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Surf's up
Deloitte 2015 IPO report

March 2015

In collaboration with

MERGERMARKET

Contents

Methodology
All dollar figures unless otherwise stated are in Australian dollars.

Data has been compiled from IPO data within the Mergermarket intelligence database and additional sources noted within this report. Information not featured in the MM data has been corroborated with data from the respective stock exchanges mentioned within the text.

Non-equity instrument listings such as debt, ETF, and sub-notes have been excluded from Mergermarket data.

ASX hits its straps

With $26bn in equity listed through 74 floats, 2014 was truly a banner year for Australian IPOs, as business owners and financial sponsors saw record value realised from taking their companies public. In value terms, this exceeded raisings for the last three years combined, and including New Zealand companies that have sought dual listings in Australia, the figures are even more impressive. The ASX also hosted the year's third largest IPO globally, and the largest among Asia's exchanges in the Medibank Private listing.

While the record year saw average year-end returns on IPOs in excess of 17%, the overall performance of the market was lacklustre at best with the S&P/ASX 200 index edging up by a bare 1% over the year. There were clear challenges to navigate, including the continued fall in investment in the resources sector. As the year progressed, it became clear that Australia's economic outlook was less positive and economic growth in New Zealand, the United States and the United Kingdom started outpacing growth in Australia.

Notwithstanding this, the Australian share market seems to have hit its straps in 2015 with the ASX 200 index up over 10% at the time of publishing this report (March 2015). Interestingly, commodity prices, a large part of the reason for the market's underperformance in 2014, have not improved. And the outlook for China remains one of slowing growth with associated credit risks. So what's the deal?

Cheap money needs to go somewhere. And money has never been cheaper in Australia. After keeping interest rates on hold since August 2013, the cash rate cut in February to 2.25% has stirred equity markets. Beyond that, the prospect of a further rate cut in the near future is no doubt adding to the current buoyancy in share prices. This is bad news for those looking for a stable, risk-free income (think retirees). But it is good news for policy makers trying to inject life into a limping domestic economy.

A solid 2015 reporting season but hardly the stuff of share market rallies

The latest interim reporting season suggests that domestic earnings are not shooting the lights out – initial findings indicate around 56% of companies have performed in line with profit expectations, 25% have failed to meet them and 19% have exceeded them – a solid result but hardly the stuff of share market rallies. Goldman Sachs analysis also recently concluded that 25% of firms have missed dividend expectations compared with 14% at the end of FY14[1].

Valuations are still well shy of the highs

That balance for asset prices between the negative of soft economic activity and the positive of low interest rates will continue to be a key theme through 2015. And it poses an important question: are asset prices sustainable?

At current interest rates, there are few signs that prices are exaggerated. On face value, the share market rally so far in 2015 does not appear to be getting into dangerous territory in terms of valuations, with the market's price to earnings ratio moving up, but still well shy of the levels seen earlier in 2014 before the market corrected.

Part of that improvement in the index and valuation multiples may be justified through factors such as

With $26 billion in equity listed through 74 floats, 2014 was truly a banner year

1 *"Earnings beats may lack quality but buyers still keen"*, article by David Rogers sourced from The Australian dated 24 February 2015

Strong start to 2015 as new IPOs continue to outperform the market, with a healthy pipeline of floats building for the year

lower energy prices and a lower Australian dollar boosting earnings potential. And then considering the global backdrop, in the US the S&P 500 index hit an all-time high of 2,119 on 25 February 2015 while the NASDAQ Composite breached the hallowed 5,000 mark. But it is also true that the global macroeconomic environment remains risky, with the potential of a further slowing in growth from China the key concern for Australia.

The improvement in investor sentiment over recent weeks is encouraging, and the Reserve Bank would clearly like to see the tide of money heading towards equity markets rather than the housing market. Now that just needs to translate into a stronger appetite by businesses to take on risk (which remains subdued) and expand their operations.

Is your business *ready to list?*

The early signs in respect of IPOs this year are already positive with stocks such as Appen, Phytotech Medical and Martin Aircraft performing strongly on debut. This indicates the window for new listings, particularly growth stocks in the technology sector, remains open as investors move capital into more productive equity investments. There have been seven listings in the first two months of the year returning 22.8% to the end of February 2015.

This report, in collaboration with mergers and acquisitions intelligence provider Mergermarket, looks at IPO activities over the past five years and presents an outlook of trends and events to come, as a dramatic shift sweeps the ASX.

We continue to see a healthy pipeline of IPOs building for the remainder of the year, although the success of these will ultimately be dictated by the quality of the assets.

In the end, there is more to a successful float than market timing. The more pertinent question is whether *you* are ready to list. We discuss the hygiene factors, motivation and innovation your business needs for a successful float.

Ian Turner
Head of Transaction Services, Deloitte Australia

Healthcare and financial services capital raisings

accounted for

59%

of 2014 listings

Decline in the number of energy and resources IPOs

30%

of IPOs in 2013

14%

of IPOs in 2014

Total 2014 listings:

74

initial public offerings

$26 billion

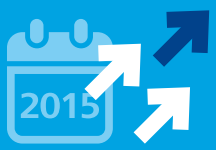
Private equity: 2014 a comeback year

17

exits valued at **$11.5bn** in 2014
($7.3bn in equity raised)

6

exits valued at **$3.2bn** in 2013
($2.1bn in equity raised)



Expectations for 2015: Strong pipeline, strong performance

While matching the overall value raised in 2014 is unlikely, a strong pipeline of issues exists and the year ahead should continue the trend of solid performance.

Questioning sustainability

A temporary boom?

Without doubt, 2014 was a stellar year for listings as market capitalisation and total listings reached new records (Figure 1 & 2). However, the end of 2014 saw the underperformance of some assets, and delays and re-pricing of others. Given these developments, market participants naturally question how long the current IPO window will remain open.

To understand appetites for IPOs in the coming months, it is informative to look at the price performance of recent IPOs, where there was ample evidence of a resurgent market (Figure 3). The average performance of IPOs with market capitalisation exceeding $75m last year was 17% on a weighted basis since listing.

Financial markets have been volatile at the start of 2015 as commodities extend their comedown and investors worry about global growth. Any major shifts in global markets or increases in volatility will impact raisings on the ASX.

