“Institutional investors’ role in implementing book building: Views of market participants”

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INSTITUTIONAL INVESTORS' ROLE IN IMPLEMENTING BOOK BUILDING: VIEWS OF MARKET PARTICIPANTS

Abstract

The aim of this paper is to assess the views of market participants concerning the institutional investors' role in implementing book-building pricing of IPOs as Nepal seeks to implement it. A total of 125 market participants were approached for data collection using a structured questionnaire that took a six-month period from January to June 2020. Descriptive and inferential statistics were employed to analyze the collected data. The study found that the role of institutional investors in the prevailing stock market is brutally meager because of the restrained regulatory provisions. Market participants opined that institutional investors play a vital role in developing the stock market and executing book building. Implementation of book building demands a rigorous amendment in the existing regulations that allow institutional investors to enter and play in the market. A precise classification and definition of the potential roles of institutional investors are essential so that the application of the building pricing mechanism could be expected to be more effective. Market participants believed that the active participation of institutional investors will help lure manufacturing and real sector companies, trading houses and hotels into the capital market for public offerings. Issue managers, portfolio managers, share registrars, and stockbrokers agree that the role of institutional investors is inevitable in implementing book-building pricing.

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INTRODUCTION

The capital market deals in borrowing and lending long-term funds via financial assets or securities that corporations need. It is also known as the securities market. Institutional investors are one of the major participants facilitating securities market transactions and are also known to be a pillar of developing the market. They are, of course, in the form of mutual funds, pension funds, hedge funds, insurance companies, and different types of investment funds. They are professional investment institutions. Being professional investors, they have an optimistic stimulus on the pricing and long-term growth of securities markets. Institutional investors are well-trained and have considerable resources compared to individual investors, and they are also able to make informed decisions. As they are informed traders, they can adjust the price of shares to fresh information, thereby promoting the market relatively in an efficient manner. They play a crucial role, particularly in pricing new issues, especially under the book-building method, by actively participating in roadshows organized by underwriters. Consequently, the price of initial public offerings becomes competitive and market-friendly. In this regard, Nepal is currently launching a book-building pricing mechanism in the primary market, where the role of institutional investors is expected to be decisive. Thus, a study of this kind would certainly offer some key ideas about the roles of institutional investors as well as directions for the effective implementation of book-building pricing in the primary market of Nepal.

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1. LITERATURE REVIEW

Institutional investors are the market players that deal with funds to buy and sale financial securities like bonds, stocks, forex, foreign contracts, etc. They often trade in large volumes of securities and provide market liquidity and stability (Bohl et al., 2006). They play a crucial role in the long-term growth of the securities market and the pricing of securities in particular. Therefore, many developed and emerging markets used to contemplate due consideration to increase the participation of institutional investors in the capital market.

The presence of institutional investors in the capital market is important in various ways. Rock (1986) states that institutional investors have played an indispensable role in the pricing of initial public offerings (IPOs) and their allocations. Rock further argues that they pose superior confidential information about issuing firms and about the market's expected valuation of the stock. Kumar (2008) advocates that they are professionals who also have information about competitors, suppliers, customers, and general economic and market conditions. More importantly, they have private information about issuing firms, which helps determine their willingness to pay for IPO shares so that issuing firms will also be ready to sell IPO shares at a price close to their value. However, when investment bankers organize roadshows to publicize imminent offerings, institutional investors transfer their interest in terms of indications of interest on both price and quantity to purchase because they have valuable intuitions about the market demand for the security as well as the forecasts of a firm and its competitors. When the book is built, and the offer price is fixed, then the investment banker/underwriter has a considerable choice over distributions of IPOs. Generally, they allocate shares to those investors who aided in determining the price of the offering and who have long-term affiliations (Jagannath et al., 2010). Institutional investors thus contribute to the pricing of IPOs since they have private information about the issuing firms.

