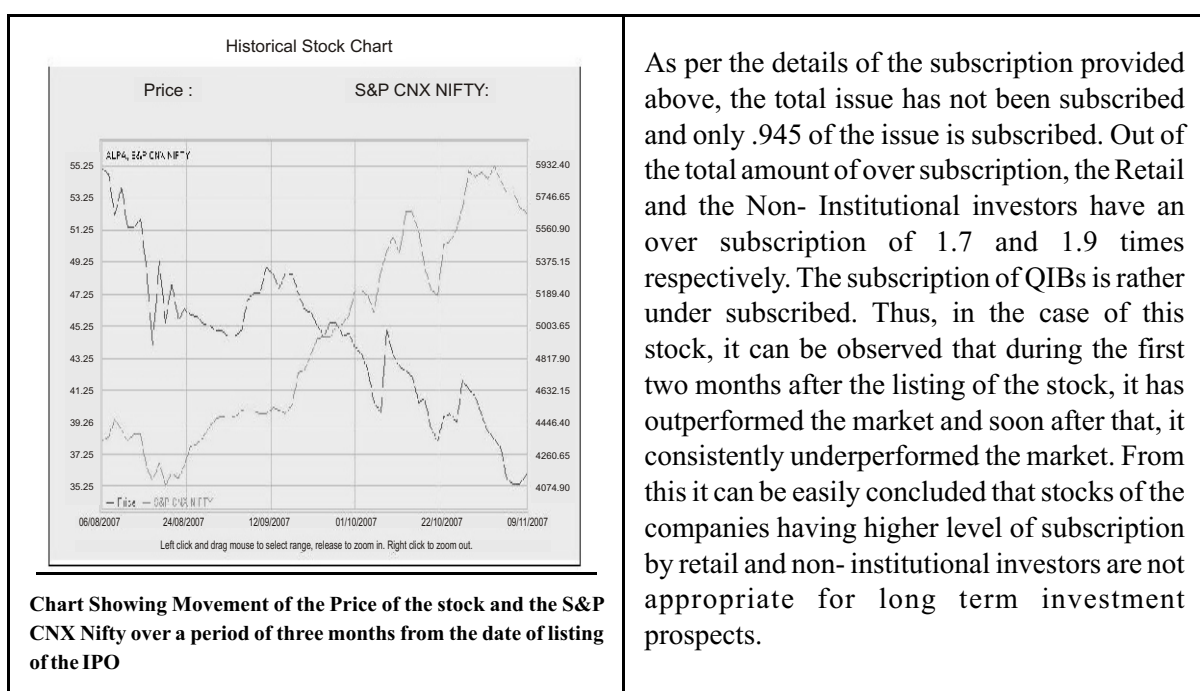
IPO SUBSCRIPTION PATTERN

Category	No. Of Applications	No. Of Shares	Subscription (No. Of times)
Retail Individual Bidders	145662	47878020	15.4395
Non-Institutional Bidders	422	56892420	42.8084
QIBs	210	268549785	60.6207
Eligible Employees	42	64080	1.068



ALPA LABORATORIES LIMITED IPO SUBSCRIPTION PATTERN

Category	No. Of Applications	No. Of Shares	Subscription
Qualified Institutional Buyers	3	827400	0.178
Non-Institutional Investors	40	2725300	1.912
Retail Investors	13379	5422400	1.674
Employee	12	5500	0.022
TOTAL	13434	8980600	0.945



KOUTONS RETAIL INDIA LIMITED IPO SUBSCRIPTION PATTERN

Category	No. Of Applications	No. Of Shares	Subscription (No. Of times)
Retail Individual Bidders	145662	47878020	15.4395
Non-Institutional Bidders	422	56892420	42.8084
QIBs	210	268549785	60.6207
Eligible Employees	42	64080	1.068