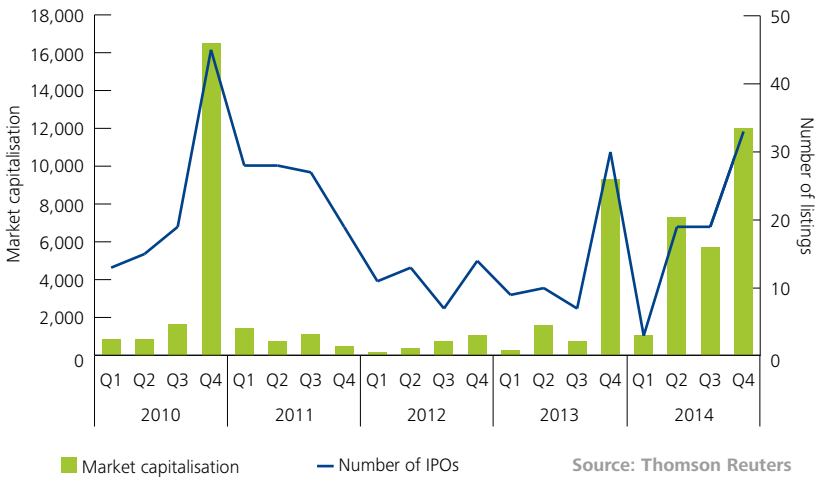
A more certain and important barometer to how long the window remains open will be the February and August reporting seasons this year, and specifically the performance of the new listings of the last two years. While the latter have been strong, the February 2015 reporting season itself has delivered relatively mixed results. Nevertheless, the ASX has gone from strength to strength, closing at a seven year high in February 2015, driven by low rates and further expected cuts. This is expected to continue to drive investor demand for new listing for the next 12 months.

From IPO to M&A

Australia's top equity capital market (ECM) bankers are tipping that 2015 will deliver more corporate mergers and acquisitions. There is sufficient anecdotal evidence including transactions where Deloitte is getting involved in an increasing number of dual track processes.

While IPO activity dominated the ECM space in 2014, other parts of the market, such as secondary raisings, rights issues and backdoor listings to finance M&A activity, are set to pick up in 2015 amid strong support for corporate deal-making.

Figure 1: ASX public listings



Note: Q4 2010 included the listings of Westfield Retail Trust ($8.4bn) and QR National ($6.2bn)

Figure 2: IPO Summary

	2010	2011	2012	2013	2014
All IPOs					
Number of IPOs	92	102	45	56	74
Market capitalisation ($bn)	19.9	3.8	2.3	11.9	26.0
Market capitalisation exceeding $75m					
Number of IPOs	17	9	4	27	42
Market capitalisation ($bn)	18.1	2.3	1.6	10.9	24.9
Equity raised ($bn)	n/a	0.6	0.7	5.9	16.7
Average size (market cap $m)	1,063	254	404	405	594
Average performance on debut (weighted)	n/a	0.1%	(0.2%)	3.3%	5.2%

Source: Thomson Reuters

The average performance of IPOs with market capitalisation exceeding $75m last year was approximately 17% to the end of the year

Figure 3: Top 20 IPOs >$75m in 2014, by performance

Corporate Profile							Stock Price Movement	
Company name	Listing date	Industry	Issue price ($)	Market capitalisation ($m)	Capital raised ($m)	Private equity owner (if applicable)	Day 1 closing price	31-Dec-14 closing price
Beacon Lighting	15-Apr-14	Retail	0.66	141.9	63.9		61%	127%
IPH Ltd	19-Nov-14	Commercial services	2.10	330.9	165.9		48%	67%
Bellamy's Australia	5-Aug-14	Retail	1.00	95.0	35.9		30%	65%
Mantra Group	20-Jun-14	Consumer services	1.80	449.0	239.1	CVC Capital Partners	(1%)	61%
Victor Group Holdings	9-May-14	TMT	0.20	103.9	4.0		10%	40%
Pacific Smiles Group	21-Nov-14	Healthcare	1.30	197.6	42.1	TDM Asset Management	37%	39%
Burson Group	24-Apr-14	Retail	1.82	297.7	143.8	Quadrant	13%	37%
Genworth Mortgage Insurance Australia	20-May-14	Financial services	2.65	1,722.5	591.5		13%	37%
Isentia Group	5-Jun-14	TMT	2.04	408.0	238.5	Quadrant	19%	36%
Healthscope	28-Jul-14	Financial services	2.10	3,637.4	2,410.2	TPG, Carlyle Group	5%	30%
Urbanise.com	22-Sep-14	TMT	0.70	108.5	20.0		-	27%
Medibank Private	25-Nov-14	Healthcare	2.00	5,679.0	5,679.0		7%	21%
Spotless Group	23-May-14	Commercial services	1.60	1,757.3	1,072.0	Pacific Equity Partners	7%	19%
Lovisa Holdings	18-Dec-14	Retail	2.00	210.0	102.0		7%	17%
Elanor Investors Group	11-Jul-14	Financial services	1.25	76.0	60.8		2%	16%
Ellerston Global Investments	20-Oct-14	Financial services	1.00	75.0	55.0		1%	14%
SG Fleet	4-Mar-14	Commercial services	1.85	449.0	188.6	Champ Ventures	(13%)	14%
Regis Healthcare	7-Oct-14	Healthcare	3.65	1,096.3	409.9		10%	11%
Godfreys Group	10-Dec-14	Retail	2.75	110.8	77.7	Investec & Nomura	4%	6%
Centuria Metropolitan REIT	10-Dec-14	Property	2.00	143.0	114.3		5%	5%

Source: Thomson Reuters

Are you ready to list?

Is your business *ready* to list?

Australia's IPO boom is set to continue in 2015, fuelled by low interest rates, strength in global equity markets, a willing queue of business owners keen to monetise their investments or pursue further expansion via listing and a build-up of demand from institutions and superannuation funds. Even if the overall value of companies listed on the ASX does not top the $26bn reached in 2014, a figure amplified by the enormous impact of Medibank Private, market momentum is likely to see more business owners asking: *is it time to list?*

Deloitte's view is that there is more to a successful float than market timing. There is a critical question owners should ask themselves: is their business *ready* to list?

Considering that even in the highly successful year of 2014, more than one in three IPOs suffered a reduction in share price between opening and the end of the year. As even more businesses eye the window for listings, some will be lured to sell prematurely, but wary buyers will be sceptical.

The IPO process requires a firm commitment from management in terms of time and resource allocation, and anything but the most rigorous effort is likely to yield less than desired results. Governance and financial reporting frameworks will need to be established and perfected to withstand the test of operating in a listed environment.

So, what's the checklist for whether your business is ready to list? There are three simple indicators:

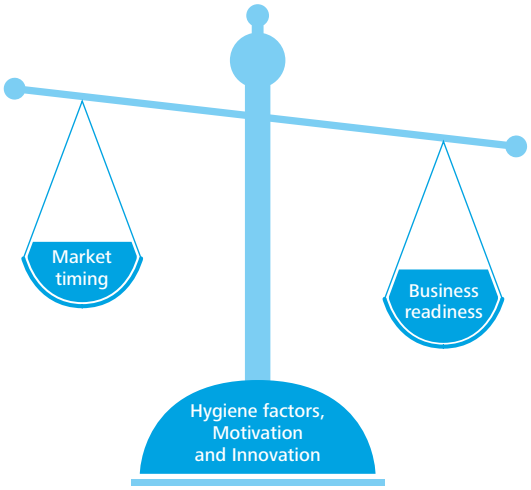
- **Hygiene factors:** Are governance and financial reporting frameworks established and perfected to withstand the test of a listed operating environment?
- **Motivation:** Why do you want to sell and are you rushing it?
- **Innovation:** Can your business demonstrate to the market it's got a strategy for growth through innovation, not just relying on the economy? How sophisticated is your business's strategy for expansion into Asia and use of digital technologies?