As institutional investors provide positive information during roadshows, then firms set IPO offer prices lower to provide profit to reimburse investors (Benveniste & Spindt, 1989). Chemmanur et al. (2010) also agreed that institutional investors have abundant information about IPO issuing firms and that underpricing is an instrument for compensating them for revealing confidential information (Setia-Atmaja & Chandera, 2021). Thus, underwriters need to propose the security at a reduced price to these investors to encourage them to buy shares under a book building. Bulk IPO allocation to institutional investors does serve as a useful economic information gathering tool. Both underpricing and allocation of more IPO shares are, of course, a truth-telling reward to institutional investors (Bodie et al., 2011). Thus, Kamath et al. (2022) stated that higher underpricing and allocation of more IPOs to institutional investors is the common phenomenon for their valuable contribution to the primary market.

Institutional investors' investment in IPOs is appreciated in better valuation of stocks. A study of 450 IPOs by Ong et al. (2020) listed in Bursa Malaysia from 2000 to 2018 documented that there was a positive association between institutional ownership and IPO valuation. It signals that the presence of institutional investors delivers information on firms' future potentials, which in turn is considered a fair valuation of IPOs. They also revealed that IPOs valued under book building had greater institutional ownership that is priced more reasonably and closer to the intrinsic value, thereby allocating a greater number of shares to them. They are also effective in stabilizing the market prices of IPOs in the aftermarket.

Huyghebaert (2004), using data on initial public offerings (IPOs) in Belgium, showed that companies that view the stock market as a means of raising funds and companies that receive less attention from corporate block-holders are more likely to allot equities to institutional investors during the IPO process. Allocating shares in advance to institutional investors helped decrease underpricing and improve post-IPO liquidity in the markets. Chemmanur et al. (2010) found that institutional investors possess predictive ability about the long-term profitability of IPOs and get substantial remuneration for their involvement in IPOs. Therefore, the participation of institutional investors in the market decreases the level of initial returns, enhances liquidity following an initial public offering (IPO), and sustains long-term success.

Institutional investors enhance the stock market by assigning value to IPO stocks. Gao et al. (2017) revealed that institutional investors tend to overestimate the value of IPO businesses. This leads to an increase in the IPO offer price and a decrease in the first-day returns, indicating that IPO firms are not maximizing their potential profits. In a similar vein, Dumrongwong (2020) found that institutional ownership is negatively correlated with early stock returns, suggesting that it contributes to the stability of stock markets. These findings suggest that institutional investors possess confidential knowledge that they use to accurately assess the value of initial public offerings (IPOs). As a result, this minimizes the early returns and minimizes the amount of money that remains unclaimed during IPOs.

Engaging in flipping operations is the most prevalent method for rapidly acquiring substantial earnings from initial public offerings (IPOs). Che-Yahya et al. (2014) found that the involvement of institutional investors plays a crucial role in regulating flipping operations in the IPO market. In addition, a study by Gao et al. (2017) revealed that institutional investors had the capacity to identify instances of pre-IPO profit manipulation, which in turn compelled IPO businesses to establish a reduced offer price. Neupane and Poshakwale (2012) discovered that when institutional investors with below-average performance show less interest in IPOs, retail investors are able to achieve a substantial initial return on their investments. Therefore, a significant presence of institutional investors who allocate a larger portion of IPOs helps to uphold the equitable valuation of IPOs in the market. Regarding mutual funds, Lakshman et al. (2013) discovered that mutual fund managers had a greater inclination to follow the crowd compared to other institutional investors. This behavior contributes to volatility in the IPO market. In general, market authorities constantly supervise the activity of mutual funds.