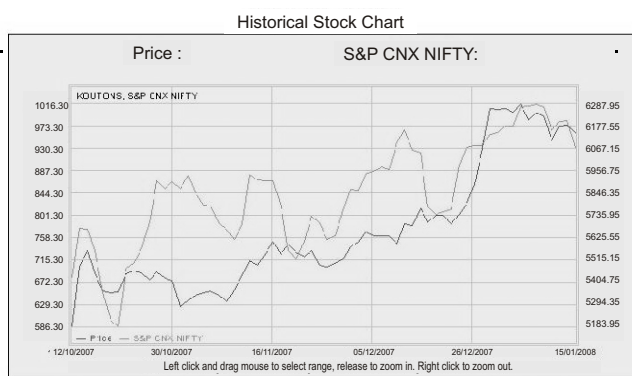


Chart Showing Movement of the Price of the stock and the S&P CNX Nifty over a period of three months from the date of listing of the IPO

The above data about subscription shows that the issue for this stock was over subscribed by as much as 60 times by the QIBs. The above chart shows that the stock moves in relation to the stock market and after the 1st two months, it has begun to outperform the market (from 26th December onwards). This stock is ideal for a long-term investor who has faith in the growing economy of India, more so because the QIBs will take a risk only to the extent of their calculations.

NISSAN COPPER LTD IPO SUBSCRIPTION PATTERN

Category	Number of Applications	Number of Shares	Subscription (Times)
Qualified Institutional Buyers	3	4366560	1.51
Non-institutional Investors	39	1,93,90,560	20.23
Retail Bidders	10,049	95,72,000	4.28
Employees	7	3,31,200	0.52
Total	10,098	3,36,60,320	5.25

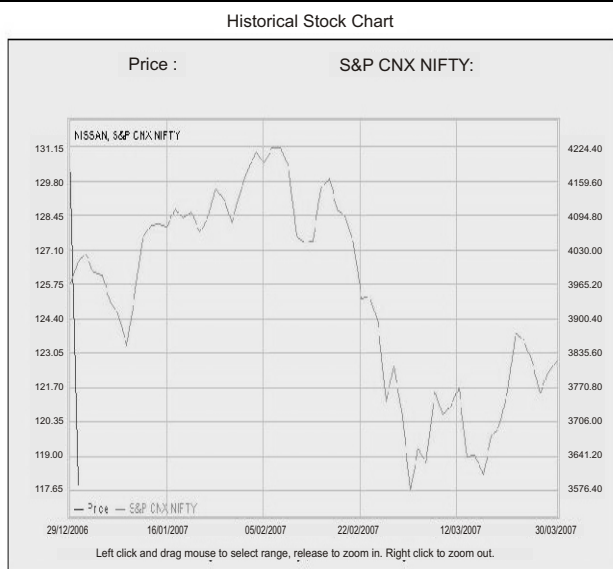


Chart Showing Movement of the Price of the stock and the S&P CNX Nifty over a period of three months from the date of listing of the IPO

In the case of Nissan Copper, the pattern of Subscription reveals that the Non -Institutional and Retail Investors have the maximum amount of over subscription and the over subscription of the QIBs at 1.51 times is approximately 13 times more in case of Non- Institutional investors. The chart above shows that the opening price was the highest after the first 15 days itself. After that, the price went so low that it never came up and there is no question of this stock under performing or over performing because the level of performance is such that it is not even worth considering. Such shares reinforce the fact that certain issues are highly manipulated and wherever QIBs are small in number, the result is most likely to be negative

BURNPUR CEMENT LIMITED IPO SUBSCRIPTION PATTERN

Category	No. Of Valid Applications	No. Of Shares Applied For	Subscription (Times)
Retail Investors	98457	257512500	15.51
Non Retail Investors	307	65292500	15.51
Employee	11	1270000	1.15

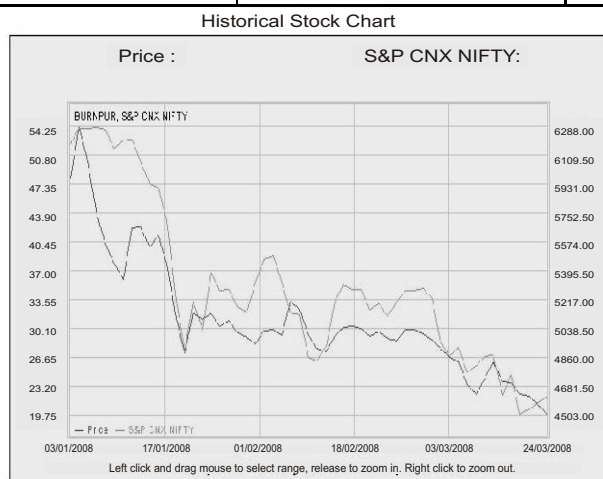


Chart Showing Movement of the Price of the stock and the S&P CNX Nifty over a period of three months from the date of listing of the IPO