Private companies accustomed to producing accounts three months following the close of the year will be required to adapt to more demanding disclosure and reporting requirements to meet the high standards of the public market. Equally, expectations are high concerning the quality of financial information placed in the prospectus in the initial phases of the IPO process.

Our evidence shows that companies do better when listing in a rough market when they are ready than listing in a strong market when they are not ready.

In a relatively weak market, well-placed businesses can have successful IPOs. In 2011, where the index fell nearly 15%, the IPOs in excess of $75m delivered positive returns on debut. Conversely, 2014 saw IPOs delivering returns in excess of 17%; however, a number of IPOs did not perform, with the bottom 10 listings declining on average by 11% by the end of the year.

Our evidence shows that companies do better when listing in a rough market when they are ready, than listing in a strong market when they are not ready



The changing nature of Australian IPOs

The ASX matures

More than monetary figures and robust growth, the number and quality of public listings on the ASX show the potential in the Australian IPO market. The ASX has shed its image as a venue primarily for mining and resource company listings, and now supports a wide range of industries, has a thriving mid-market, and regularly attracts listings from overseas.

Perhaps more importantly, the IPO market in Australia is increasingly a key component in the country's strategic corporate finance landscape – giving sophisticated institutional investors opportunities to participate in the rebalancing of the economy, while allowing the companies themselves to optimise their capital structures and create shareholder value.

More Asian issuers

The depth and liquidity of the Australian market, combined with the strong governance principles, makes it an attractive listing destination for international companies. In particular, the fast-growing economic ties between Australian and Asia-Pacific markets has resulted in the ASX now attracting a number of companies from across the region to list. For example, SpeedCast listed on the ASX in August 2014, a company headquartered in Hong Kong and with a strong and broad Asia Pacific revenue base. The decision to list on the ASX was due to Australia's wealth of mid-cap fund managers who have afforded it a market cap of around $250m.

Going forward, there is likely to be an increasing number of Asian businesses, particularly those from China and South East Asia, considering listing on the ASX. These companies will likely be looking to establish footholds in Australia. In addition to the benefits of liquidity and a strong investor base, this can help the business itself in establishing local credibility and market entry.

Stacking up against Asia's exchanges

The ASX compares well to other exchanges in terms of the costs and processes involved in a public listing. Many overseas markets, like Hong Kong, may offer better listing opportunities, but come with substantial additional costs and administrative burdens. Some of the onerous listing rules that restrict the ability of companies without a record of profitability to list have acted as a deterrent to them listing in Asian markets over the last year. These features make the ASX an attractive destination for regional technology firms, as well as a venue for dual listings.

Figure 4: Comparing exchanges: Tale of the tape in 2014

ASX (Australia)

Number of listings	74
Equity raised	AU$17.5bn (US$14.2bn)
Market capitalisation	AU$26.0bn (US$21.1bn)

SGX (Singapore)

Number of listings	27
Equity raised	SG$3.2bn (US$2.4bn)

HKEx (Hong Kong)

Number of listings	108
Equity raised	HK$225.0bn (US$29.0bn)

Data sourced from Thomson Reuters, Mergermarket, media reports

Note 1: Excludes listings on the HK GEM Board
Note 2: USD equivalents are based on average FX rates for the 2014 year

Likewise, Singapore offers limited IPO opportunities, with only 27 public offerings raising SG$3.2bn in 2014, none of which were private equity backed (Figure 4). The SGX is traditionally a yield centric market and tends to not be the best avenue for companies looking for high growth, creating potential for the ASX to become a regional tech hub.

The ASX is also looking to ramp up its attractiveness as a listing destination, particularly following dual listings from New Zealand. Not included in the statistics discussed in this report were an additional seven IPOs of significant New Zealand companies which sought dual listings on the ASX in 2014. Exceeding a combined market capitalisation of $3.3bn and capital raised of $1.3bn, these were Genesis Energy, Intueri Education, Gentrack, Vista Group, Metro Performance Glass, Orion Health and Evolve Education. By comparison, in 2013 there were three New Zealand listings on the ASX, namely Mighty River, Z Energy, and Meridian Energy.

Privatisations tipped to generate listings

Increased government privatisations are set to generate further IPO activity in 2015. Following the success of the Medibank Private IPO – a deal that was many years in the making, following the passage of the Medibank Private Sale Act of 2006 – the Federal Government has said it is very pleased with the outcome of the sale and is considering other floats.

The Federal Government announced in 2014 that it would commission scoping studies for four asset sales recommended by the National Commission of Audit, with the proceeds to go into a new asset recycling fund to invest in infrastructure. The government did not give a time frame for the studies or the potential sell-offs, comprising: Australian Hearing; Defence Housing Australia; the Royal Australian Mint; and the registry service of corporate regulator, Australian Securities and Investments Commission.

Listing potential and looking forward to 2015

Expectations are also that international companies will list their domestic Australian subsidiaries on the ASX in 2015. One such deal, the IPO of Genworth Australia, occurred in May 2014 and has been generally well received by the market. IPOs such as this allow international companies to capture the value present in their local subsidiaries. The IPOs also afford the subsidiaries greater financial flexibility and improved access to capital markets, both of which contribute to their growth.

In 2015, it may be difficult for the market to match the overall value that was raised in 2014. However, by other metrics, the market should continue to perform well. The pipeline of issuers looking to list is strong. There is a diversified sectoral array for investors to choose from and the domestic institutional and retail investor base looks to have a healthy appetite to continue to invest in quality assets, given the market performance in 2014.

Poor performing IPOs

While there has been significant IPO activity, as well as overall strong share price performance as indicated by the 11.3% average gain delivered by 2013 and 2014 IPOs (greater than $75m market capitalisation), the recent IPO activity has not been without some poor performers. There have been 13 IPOs experiencing share price declines in excess of 10% to the end of 2014 (seven in 2013 and six in 2014). The five worst performers – Malabar Coal, Vocation, McAleese, Ensogo (iBuy) and Sunbridge Group, all listed in 2013. Furthermore, of the 69 IPOs in 2013 and 2014 (greater than $75m market capitalisation), 24 experienced share price declines on the day 1 closing.