The introduction of anchor investor rules in 2009 in the Indian stock market aimed to facilitate the price discovery process during book building. Kumar and Sahoo (2021) found that IPOs have lower performance over a lengthy period of time while anchor regulation was in effect in India. Specialized institutional investors are confirmed to contribute to the reduction of information asymmetry, which in turn leads to a decrease in long-term returns. Further, Sharma et al. (2024) documented that anchor-backed firms reveal higher operating performance after the IPO since they also play a monitoring role in the firms. In addition, Hanley and Wilhelm (1995) found that institutional investors receive a significant portion of the immediate gains associated with IPOs. They derive pleasure from purchasing undervalued products and will also participate in less appealing opportunities. These findings provide evidence for the notions of winner's curse and validate the practice of book building.

In Nepal, the history of the institutionalization of the securities market started with the establishment of the Securities Exchange Center (SEC) in the year 1976 under the Company Act, 1951. SEC aimed to mobilize public savings and encourage people to participate in the ownership of industries and businesses. SEC has undertaken both new issues and managed the sale of the shares and debentures as well as listing shares and debentures to qualify for trading (Timilsina, 2004). Later, His Majesty's Government established the Securities Board of Nepal (SEBON) in 1993 as an apex regulator of the securities market, and Nepal Stock Exchange Limited (NEPSE) with the aim of inducing organized and systematic dealing of securities. Though the Nepali new issue market has a long history, the market has yet to develop since it has been adopting a conventional method of IPO pricing to date namely the fixed price method.

Regarding institutional investment, Citizen Investment Trust (CIT) was established as an institutional investor in Nepal after the country's economic liberalization in 1990. It played a pioneering role in developing the share market by acting as a market maker. Nevertheless, the organized institutional functioning as market makers were not efficient right from the beginning (Koirala & Bajracharya, 2004). The Government of Nepal has well recognized the role of institutional investments for the securities market development, in the country since the Eighth Plan (1992–1997) period. The participation of institutional investors like mutual funds, pension funds, employees' provident funds, insurance companies, etc., in the market has been encouraged by incorporat-

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ing necessary provisions in the long-term national plans. Within the plan period, the Citizen Unit Scheme and NCM Mutual Fund were brought into operation in the securities market. The programs were announced to encourage domestic and foreign institutions to operate mutual funds in the Ninth Plan (1997-2002) period but were not implemented. The provision of institutional investment made in the Eighth Plan has still been awaited in practice. More recently, the Fifteenth Plan (2019/20–2023/24) of the National Planning Commission (NPC) accepted the challenges, and opportunities of bringing institutional investors into the capital market, and the government has assumed a strategy to increase the attraction of small and domestic and foreign institutional investors. However, the operational policies of the strategy ignored defining the procedures to be followed for bringing institutional investors into the stock market. This implies that the importance of institutional investors in the securities market is less talked and their participation is also negligible in Nepal.

In the regulatory regime, the term "institutional investors" has not been well-defined by the associated regulations in the securities market. Institutional investors, as stated in the Eighth Plan, had no flexibility in their rules to invest in the primary market securities. For instance, the Employees' Provident Fund (EPF) was allowed to invest only in promoter shares of banks and financial institutions (BFIs). At the same time, Citizen Investment Trust (CIT) has no clear mandate for investing in IPO shares. There is a provision of quota of only five percent share of IPOs to the mutual funds. Insurance companies were allowed a very nominal amount of their total investible funds in the equity market. In the later period, Securities Allotment Guidelines 2011 roughly defined investors into two categories viz. "retail investors," who invest in securities worth less than Rs.50,000/- and "other investors," which include all the investors who employed the amount greater than Rs.50,000/- in the securities. The restrained regulatory provisions, as such, imply that the role of institutional investors in the Nepali securities market has almost been ignored though they are crucial for the development of the capital market.