The above-mentioned details about the subscription pattern reveal that there was no subscription by the QIBs for this particular stock. The entire over subscription is attributed to the Retail and Non- Retail investors. The above chart indicates that the stock price rose immediately after the listing for the large investors to exit with large profits and after 15 days or the 17th of January, the stock fell continuously and it under performed as compared to the market. This type of stock is not suitable for a long-term investor.

INFO EDGE INDIA LTD (NAUKRI.COM) IPO SUBSCRIPTION PATTERN

Category	No. Of Applications	No. Of Shares Bid	Subscription
Qualified Institutional Buyers	238	242060500.00	84.1985
Non-Institutional Bidders	342	31959440	66.7008
Retail Individual Bidders	101353	17515380	12.1851
Employees	157	134620	0.2529

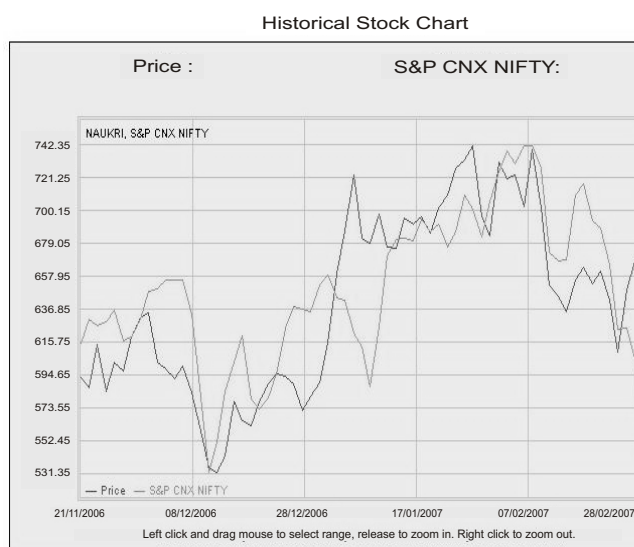


Chart Showing Movement of the Price of the stock and the S&P CNX Nifty over a period of three months from the date of listing of the IPO

The above given subscription pattern shows that the IPO of this stock was primarily subscribed by the QIBs and the over subscription in case of the Retail Investors is a mere 12 times. Besides this, the above graph shows that immediately after one month of listing ,this stock outperforms the market at most levels during the three months of the period of study. This is a good investment option in the long run and the high component of the QIBs is another factor, which makes it a highly prospective investment.

ARIES AGRO LIMITED SUBSCRIPTION PATTERN

Category	No. of Applications	No. of Shares Bid	Subscription
Qualified Institutional Buyers	22	17057500	7.58
Non-Institutional Investors	73	3865700	5.73
Retail Individual Investors	29092	9704489	6.16

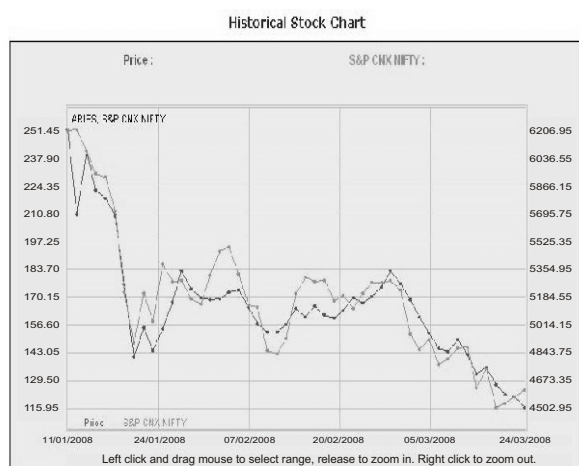


Chart Showing Movement of the Price of the stock and the S&P CNX Nifty over a period of three months from the date of listing of the IPO

The subscription pattern reveals that on an overall basis, the level of over subscription is not very high but the highest is by the Qualified Institutional Buyers. This is a positive indicator. The above chart depicts that the movement of the price of the stock is completely in tandem with the market. This is a positive indicator and a good investment option for those investors or speculators who can appropriately assess the market with a certain level of surety so as to be able to get returns from such a stock during the short or long term.