Innovations in IPOs

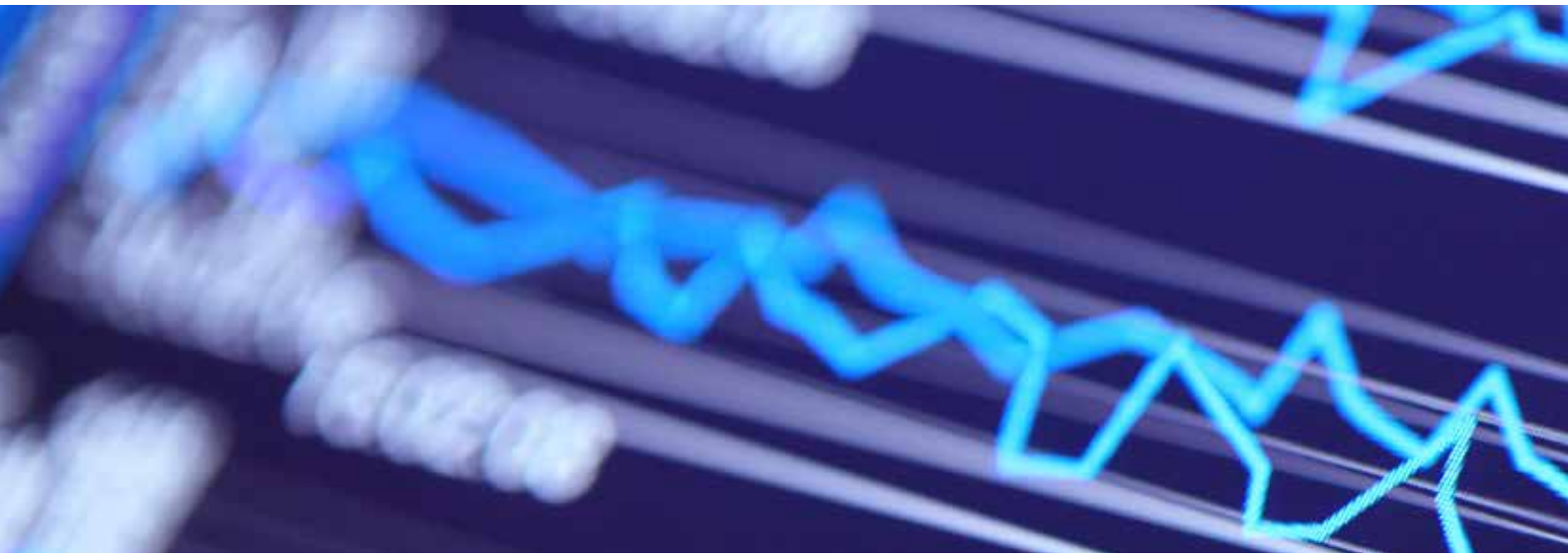
One of the key innovations of the year came from the Medibank Private IPO. As with any large privatisation, the government seller had a number of competing considerations that would affect the process. It wanted to achieve a full price, but not so much that the shares would underperform in the aftermarket. It also wanted to attract a strong core group of institutional investors into the book, but not so much that retail investors were excluded.

The solution to meeting these requirements was an innovative, 24-hour preferential allocation policy. Taking this approach allowed institutional investors to make early, firm bids to secure their participation. The book was then opened to retail investors at a lower price, thus allowing the deal to secure price tension. As a result, there was a 60% retail participation rate.

Healthscope's public listing also brought a level of innovation to the market during the book build phase. The IPO was part of a dual-track process and took the unusual step of underwriting the IPO with cornerstone investors priced at the top end of the range rather than with the bankers themselves. The cornerstone investors contributed $1.7bn of the $2.4bn equity raised, a significant investment which had not been seen in the Australian market before. This gave the deal stability going into the book build, which reportedly resulted in 110 institutions participating in the IPO. Of these, more than two-thirds were offshore investors.

Similar preferential allocation policies are utilised on a more informal basis in the market, where the retail offer is scaled off an early indication to provide momentum to the book.

Complexities of structuring an IPO



There are complex commercial and legal requirements involved in an IPO and the complexities are rapidly increasing. This is occurring through innovations in the way IPOs are structured, the rising number of private equity-backed IPOs (including partial IPOs which allow the private equity shareholders to participate in the future growth of their companies), dual listings or listings of businesses headquartered overseas, exit and escrow arrangements, and the pressure to perform in a competitive IPO environment. Understanding the tax issues associated with an IPO is similarly not without its complexities.

Depending on the tax profile of the corporate group and commercial objectives, millions of dollars in cash tax savings and value can be added through proper analysis of opportunities and risks. For example, the global effective tax rates applied to forecasts, recognition of tax structuring benefits or tax attributes over the forecast period, dividend and franking forecasts and the treatment of one-off costs associated with the IPO can impact a prospectus.

Where such benefits can be identified in the prospectus and showcased to potential investors, it can impact the value proposition for the listed group, shareholders (both exiting and continuing), and public and institutional investors.

In Australia, a new company is often incorporated to act as the listing vehicle. In this case, the exiting shareholders dispose of their shares to the new company, rather than directly to the public. There are generally important legal and commercial reasons for using such a structure, including:

- Managing prospectus liability for the shareholders (which is often a primary driver)
- Avoiding the need to convert the existing company to a public company (which can take time) and allowing the required directors and officeholders to be in place
- Providing a new clean company to be the listing vehicle and structurally separating existing operations
- Potentially allowing for a simpler settlement process.

The new company structure can take many forms, including:

- 'FloatCo' (or 'TopHat') whereby FloatCo issues shares to the public and applies proceeds to acquire all shares in the company (with any continuing shareholders rolling over their shares to FloatCo);
- 'SaleCo' (or 'SideCar') whereby SaleCo acts as a conduit entity to acquire shares in the company from exiting shareholders and disposes of those shares directly to the public, with continuing shareholders retaining their existing shares in the company;
- 'ListCo' which can involve the interposition of a new listing vehicle above the company prior to the IPO; and
- In some cases a combination.

Pros and cons of a FloatCo structure

While all IPO structures have their pros and cons from a commercial and legal perspective, the use of a FloatCo structure in particular gives rise to a number of specific tax considerations, including:

Availability of tax rollover to defer gains for continuing shareholders (particularly important to consider for private equity and cornerstone investors)

Potential resetting of the tax value of underlying assets of the listed group to market value

Uncertainty relating to the proposed changes to the tax treatment of 'deductible liabilities' held at the date of the IPO

Availability of tax attributes such as tax losses going forward, particularly for the forecast period

Ability to incorporate a financing company to manage future dividend traps

Stamp duty depending on the tax profile of the company

Regardless of the chosen structure, whether there are benefits in paying a pre-IPO dividend requires consideration and can impact value.