The extant literature revealed that the active participation of institutional investors is essential in capital market development and its stability. Their roles seem exclusively prominent especially in the primary market while discovering IPO prices. From the very beginning, the Nepali market has been implementing the fixed price method of IPO valuation, in which very little effort has been paid to introduce institutional investors into the market. Because of this, the market could not be extended to the desired level, and the size of the market is still limited to its narrow base with the banking sector initially after the liberalization, privatization, and globalization wave of the 1990s followed by the hydropower sector in the later period. Manufacturing and real sector companies, trading, hotels, and many other sector companies are still rarely present in the capital market. They fear going public because they should leave a huge sum of money on the table as well as loss of control through the existing pricing method. As such, the active participation of institutional investors and the introduction of the market-based pricing of IPOs in the market could be the prime agenda in the days to come in Nepal. There is no room for laying-off only in conventional practices as the international market has been becoming complex and highly competitive, which motivated the researcher to undertake the study on the issue at hand in the context of Nepal. So far, very few empirical studies have been found in the area of the new issue market. Moreover, exploring the roles of institutional investors in the stock market as a whole and a fair price determination of IPOs in the new issue market is almost nil. Therefore, this study could be one of the important studies that might guide policymakers to formulate policies conducive to book-building pricing and motivate market participants to contribute to the implementation of the new pricing mechanism. More specifically, this study will help encourage institutional investors to participate in the market and thereby implement book-building pricing in Nepal.

2. METHODOLOGY

To analyze the significance of institutional investors in the IPO markets, the study mainly employed a descriptive research design. This enabled us to understand the existing practices and potential role of institutional investors in Nepal's new issue markets. This study has used a structured questionnaire, which is distributed to each of the

Table 1. Respondent types, population, questionnaire distribution, collection and response rate

Source: Questionnaire survey 2020.

Respondent type	Population*	Questionnaire distribution	Collection of filled-up questionnaire	Response rate
Issue manager	22	20	18	90.00
Share registrar	23	20	20	100.00
Portfolio manager	29	25	20	80.00
Mutual fund	11	11	9	81.81
Stock broker^	50	30	27	90.00
Retail investors^^	–	35	31	88.57
Total	–	141	125	88.65

Note: * As per SEBON annual report 2019/20. ^ Stock brokers are not directly involved in primary market operations so only those who have expertise in primary market activities were chosen as samples. ^^ Retail investors comprised only those primary market experts having strong academic backgrounds in the market and few others are regular market players in IPOs.

merchant bankers, stockbrokers, and some other participants by physically visiting their workplaces. Before the distribution of the questionnaire, the preliminary testing of the questionnaire was made among five prospective market participants to examine its validity. With minor changes being made in the questionnaire, a total of 141 questionnaires were distributed, and 125 responses (88.65 percent response rate) were received from market participants. Table 1 presents the details of market participants, questionnaire distribution and collection, and the response rate.

The collection of the filled-up questionnaire through frequent visits and a series of phone calls of several times became quite difficult. However, the survey data were obtained by "delivery and collection" methods. A six-month period of January to June 2020 has been spent in the course of data collection.

The survey instrument 'questionnaire' employed in the survey included three major sections, including respondents' profiles followed by multiple-choice questions to measure the market participants' views towards institutional investors' role. The final section asks about the level of agreement and/or disagreement associated with the potential roles of institutional investors in the IPO market while implementing a book-building pricing method. The development of the items was done by intensive re-evaluation of the theoretical and empirical literature related to the issue for the utmost validation. A total of eight Likert scale items were set, as shown in Table 2.

The respondents were asked to rate their views on a five-point scale ranging from 1 to 5, with 1 = "strongly disagree," 2 = "disagree," 3 = "neither disagree nor agree," 4 = "agree," and 5 = "strongly agree."