BINANI CEMENT LIMITED IPO SUBSCRIPTION PATTERN

Category	No. of Applications	No. of Equity Shares	Subscription
Qualified Institutional Bidders	15	16,302,240	1.3253
Non-Institutional Investors	67	566,880	0.2765
Retail Investors	26994	8,653,507	1.407
Eligible Employees	42	64080	1.068

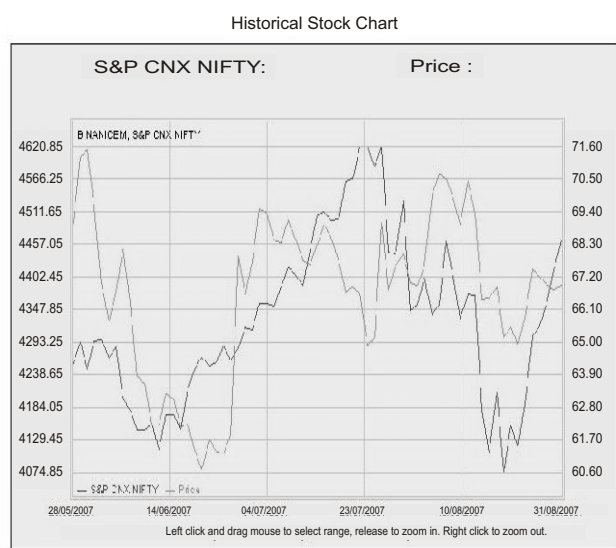


Chart Showing Movement of the Price of the stock and the S&P CNX Nifty over a period of three months from the date of listing of the IPO

The subscription pattern indicates that the over subscription in case of the Retail Investors and the QIBs is almost the same and this indicates that on a whole, this sort of stock can be expected to perform or not perform in the long run. The graph above substitutes this particular fact as the stock seems to be continuously out performing and underperforming in an alternative way during the three months the stock was listed. This sort of stock can be referred to as a neutral one and this sort of a stock may or may not be the best option for either a long term investor or speculator.

ALLIED COMPUTERS INTERNATIONAL (ASIA) LTD SUBSCRIPTION PATTERN

Category	No. of Applications	No. of Shares	Subscription
Qualified Institutional Buyers	5	35,00,000	7
Non-Institutional Investors	147	53302000	32.9
Retail Investors	18296	96397500	33.47
Total	18448	153199500	30.63



Charts Showing Movement of the Price of the stock and the BSE Sensex over a period of three months from the date of listing of the IPO

The subscription data shows that in the case of this company, the major amount of oversubscription is in the case of the Retail and Non- Institutional Investors. This along with the above graph shows that the stock initially out performed the market but after the mid of January, it has constantly under performed the market and represents a stock that is not best suited for a long term investor. Though this stock has been recently listed, it still does not represent a bright horizon of return.

TULSI EXTRUSIONS LIMITED IPO SUBSCRIPTION PATTERN

Category	No. of Applications	No. of shares bid	Subscription
Qualified Institutional Buyers	6	4313400	1.54
Non-Institutional Bidders	44	1481025	1.76
Retail Individual Bidders	10524	4533525	2.31
Employees	24	114000	1.14