In addition to sound tax planning, companies should also understand the accounting implications of a new company structure given ASIC's recent focus in this area, in particular with fair value disclosures.

While the commercial drivers of an IPO are obviously paramount, the tax and accounting opportunities and risks cannot be ignored given the impact on the value proposition of an IPO.

Fair value disclosures

We note that in a majority of capital raisings, the transactions contemplated under the Offer are evaluated in accordance with AASB 3 Business Combinations to determine whether or not a business combination has occurred. Often in such transactions no acquisition of a business has occurred and consequently the transaction is accounted for as a form of capital reconstruction and group reorganisation. Accordingly the financial statements of the new IPO company are seen as a continuation of the existing company pre-listing, and the assets and liabilities are recognised and measured at the carrying amounts rather than at fair value.

However the accounting for these transactions is very transaction specific and some may be accounted for as business combinations. An IASB project on accounting for common control transactions is likely to address such restructures in the future. The outcome of these deliberations, and the timing of any decisions and whether any potential changes are retrospective or only prospective could mean that the financial reporting outcome may be different to that reported in the Prospectus.

Because of the alternative views as to the appropriate accounting for these types of transactions, as an interim measure current practice is for most Prospectuses to include by way of fair value disclosures:

- The Directors' estimate of the excess of the fair value compared to the book value of net assets, if a purchase price allocation were required to be undertaken in the future. The disclosures should note what assets the increase would be allocated to with any residual to goodwill. Investigating Accountants would typically require recent valuations to support these disclosures.
- A statement that to the extent any of the excess was allocated to finite life intangible assets (trademarks, brand names and software), profits would be impacted by the annual amortisation of these intangible assets.

The shift from mining

The ASX has undergone a transformation over the past two years from a market dominated by resources companies to one where a diverse range of companies are going public (Figure 5 & 6). While the ASX remains one of the world's leading exchanges for resources companies to list, the macroeconomic environment and the end of the commodity super-cycle has damaged the outlook for many potential new listings in this sector. Furthermore, Australia's institutional investment market now demands investments from a wider range of sectors.

Energy and resources fades…

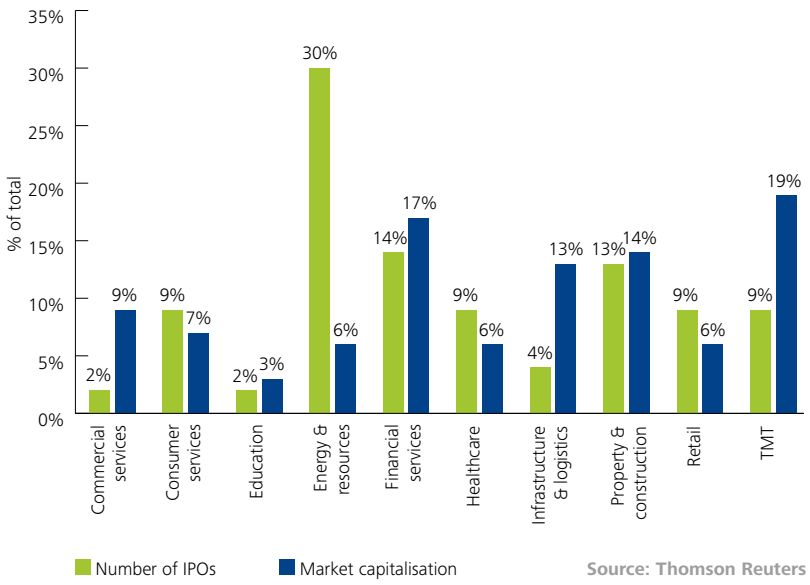
It has been clear for a number of years that the Australian market would need to diversify away from the resources sector, as the fall in commodity prices affected the ability of numerous mining companies to remain viable. This was especially true for those in the high-risk exploration categories, a trend that accelerated in 2014, as commodity prices began to slump. That decline has continued, with the iron ore price nearing a 5.5 year low and in danger of a move below US$60. Likewise, the price of coal has fallen 26%, while the price of oil collapsed in the second half of last year.

Data for 2014 shows just how complete the decline of the energy and resources sector has been. In total, the sector accounted for just 3% of market capitalisation and 14% of IPO volumes, with an average listing size of $97m. By contrast, in 2013 almost one-third of IPO volumes came from energy and resources companies.

Looking at performance, in the five years to 2014, the energy and resources sector had difficulty retaining initial share prices. Average Day 1 closes for the period were down 10.1%, with share price performance for the sector as of 31 December 2014 closing at -83.3% (Figure 7).

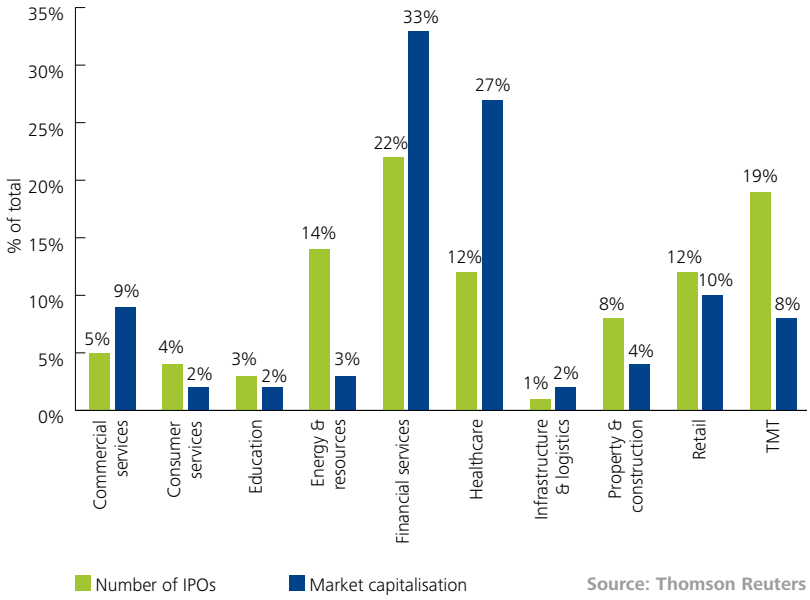
The scale of the problem for the Australian market was neatly laid out at the beginning of 2014 by the IMF. In its *Article IV Annual Assessment of the Australian Economy*, it noted that: "A shift to broader-based growth would be helped by making the most of opportunities offered by a growing Asian middle class, which could support demand for Australia's services exports—in particular health, education, tourism, and professional services."

Figure 5: ASX IPO figures (all IPOs in 2013)



Source: Thomson Reuters

Figure 6: ASX IPO figures (all IPOs in 2014)



Source: Thomson Reuters

…while financial services and healthcare begin to shine

The most surprising aspect is the speed with which companies from other sectors have come in to fill the gap left by resources companies. Financial services in particular stands out for its large share of the IPO value pie. With 17 listings, market capitalisation totalled $8.5bn in 2014. As of 31 December 2014, the average share price for the sector had improved 16.4%.