Several software programs, including Microsoft Excel version 10 and the Statistical Package for Social Science (SPSS) version 25, were used to code and analyze the gathered replies. In particular, eight Likert scale items pertaining to the possible involvement of institutional investors were used to gauge the questionnaire's reliability using Cronbach Alpha. To better understand the existing situation and possible responsibilities of institutional investors in the stock market – and the

Table 2. Likert scale items concerning the potential roles of institutional investors

Code	Item
q1	Institutional investors are well in understanding issuing firms along with their business operations
q2	Institutional investors are proficient in the fundamental valuation of firms that guide them to estimate price bands
q3	Institutional investors can guarantee to subscribe to the IPOs as they demonstrate indications of interest during roadshows
q4	Institutional investors are expected to have abundant knowledge to comprehend the risk of the markets and act accordingly
q5	The participation of institutional investors in the capital market induces manufacturing and real sector firms to enter the capital market because of their expertise role and massive investment in IPOs under free pricing like book building
q6	Institutional investors' expertise and skills can be valuable to individual retail investors regarding fair pricing of IPOs
q7	Institutional investors, like mutual funds, invest substantial amounts in various portfolios of securities that benefit small investors indirectly under book-building pricing
q8	Institutional investors need enough flexibility in their regulations relating to an investment in IPOs under book-building

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implementation of book-building pricing in particular – the data were analyzed using both univariate and bivariate descriptive statistics. The definition of the features and evaluation of the possible roles of institutional investors were done using the following metrics: frequency, mean, standard deviation, percentage, minimum and maximum values, and inter-item correlation coefficient. A one-way ANOVA test was utilized to evaluate the divergent opinions among market players about the possible contributions of institutional investors to the implementation of book-building pricing in Nepal.

The eight items were first analyzed for internal consistency (reliability) using the SPSS facility to construct the scale of institutional investors' potential roles. Reliability analysis, with a Cronbach alpha value of 0.783, shows that removing any item does not increase the scale's reliability (Burns & Burns, 2008), meaning all eight items are retained to construct the scale. The summated scale of institutional investors' potential is built using the SPSS facility.

After constructing the scale, it is important to explore if there is any problem in the constructed scale, such as outliers and non-normality of data points, and if the parametric methods could not be used with great safety. The standardized value of potential roles of institutional investors scale, i.e., the z-score of the scale, varies from a minimum value of –1.805 to a maximum value of 1.719, which is within the range of ±3, implying that there were no outliers in the scale. Histograms and plots of the scale also indicate that the scale values were also normally distributed.

3. RESULTS

3.1. Institutional investors' role

This section deals with the roles played by the institutional investors in the primary market, in which 97 (77.6 percent) participants viewed the prevailing institutional investors' role is inadequate in the Nepal stock market. This implies that the presence of institutional investors is poor in the market, although their importance has been well-recognized in the various national plans of the government (GON NPC, 2020). Most market participants (66.0 percent) viewed institutional investors as the leading players in discovering prices under the building method. They believed that institutional investors are supposed to be well-equipped and have the ability and enthusiasm to work as the convincing force for corporate bodies to track effective governance. They also believe that they play a critical role in protecting small investors' investments.

One of the questions asked to the market participants was, "The role of institutional investors is crucial in the development of capital market and effective application of book building pricing in particular. Do you agree with this statement?" A large number of market participants (93.66 percent) believed that institutional investors played a crucial role in the growth of the capital market. Merely 6.40 percent of participants in the market expressed their ignorance of the significance of institutional investors in the capital market. Out of the three possible responses to the question, "Yes," "No," and "Don't know," none of the market participants chose the "No" option. This suggests that most participants well-known about the significance of intuitional investors in the growth of the capital market and price discovery under book building.

As mentioned in section two, the institutional investor base in the Nepali capital market is not very strong. Market participants suggested a vaviours forms of potential institutional investors in this regard. The market players that are advised to participate as institutional investors include Non-Residential Nepalese organizations (NRNs), merchant bankers, brokers, securities dealers, insurance firms, bank and financial institutions, mutual funds, holding corporations, citizens' investment trusts, and employment provident funds. They believed that institutional investors' involvement would aid in the market's development and the implementation of book-building pricing in Nepal.