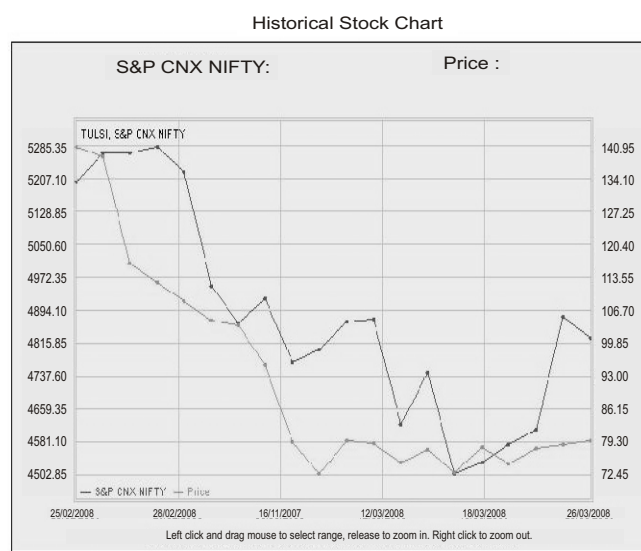
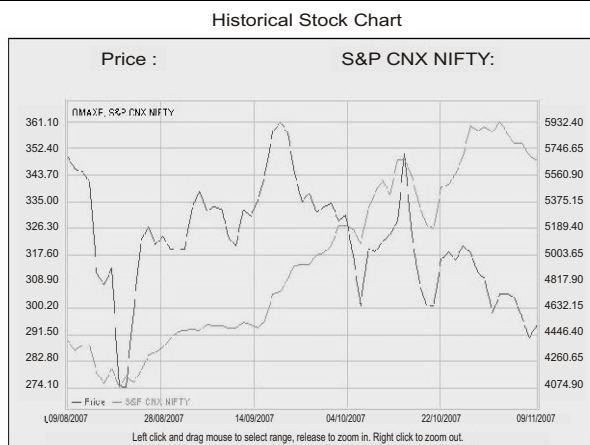


Chart Showing Movement of the Price of the stock and the S&P CNX Nifty over a period of three months from the date of listing of the IPO

The subscription pattern above shows that the amount of over subscription among all the categories is almost the same and the chart above shows that this stock has risen only twice in the last three months i.e. from the date of its listing, it matched the performance of the market and beyond that, it has always under performed in comparison to the market. This basically indicates that the stock may or may not be an ideal investment in the long run. Another factor that adds to this assumption is the fact that this stock has been recently listed and even the QIBs are not very confident about its performance.

OMAXE LIMITED IPO SUBSCRIPTION PATTERN

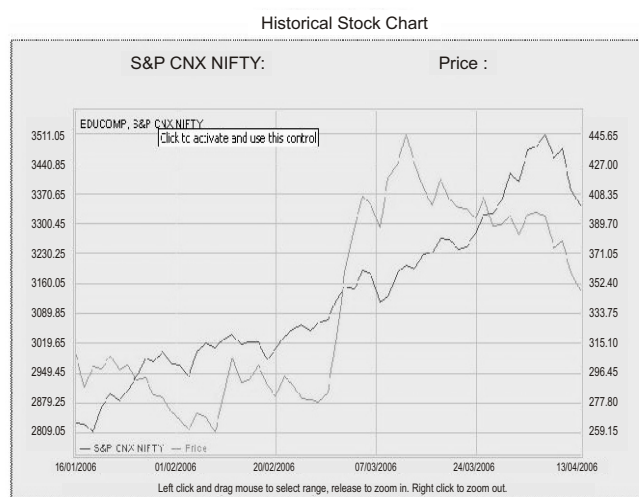
Category	No. of Applications	No. of Shares	Subscription
Retail Individual Bidders	456086	71586860	12.396
Non-Institutional Bidders	1642	138656620	72.0294
QIBs	287	1001317120	86.6941
Eligible Employees	529	336380	1.1344



The subscription chart shows that the QIBs have the maximum amount of over subscription and the chart above shows that from the 3rd month of listing that is from 4th October onwards, the stock has been constantly outperforming the market and this is a very good sign for the long term investors and an even better signal for the proposed long term investors. This stock is sure to do well because the QIBs have the maximum amount of confidence in it which is evident from the amount of over subscription by them.

EDUCOMP SOLUTIONS IPO SUBSCRIPTION PATTERN

Category	No. of Applications	No of Shares Bid	Subscription
Retail Individual Bidders	96283	30127152	211.5193
Non-Institutional Bidders	240	48915925	81.5265
Qualified Institutional Buyers	87	56356500	28.1782
Total	96610	135399677	33.8488



The subscription data reveals that the over subscription figures are highest among the Retail and Non- Institutional Investors but the amount of over subscription by QIBs is also quite high though not in comparison to the other categories but in general. The stock of such a company (which is based on a whole new concept), the QIBs have substantial amount of faith in its longevity. The chart also shows that the company has, on a number of occasions, outperformed the market and is likely to perform better in the long run as the concept of the company's product matures. Thus, this stock may, and as a matter of fact, has turned out to be a good investment prospect if seen in the light of the market conditions today.

