

The Influence of the Reputation of Finance Intermediaries on IPO Underpricing in China Growth Enterprise Markets (GEM)

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Abstract

Growth Enterprise Markets (GEM) in China was established in October 30, 2009. The paper analyses the underpricing effects and IPO stock's first month, first quarter return in GEM of China, researches nearly 150 listed company in GEM. Its finds weak reputation effects of finance intermediaries on IPO underpricing and periods returns. This shows the failure of information generation function and failure of certificate function of finance intermediaries in new emerging market in China.

Key words: Growth enterprise market; Underpricing; Reputation of finance intermediaries; Information generation; Information certification

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INTRODUCTION

With the development of information economics and game theory, research on the reputation of economics attracts more attention. Stock market is a typical unsymmetrical information market. Issuing company gets more understanding of listed company's finance status, operating performance and perspective than individual

investors which often leads to adverse selection. To avoid this adverse selection, the syndicate of enterprise hope to pass the information of its enterprise to market investor effectively. Thus, they select the accounting firm, investment bank and venture capital group to identify the entrepreneur reputation, so the reputation of financial intermediaries works. For the Reputation of Finance Intermediaries on IPO, Liu Yixun, compares the underpricing of venture backed and non-venture backed IPOs in China; discovers that the venture backed IPOs in China tend to underprice more than non-venture backed their counterparts^[1]. Weber J & Willenborg M. find that the pre-IPO opinions of larger auditors are more predictive of post-IPO negative stock delistings, expert informational intermediaries add value^[2]. Jerry Coakley, *et al.* present a paper on UK IPO underpricing and venture capitalists^[3], a Many articles do research on reputation of underwriter on underpricing of IPO and long term effects^[4-11], the paper does research on reputation effects of key financial intermediaries, underwriter, accounting firm, venture capital group. From analysis it found no significant effects of financial intermediaries on IPO underpricing, but for IPO stock's first month and quarter return effects, they play a function, the empirical analysis show us the efficient of "information generation function" and "identification intermediary function" in china market.

METHOD

Take the data of 150 listed company in GEM as research sample, data resources comes from CSMAR database <http://www.gtarsc.com/>; reputation of accounting firm comes from <http://www.cicpa.org.cn/>, take comprehensive ranking during 2006-2010, take reputation variables for first 10 higher reputation firm as 1, rank 10-20 as 2, the others as 0. the regular approach to measure the reputation of underwriter comes from <http://www.weihai.com.cn>, take the reputation variables for first 10 higher reputation

firm as 1, rank 10-20 as 2, the others as 0. the rank for venture capital group comes from <http://www.pedaily.cn/report/322/Index.aspx>, the reputation variables for first 10 higher reputation firm as 1, rank 10-20 as 2, the others as 0. Sample data comes from 150 listed company in GEM market, china, using multifactor analysis to check the return effects of IPO and the return effect for first month,

first quarter.

Endogenous variable: return of underpricing, return of ipo stock's first month, return of first quarter Exogenous variable: reputation of underwriter, reputation of accounting firm, reputation of venture capital firm.

We take ANOVA, the analysis of variance in this paper.

Table 1
Reputation Rank for Financial Intermediaries

Code	IPO	Month	Quarter	Underwriter	Under1	Accounting	Acc-firm	Investment-group	Inve-group
300001	0.848739	0.071898	-0.12938	GF securities	1	Shandong huide	3	Qingdao derui	3
300002	0.774138	0.923876	1.012212	cities	1	lixing	1		3
300003	1.186207	0.81213	-0.89426	Cinda securitise	3	daxing	1	csis	3
300004	0.75841	-0.022305	-0.22458	Essence securities	2	Guangdong zhengzhong pearl river	3	Chongqing science and technology	3
300005	1.528788	0.049578	0.15065	Dongxingsec	3	lixing	t1	liding	3
300006	1.169697	-0.27272	-0.32569	Guojing securities	3	Sichuan huaxing	3	investment group	3
300007	0.804074	0.343917	0.310726	Guojing securities	3	zhonglei	2		3
300008	0.827698	0.125274	0.162016	Guojing securities	3	lixing	1	Shanghai jiachuan	3
300009	1.945882	-0.20892	-0.24039	Guojing securities	3	Huapu tianjian	3	Jianshu gaoda	3
300010	0.875	-0.07716	0.26795	Sealand securities	3	Beijing jingdu tianhua	2		3
300011	0.865135	0.584336	0.890745	Industrial securities	3	daxing	1	China vc investment	3

In table 1, under1 denotes the reputation for underwriter, acc-firm denotes the reputation for accounting firm, and inve-group denotes the reputation for investment group.

EMPIRICAL RESULT

Table 2
The Analysis of Underpricing Effects of Financial Intermediaries

Test of between subjects effects

Source	Dependent	Sum of square	df	Mean squar	F	Sig.
Correct model	IPO	1.524a	15	.102	.614	.860
	Month	6.078b	15	.405	1.169	.303
	quarter	6.460c	15	.431	1.296	.213
Intercept	IPO	2.800	1	2.800	16.924	.000
	Month	.151	1	.151	.434	.511
	quarter	.374	1	.374	1.125	.291
under1	IPO	.173	2	.087	.524	.593
	Month	.491	2	.245	.708	.494
	quarter	.494	2	.247	.743	.478
accfirm	IPO	.290	2	.145	.878	.418
	month	.750	2	.375	1.082	.342
	quarter	1.234	2	.617	1.857	.160
invegroup	IPO	.425	2	.212	1.283	.280
	Month	.269	2	.135	.389	.679
	quarter	.524	2	.262	.788	.457

To be continued

Continued	Source	Dependent	Sum of square	df	Mean squar	F	Sig.
	under1 * accfirm	ipo	.251	4	.063	.380	.823
		month	2.998	4	.749	2.162	.076
		quarter	2.650	4	.662	1.993	.099
	under1 * invegroup	ipo	.080	2	.040	.240	.787
		month	.600	2	.300	.865	.423
		quarter	.717	2	.358	1.078	.343
	accfirm * invegroup	ipo	.253	2	.126	.764	.468
		month	1.987	2	.994	2.867	.060
		quarter	2.791	2	1.395	4.198	.017
	under1 * accfirm * invegroup	ipo	.058	1	.058	.351	.554
		month	1.698	1	1.698	4.900	.029
		quarter	2.301	1	2.301	6.923	.009

Table 2 shows the effects of individual variables and the effects of the combined variables.

CONCLUSION

The empirical finding is that different financial intermediaries have different influence on return of IPO, return of first month, and return of first quarter.

1) For IPO underpricing return, there is no significant difference between the IPO stock's first month return and first quarter return for each financial intermediaries's reputation.

2) For first month and first quarter return the combined effects of underwriter and accounting firm, accounting firm and venture investment group work in 0.1 significant level.

3) For first month and first quarter return, the combined effects of underwriter, accounting firm and venture capital group works in 0.05 significant level.

In theories, for a security market, if reputation effects works, higher reputation financial intermediaries have negative correlation with IPO underpricing. But empirical result is that for GEM in china, financial intermediaries don't play signal deliver function well, reputation mechanism have less effects in china stock market. Its totally different from the negative correlation of IPO underpricing effects in mature European and U.S market. The reduction of the reputation of financial intermediaries exist in china. The reason comes from many parts, some from institutional imperfection, some from market structure imperfection, and some from supervision imperfection. So it shows the deficiency of the reputation mechanism, behavior anomie, distortion of market function. but the combination effects of top underwriter, accounting firm and venture capitalists works.

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