3.2. Descriptive analysis of Likert items

Table 3 shows the computed mean value on each statement ranging from 3.125 to 4.061. Item q8, 'institutional investors need enough flexibility in their regulations relating to an investment in IPOs under book building', accounts for the highest mean score of 4.061 and standard deviation of 0.760. The flexibility in the regulatory framework helps them build a conducive environment for active participation in the market and foster their investment in IPOs. Item q6 ranked as the second important variable, and the institutional investors' potential role for the benefit of retail investors accounted for 3.801 mean scores with 0.780 standard deviations. Institutional investors are believed to be market specialists with expertise and skills in analyzing the market and providing factual information to the underwriters to determine a fair price. Consequently, retail investors will benefit by buying IPOs. They will likely to remain safer with the problem of adverse selection of IPO stocks suggested by Rock (1986).

Table 3. Descriptive statistics of each of the eight Likert scale items

Source: Questionnaire survey 2020.

Item	Mean	Std. Dev.	Range
q1	3.580	1.166	2-5
q2	3.668	1.210	2-5
q3	3.125	0.648	2-5
q4	3.609	0.928	1-5
q5	3.637	0.844	2-5
q6	3.801	0.780	2-5
q7	3.483	0.836	1-5
q8	4.061	0.760	2-5

Another important expected role of institutional investors as per the perception of market participants is that 'institutional investors are proficient of fundamental valuation of firms that guide them to estimate price band (q2), which accounts for a mean score of 3.668 and standard deviation of 1.210. 'Involvement of institutional investors in the capital market induces manufacturing and real sector firms to enter the capital market because of their expertise role and huge investment in IPOs under book building pricing' (q5) ranked number four. It implies that market participants believed that the active participation of institutional investors in the capital market is crucial because they exercise their expertise in creating awareness among stakeholders and are themselves participating in IPO investments, which creates an environment of investments and stability in the market. Consequently, it will help lure manufacturing and real sector firms to enter the capital market. Similarly, market participants believed that institutional investors are expected to have abundant knowledge to comprehend the risk of the markets and act accordingly (3.609). 'Institutional investors, like mutual funds, invest considerable amounts in the various portfolios of securities that benefit the small investors indirectly under book building (3.483), accounting for another essential role of institutional investors while adopting book building. This indicates that general investors who are not supposed to have direct access to the primary market can participate through mutual fund units when the IPOs are issued through book building. Moreover, mutual funds, as institutional investors, can process information more efficiently, which helps fair price discovery, which could also be beneficial for uninformed investors and the market as a whole.

Market participants also believed that institutional investors are well-equipped to understand issuing firms and their business. They can also guarantee that they will subscribe to the IPOs as they demonstrate indications of interest during roadshows. In this regard, Rock (1986) advocated that institutional investors have greater private information about firms issuing IPOs that the firm cannot express realistically. As such, they will have an important role in implementing book-building pricing and creating a pleasing environment for investment in Nepal's capital market.

3.3. Relationship analysis of Likert items

Table 4 presents an inter-item correlation matrix of eight items. The majority of items are positive and significantly correlated at the 0.01 level. The relationship between items q2 and q4 is highly positive (0.782) and influential, indicating that institutional investors are competent in the fundamental valuation of firms to estimate prices and are also capable of understanding the risk of the markets and acting accordingly. The results suggest that institutional investors are crucial players in the fair price discovery of IPOs and can learn about the risk associated with IPOs.

The relationship between items q1 and q2 is also significantly positive, implying institutional investors can extract information about issuing firms and fundamental valuations that ulti-

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Table 4. Inter-item correlation matrix of eight Likert scale items

Source: Questionnaire survey 2020.

