

**AN EXAMINATION OF THE UNDERPRICING OF INITIAL
PUBLIC OFFERING IN KUALA LUMPUR STOCK EXCHANGE**

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Abstract

Previous studies have documented that initial public offerings (**IPOs**) are typically **underpriced**. This dissertation has two major objectives. First to test the existence of **underpricing in the Kuala Lumpur IPOs**. The study by Dawson (1987) is extended by **industry-specific** sub samples, with the aim to determine whether different business sectors show a significant difference in underpricing levels. Second to study Rock's(1986) information asymmetry model of underpricing. The **findings** show that underpricing phenomena of **IPOs** occurs in the Malaysian market, **with** the industrial sector contributing the most to the overall underpricing and is found to be **significantly different** from other sectors. Using the proxies for ex-ante and ex-post uncertainty, the study tends to explore the relationship between the level of underpricing and the uncertainty surrounding the new issues. The results support the proposition by **Beatty & Ritter** (1986) that the level of underpricing is positively related to the uncertainty surrounding the new issues.

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1. INTRODUCTION

The existence of underpricing for initial public offerings (**IPOs**) of common stock appears to be a recurring phenomena across major capital markets. Previous studies indicate that the **underpricing** occurs across a number of **different** time periods and samples (**McGuinness**, 1992). In Malaysia, a study by Dawson (1987) for twenty one **IPOs** for the period 1978-1983 provides similar evidence.

This study is a replication of **McGuinness's** (1987) study. For the **IPOs** in the **Kuala Lumpur** stock market, the level of underpricing, as well as possible explanations of the underpricing phenomena are determined. Furthermore, this study extends Dawson (1987) by using a larger sample from a more recent time period.

This study has two major objectives. First, to determine the level of underpricing for newly listed shares in the Kuala Lumpur Stock Market for the period 1990-1993. In total sixty six **IPOs** were analysed which compares favourably with the twenty one issues **scrutinised** during the period 1978-1983 in Dawson (1987) for the same market.

The previous study by Dawson (1987) is extended by splitting the sample of **IPOs** into industry-specific sub-samples. It is aimed to allow comparisons of underpricing levels across **different** business sectors. Further, the market index used to adjust for the price movement **differs** from Dawson (1987). Instead of using the **KLSE Industrial Price Index** as in Dawson (1987), the current study uses the **KLSE Composite Index**. The results are compared so as to identify any significant differences in the results when using different indices.

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