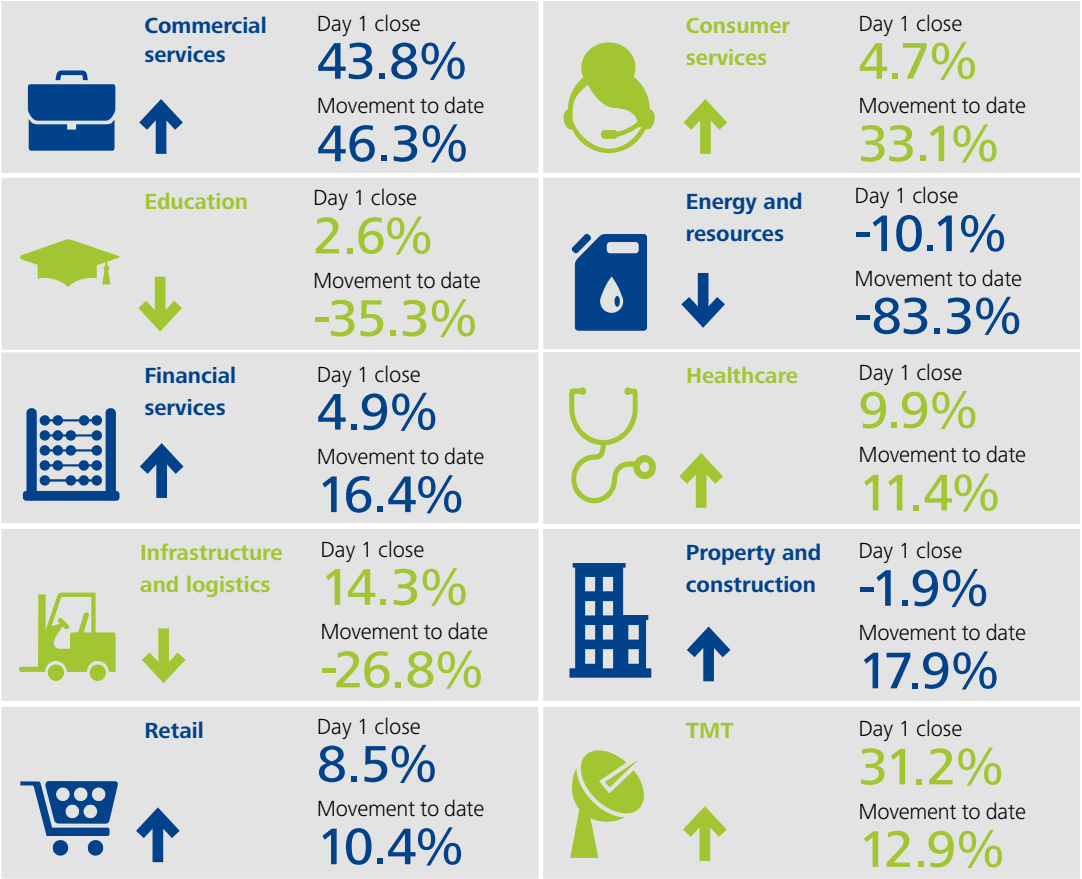
However, the real story of the year can be found in the healthcare sector, which accounted for 27% of equity raised for 2014. Performance in the sector has been equally impressive: average Day 1 closes were up 9.9% with year-end shares up 11.4%. Australia's aging population, a segment with increasing healthcare and aged services demands, has driven heated investor interest, and market participants expect this trend to continue in the year ahead.

Small tech with big potential

With technology, media, and telecommunications (TMT) sector equity raisings maintaining momentum – raising $1.7bn in 2013 and 2014, and with average share prices for 2011 through 2014 up at 12.9% – a new wave of listings among smaller Australian tech companies is expected in 2015. This is being bolstered by increasing investor interest in high-growth businesses with global potential. The preparedness of the stock market to embrace young and sometimes less proven tech businesses gives a viable alternative to private businesses seeking venture funding, according to a Mergermarket intelligence brief citing the managing director of a Melbourne-based company that raises capital for technology and services businesses.

Listings of small tech firms in 2014 included digital applications group Rewardle. The company was a standout deal given that Rewardle is a young tech business with little

Figure 7: Sector performance



Note: Based on Day 1 closing price and the closing share price at 31 December 2014

Source: Thomson Reuters

revenue that was able to raise $4.0m. Currently, interest is brewing in tech stocks and other emerging sectors with export potential, especially those outside the mining sector that offer investors a substantial return rate.

IPOs with export exposure

With a depreciating Australian dollar, IPOs with export exposure are going to be in greater demand as investors seek profitable businesses in high growth sectors. Interest is also growing among investor groups that want to fund tech companies that export or plan on doing so in the near future.

Companies with material offshore earnings will generally become more attractive to investors as the Australian dollar weakens, said the managing director at an investment bank in a Mergermarket intelligence brief. However, the banker cautioned that with currency exposure being one of many investment case considerations, and the Australian dollar being particularly volatile, these companies will require a deeper and more holistic case-by-case evaluation.

Interest rates anticipated to remain low

During times of low interest rates, IPO activity has historically increased, as has been evidenced by the number of IPOs in 2013 and 2014 during times of historically low interest rates. The Reserve Bank of Australia lowered the cash rate by 25bps in February 2015, with indications of a further 25bps rate cut sometime in 2015 which should encourage IPO activity.

Reverse listings

Another trend to emerge in 2014 was the reverse listing of technology companies via acquisitions by listed resources companies. According to ASX figures, there were 30 reverse listings in 2014, half of which were tech firms buying resource businesses.

The process allows unlisted companies to gain access to public exchanges by being purchased by the listed company. This brings a similar outcome to an IPO process, but via a different route. These deals – such as InterMet Resources Ltd's acquisition of One-Page in October 2014, and AO Energy Ltd's acquisition of Reproductive Health Science in April 2014 – show that many companies value having the prestige and liquidity of a public listing. It also shows how investors who once were happy to be invested in the resources sector are now seeking exposure to other sectors.

Long term or cyclical?

It is important to note that the relative decline in the resources sector's participation in the Australian IPO market is likely to be a cyclical rather than structural change. Even though the so-called commodities 'supercycle' began to turn in 2009, there have been 270 junior floats (<$75m market capitalisation) on the ASX. Australia still has the third largest pool of institutional capital in the world, and on the ASX, metals and mining companies are the biggest component on a value and volume basis.

When the fundamentals of the sector start showing signs of improvement, appetite for new listings may resume. However, 2014 has demonstrated that the Australian IPO market is now more diverse than in previous years and that it is no longer dependent on the resources sector.