Item	q1	q2	q3	q4	q5	q6	q7	q8
q1	1	0.699**	0.141	0.568**	0.369**	0.067	0.172	0.011
q2		1	0.379**	0.782**	0.579**	0.122	0.366**	0.248
q3			1	0.360**	0.445**	0.033	0.129	0.107
q4				1	0.398**	–0.069	0.359**	0.103
q5					1	0.210	0.213	0.123
q6						1	0.181	–0.025
q7							1	0.552**
q8								1

Note: ** Significant at the 0.01 level. Under book building pricing, Table 4 reveals a similar relationship among other variables, indicating that institutional investors' role is indispensable in implementing free pricing like book building.

mately assist underwriters in determining price bands in the book-building process, which is similar to the ideas of Chemmanur et al. (2010). Items q1 and q4 are also significantly correlated, meaning that institutional investors possess skills in understanding both the internal affairs of issuing firms and the risk associated with the market. Similarly, the significant positive relationship between q7 and q8 implies that to huge investment in a portfolio of securities, institutional investors need enough flexibility in their regulations

3.4. Summary measures of institutional investors' roles

The summary measures of the potential roles of institutional investors' scale and its reliability based on the responses of market participants are shown in Table 5.

Table 5. Summary statistics along with Cronbach's alpha value of the summated scale of the eight Likert scale items

Source: Questionnaire survey 2020.

Mean	SD	Range	Skewness	Alpha
3.421	0.521	2.371 – 4.350	–0.283	0.783

It appears that institutional investors will play a significant role in adopting the book-building pricing mechanism in Nepal, as the weighted mean value exceeds the theoretical mean of 3.0. According to market participants, if regulations are allowed to be more flexible, particularly when it comes to investing in IPOs, this will give them the chance to put their knowledge and experience into practice (Bohl et al., 2006); fundamentally value firms (Ong et al., 2020); estimate price bands; and determine the fair price of IPOs (Dumrongwong, 2020) through a bidding process. As a result, book-building may be implemented. It was their belief that the involvement of institutional investors in the book-building process lured real sector and manufacturing enterprises to join the capital market (SEBON, 2007). In a similar vein, they possess superior knowledge and proprietary data about the company and the industry and are able to respond appropriately (Rock, 1986). In line with the opinions of Lakshman et al. (2013), they also believed that tiny and ignorant investors, as well as mutual funds, would greatly benefit from book-building pricing. However, as mutual funds often work for the short term and exhibit herd behavior, their views are in conflict. The values of the prospective roles of institutional investors' scale might theoretically vary from 1 to 5. Range between 2.371 and 4.350 are the scale's practical minimum and maximum values, which show that market participants' opinions about institutional investors' possible involvement, are essentially consistent. The distribution of possible institutional investor positions is almost bell-shaped, as indicated by the negative but less than one skewness score. With a Cronbach Alpha of 0.783, the scale elements that are intended to gauge institutional investors' possible contributions to the implementation of book-building pricing are appropriately specified. These data suggest that institutional investors play a crucial role in the stock market.

3.5. Connection between market participants and institutional investors' potential role

Six types of market players were compared using a one-way ANOVA to see how their actions might affect institutional investors' prospective roles: issue manager, share registrar, portfolio manager, stockbroker, mutual fund, and retail investor. The possible roles of institutional investors have a noteworthy impact because of six different groups of market participants [F(5, 119) = 7.438, p = 0.000].

Table 6. One-way ANOVA test for testing equality of mean role of institutional investors across market participants

Source: Questionnaire survey 2020.

Market participant	Mean	Std. dev.	n
Issue manager	3.619	0.607	18
Portfolio manager	3.531	0.409	20
Share registrar	2.998	0.581	20
Mutual fund	3.571	0.392	9
Stockbroker	2.863	0.316	27
Retail investor	3.655	0.411	31

Note. F-value = 7.438, df = 5, 119 and *p*-value = 0.000.

Post hoc comparisons employing the least significant difference (LSD) test showed that the mean institutional investors' potential role of issue manager (M = 3.619, SD = 0.607) was significantly different than the share registrar (M = 2.998, SD = 0.581) as well as stockbroker (M = 2.863, SD = 0.316) at 0.05 level. Similarly, the mean potential role of institutional investors such as portfolio managers (M = 3.531, SD = 0.409) was significantly different than the share registrar and stockbroker. However, the mean role of institutional investors like issue managers was not significantly different from that of portfolio managers, mutual funds, and retail investors. Taken together, these results suggest that market players/participants do have an effect on institutional investors' potential role, and hence, they are associated.