CONCLUSION AND HYPOTHESIS

The entire analysis and the study was undertaken with the objective of assessing the price behavior of the shares of the companies which have come out with Initial Public Offerings in the recent past. In order to be able to make a fast and an easy assessment, the figures have been summarized in Table I.

SUMMARIZED DATA FOR ALL THE COMPANIES

PARTICULARS	CINEMAX	ALPA	KOUTONS	NISSAN	BURNPUR	NAUKRI	ARIES	BINANICEM	ACIASIA	TULSI	OMAXE	EDUCOMP
Issue Price	155.00000	68.00000	415.00000	39.00000	12.00000	320.00000	130.00000	75.00000	12.00000	85.00000	310.00000	125.00000
Correlation Between Market and Stock	0.71442	-0.79667	0.24014	0.41316	0.92515	0.71527	0.92571	0.43161	0.64562	0.85521	-0.22428	0.75706
Probable Error	0.03892	0.02988	0.07543	0.07162	0.01287	0.04024	0.01351	0.06607	0.04583	0.04051	0.07945	0.03717
Correlation/Probable Error	18.35676	26.66074	3.18356	5.76878	71.86298	17.77302	68.50784	6.53226	14.74292	21.10983	2.82285	20.36795
Mean Price of Stock	138.59028	24.44338	795.16218	52.62541	30.86316	641.44851	163.72843	66.66159	48.63672	92.25250	322.26231	338.36917
Average Return	0.15142	-0.56599	0.72033	-1.68293	-1.13087	0.21648	-1.22062	-0.02335	0.14045	-2.59535	-0.20083	0.43337
Standard Deviation	5.10171	3.16899	4.06731	4.19581	6.93413	3.31198	6.29819	2.15678	5.52583	6.68767	3.47632	4.41135
Coefficient Of Variation	33.69321	-6.39407	5.64647	-2.49316	-6.13167	15.29932	-5.15984	-92.38187	39.34448	-2.57679	-17.30991	10.17916
Standard Deviation (15 Days)	8.82488	5.59262	6.36533	3.99800	10.77811	3.00035	10.51934	2.17206	6.74203	6.76047	5.23663	3.69810
Standard Error (15 Days)	12.27857	1.44401	1.64352	1.03228	2.78289	0.77469	2.71608	0.56082	1.74079	1.74555	1.35209	0.95485
Test Of Significance (15 Days)	7.20175	16.31335	231.91819	13.19935	6.77825	414.94030	12.41805	14.86815	21.04608	4.15486	9.06914	223.45919
Beta	1.81846	0.75684	1.05979	0.53941	1.35446	0.85203	1.09684	0.51768	0.43705	0.94887	0.99948	1.94948

SUMMARIZED DATA OF OVER SUBSCRIPTION FOR ALL THE COMPANIES

CATEGORY	CINEMAX	ALPA	KOUTONS	NISSAN	BURNPUR	NAUKRI	ARIES	BINANICEM	ACIASIA	TULSI	OMAXE	EDUCOMP
Retail Individual Bidders	15.4395	1.6740	15.4395	4.2800	15.5100	12.1851	6.1600	1.4070	33.4700	2.3100	12.3960	211.5193
Non-Institutional Bidders	42.8084	1.9120	42.8084	20.2300	15.5100	66.7008	5.7300	0.2765	32.9000	1.7600	72.0294	81.5265
QIBs	60.6207	0.1780	60.6207	1.5100	0.0000	84.1985	7.5800	1.3253	7.0000	1.5400	86.6941	28.1782
Eligible Employees	1.0680	0.0220	1.0680	0.5200	1.1500	0.2529	0.0000	0.0000	0.0000	1.1400	1.1344	0.0000