Private equity

Private equity was back in mid-2013, after an almost four-year hiatus from taking portfolio companies public on the ASX (Figure 8). PE-backed IPOs accounted for 46% of public listing value and 40% of volume for the year following several years of little exit activity.

The period 2010 to 2012 saw a limited number of PE-backed public listings come to market as private equity firms avoided exits until higher valuations could be realised. In 2013, notable exits via IPO began to emerge – six exits worth a total of $3.2bn market capitalisation, which included Australia's largest assisted reproductive services provider Virtus Health, consumer electronics retailer Dick Smith, and online foreign exchange and payments company OzForex – however, it was not until 2014 that new records were achieved. The lack of deals in previous years had created a backlog and, under favourable market conditions, this was finally released in 2014.

Exits over the past year have been swift. The 17 PE-backed exits in 2014 have delivered combined market capitalisation exceeding $11.5bn. Exits were spread across sectors, although the healthcare sector stood out for its total equity raised (Figures 9 & 10).

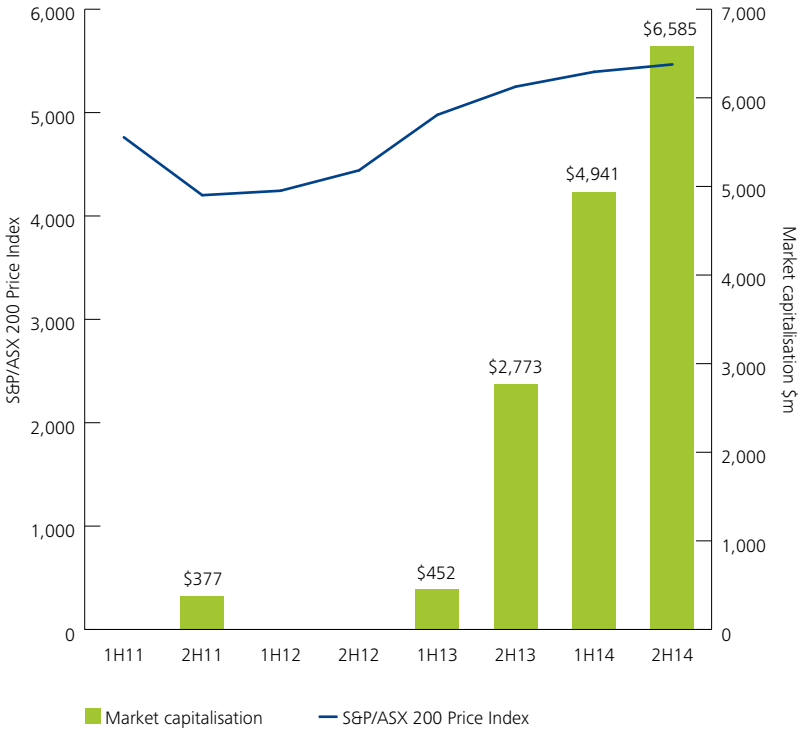
The analysis in this section reflects all PE exits valuing the companies in excess of $75 million (market capitalisation) at listing. Consistent with the remainder of the report, dual-listed New Zealand companies, notably Metro Performance Glass floated by Crescent Capital Partners in July 2014, and Orion Health Group in November 2014 have been excluded. Note also that the $670m listing of Nine Entertainment by US hedge funds Apollo Global Management and Oaktree Capital Group valuing the equity at $1.9bn has been excluded.

Quarterly trends, standout sectors

The first quarter of 2014 had a single listing, with Champ Ventures testing the waters with a $188.6m exit of its vehicle-leasing company SG Fleet, valuing the company at $450m.

Both deal volumes and values spiked in Q2 2014 when $2.8bn was raised via seven PE-backed IPOs with a market capitalisation of $4.5bn. At the time, Australia's benchmark index S&P/ASX 200 was trading close to its highest level in five years, a surge in conditions that drove the flurry of deal activity.

Figure 8: PE-backed IPOs (exceeding $75m market capitalisation at listing)



Source: ASX, Thomson Reuters

Private equity exits soared in 2014, with 17 significant exits raising $7.3bn on the ASX, valuing the companies at $11.5bn

A significant portion of the $2.8bn was on account of Pacific Equity Partners, which floated a 51% stake in cleaning and catering contractor Spotless Group for a $1,072.0m raising, and its stake in hygiene and personal care product manufacturer Asaleo Care for a $661.5m raising. The Spotless IPO followed a year-long turnaround of the company after it was taken private in mid-2012. The listing also helped boost deal totals in the business services sector.

Figure 9: Private equity exits by sector (>$75m), number of IPOs (2013-2014)

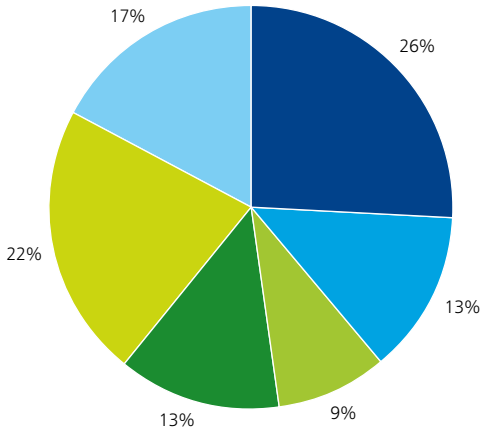
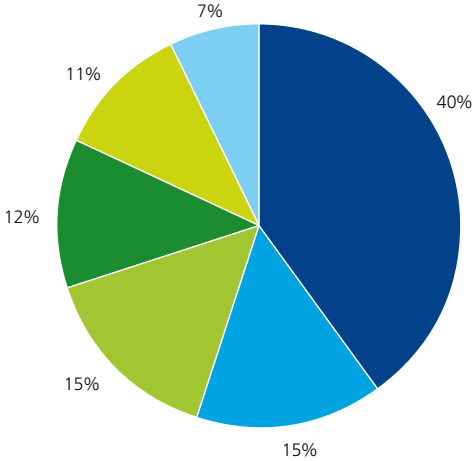


Figure 10: Private equity exits by sector (>$75m), value of IPOs (2013-2014)



Healthcare
TMT
Consumer products & services
Commercial services
Financial services
Retail

Source: Thomson Reuters

Q3 2014 saw equally impressive IPO values, with private equity firms raising $2.8bn in three listings, valuing the companies at $4.2bn. The quarter was dominated by the $2.4bn listing of Healthscope by the Carlyle Group and TPG Capital, which accounted for approximately a third of PE equity raisings for the year.