4. DISCUSSION

The majority of the market participants (66.0 percent) viewed institutional investors as the main players in discovering prices under the building method. This result is in line with Rock's (1986) view, in which he documented that due to superior private information about the issuing firms, institutional investors played an effective role in determining the price of IPOs in the market. However, the presence of institutional investors in the market currently is inadequate, though their presence in the capital market is crucial.

A large number of market participants (93.66 percent) believed that institutional investors played a crucial role in the growth of the capital market. This result is aligned with Bohl et al. (2006), who claimed that as they are institutional investors, they have a significant influence on the securities markets' long-term growth. Furthermore, according to Benveniste and Spindt (1989), institutional investors must openly participate in roadshows with their "indications of interest" at prices within the underwriter's anticipated price range and demand the size of IPOs. This makes them essential to the successful implementation of the book-building method.

'Institutional investors need enough flexibility in their regulations relating to an investment in IPOs under book building', accounts for the highest mean score of 4.061, which indicates that to implement free pricing like book building, it is imperative to bring extensive changes in existing policy with greater flexibility that help institutional investors like mutual funds, pension funds, CIT, EPF, BFIs, insurance companies, etc. to function smoothly in the market. Similarly, 'institutional investors are proficient in the fundamental valuation of firms that guide them to estimate price band' accounts for a mean score of 3.668. It means market participants believed that institutional investors rightly calculate the true and fair value of the firm. Consequently, the information provided in their indications of interest during roadshows helps underwriters to estimate price band or range as reasonably as possible (Ong et al., 2020). Likewise, market participants believed that institutional investors are expected to have abundant knowledge to comprehend the risk of the markets and act accordingly, which is in line with the findings of Sharma et al. (2024), who argued that institutional investors also play the monitoring role of firms.

Testing the mean role of institutional investors across market participants suggests that active market participants such as issue managers, stockbrokers, portfolio managers, and share registrars strongly believe that institutional investors' potential roles are the key to the efficacious execution of book building.

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CONCLUSIONS

The paper aims to assess the roles and importance of institutional investors in implementing book-building pricing. The results show that the role of institutional investors is vital in the development of the capital market. The presence of institutional investors in the capital market requires adequate flexibility in regulations and participation in book-building activities followed by their presence in the market, which is also beneficial to retail investors because of their expertise in their field. The result also reveals that the market participants, such as issue managers, portfolio managers, share registrars, and stock brokers, have a high level of belief that the role of institutional investors is crucial in implementing book-building pricing mechanisms.

In this regard, the study concludes that the role of institutional investors is expected vital to implement book building, in which they need conducive regulations to function in the market. The existing regulations need to be amended, and formulate necessary bylaws that help make the book building pricing more effective to operate. The study also concludes that the presence of institutional investors rightly calculates the true and fair value of the firm and can estimate the reasonable price band of IPOs. They also monitor the operating performance of firms. It obviously helps build the confidence of retail investors in the market. Finally, it concludes that the key market participants agreed upon the importance of institutional investors' presence in the market, thereby implementing book building in the primary market.

There are some limitations of the paper. This study aims to explore only the current status and the potential roles of institutional investors in Nepal. Regarding data, only experts in the capital market have been employed as respondents, and hence, the views of general investors are ignored. The reliability of the results is based on the accuracy of the opinions/views provided by the respondents or market participants. Data have been analyzed using descriptive statistics only to find the current status and potential roles of institutional investors because this kind of thorough study about institutional investors' roles is new in the context of Nepal. The researchers are not sure that the use of complex analytical tools may or may not be applicable in the new context. Another limitation is that the study did not incorporate the new provisions of amended regulations and newly enacted book-building directives because it came into effect towards the end of 2020.

AUTHOR CONTRIBUTIONS

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