Table I

The Correlation between the market and the scrip has been derived so as to assess the relationship between the market and the scrip. The ultimate purpose is to track the behavior of the price of the scrip in the market. The figures of Correlation show that only Alpa Laboratories and Omaxe have had a negative correlation. Thus, these companies have given more emphasis to the specific factors of the company in comparison to the others who discounted the share price of the scrip along with other existing players. The Probable Error and the ratio between the Correlation and the Probable Error are a mere extension to check the relevance of the Coefficient of Correlation. As per the statistical rule, if the Ratio of Correlation to probable error is greater than or equal to 6, the Coefficient of Correlation is an appropriate, accurate and significant measure. The above figures reveal that except for Koutons, Nissan Copper and Omaxe, the coefficient of correlation for all other companies is a relevant measure. Taking into account these factors, it can easily be concluded that Cinemax, Burnpur Cement, Info Edge, Aries Agro, Tulsi Extrusions and Educomp Solutions are the companies which are likely to move in tandem with and respond to the market efficiently and effectively.

The mean price of each stock for a period of three months has been calculated in order to assess whether the issue price is over or under priced. The figures that have been calculated show that barring Cinemax, Alpa Laboratories and Binani Cement, the issue price of all other companies is under priced. Though this is a positive indicator from the investors' point of view, as he/she stands to gain further more at the end of the day, but as a whole, it reflects the uncertainty that the company has about its own level of success and achievement.

The data was further analysed using statistical tools like Average Return, Standard Deviation and Coefficient of Variation. The Standard Deviation and Coefficient of Variation represent the level of risk. As per the figures above, Koutons represent the best combination of risk and return. If one compares the risk and the level of return with the amount of over subscription, one major fact that comes to the forefront is that the companies which have been highly oversubscribed by the QIBs are actually the ones which have the best combination of risk and return- be it Cinemax, Koutons, Info Edge, Allied Computers or Educomp Solutions. This is a major factor which can be taken into account while selecting a stock in the secondary market especially from the investment point of view. However, a company like Omaxe has only shown a marginal level of negative return for a decently high level of risk because of the negative correlation with the market. However, the high level of over subscription by the QIBs is what gave this share the stability and allowed for a very low level of negative return.

The next set of figures, which assist in making the analysis more accurate, are Standard Deviation, Standard Error and Test of Significance. All these figures have been calculated for a period of only 15 days so as to ensure that there is no unusual impact due to the market factors. These have been calculated to find whether there is a

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(Contd. from page 11)

significant difference between the Issue Price and the Mean Price of the stock for 15 days. The statistical rule says that the Test of Significance should be greater than or equal to the value of 2.58 to conclude that there is a significant difference. The above calculated figures enforce the fact that in all the cases, there is a significant difference because all the figures are greater than 2.58 and the issue is either over or under priced. The value for the test of significance is relatively higher in case of the companies which have a high level of over subscription by the QIBs as can be seen in the case of Koutons, Info Edge, Allied Computers and Educomp Solutions. This only goes to show that the companies in which the QIBs have confidence tend to outperform their own expectations which cause the issue price and mean price to differ significantly.

The last part of our analysis is about the Beta, which in this case signifies the movement of the stock vis-a-vis the entire market. A stock with a high Beta denotes that the stock has been included in the list of stocks being traded by the market participants in routine. This helps us to understand one fact that all the companies that have a high beta in our analysis (be it Cinemax or Koutons or Info Edge or Omaxe or Educomp Solutions) represent a stock that is popular among the players. If one looks at the figures of oversubscription, it is clearly indicated that the above stocks are mostly oversubscribed in large quantities by the Qualified Institutional Buyers and have relatively been the best performers if looked at from the perspective of long term investment. Thus, a stock with a Beta of approximately 1 or greater than 1 represents a safe investment option as indicated by the holding of the Qualified Institutional Buyers of the same.

All this analysis along with the analysis of the chart of each individual company has come to reveal one major fact and conclusion that the Subscription pattern is in fact one of the ways to judge the performance of the stock. The QIBs represent those set of people who do not gamble in the market but look at it as an investment opportunity which has the capability of being assessed and forecasted. However, it cannot be regarded as a rule, as there are always some exceptions to the rule in the real world. But it provides a parameter to the investors in securities market that will help them safeguard their investments and long term interests in the best possible manner.

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