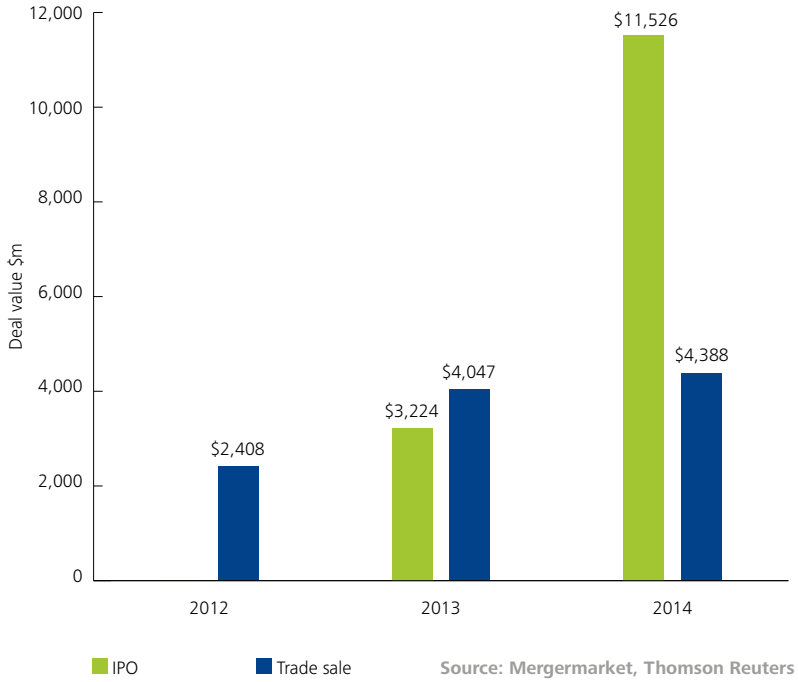
Trade sale loses shine

Valuations have factored significantly into the decision-making process among fund managers to exit investments via listings or trade sales (Figure 11). Indeed, the valuations on offer and overall performance of the ASX provided the required motivation for private equity firms to follow the IPO path as opposed to selling to corporate acquirers.

Healthscope provides an excellent example of a listing trumping a trade sale. Going into 2014, private equity owners Carlyle Group and TPG were yet to commit to an exit strategy, with consideration given to both an IPO and a corporate sale. As market activity began to heat up in the first quarter of the year, attention turned to a public market exit. The listing in July allowed the private equity firms to achieve a valuation of 22 times forward earnings – in all likelihood, a much higher valuation than a trade sale would have offered. And the results showed, with Healthscope's shares up 30% by the end of the year.

PE-backed listings accounted for 46% of public listing values for 2014, and delivered returns averaging 15% by the close of the year

Figure 11: Private equity exits: IPO vs. trade sale (>$75m market capitalisation)



Market data reinforces the attractiveness of the IPO market. In 2012, there were nine trade sales of PE-backed Australian companies with a combined value of $2.4bn. While IPOs staged a comeback in 2013, reaching approximately $3.2bn, values still fell short of sales to corporate acquirers. In 2014, PE-backed IPO values overtook trade sales, with 17 deals worth $11.5bn (raising $7.3bn in equity) against 16 trade sale deals with a value of $4.4bn.

Retaining a stake

In a number of cases, PE backers have retained shares in the companies they are taking public. These can be critical from a marketing perspective to demonstrate confidence in the IPO as owners are not simply offloading assets that have peaked in terms of attractiveness. By remaining involved with the company, this can help align the interests of the new shareholders with the PE sellers – both want to see the newly-listed shares perform strongly.

The June 2014 listing of media intelligence company iSentia by Quadrant Private Equity illustrated this trend. As part of the IPO, Quadrant retained 25% of the company's shares.

While still in the pipeline, Ironbridge Capital has also announced intentions to retain equity in its portfolio company, Fleet Partners. In filings with the ASX, Ironbridge has said that it will sell between 50% and 80% of the vehicle fleet management company, retaining a significant stake post listing. This will allow it to benefit from the potential consolidation of the fleet vehicle market that the listing will encourage.

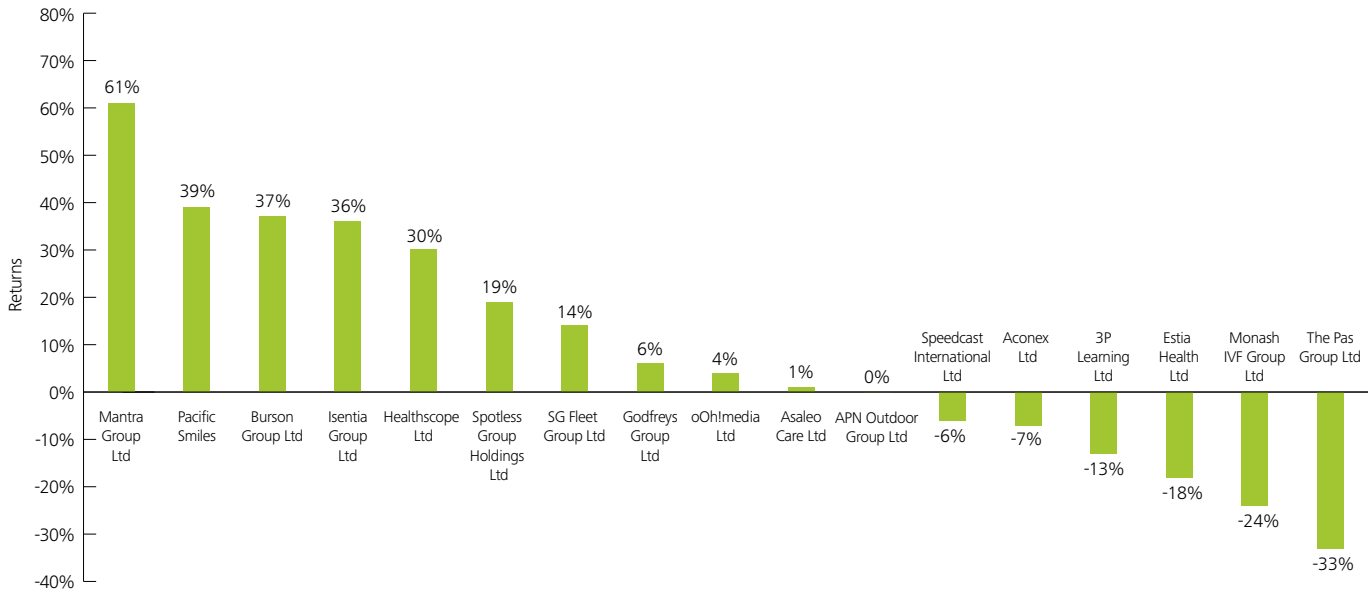
Australia's IPO market has caught up with global trends in other developed markets such as the US, UK and Canada where private equity firms have much more "skin in the game" after the listing.

Not surprisingly then, the 17 listings in 2014 delivered average returns of nearly 15% by the end of the year – these were influenced by above average returns for the highly successful Healthscope listing. Excluding this as an outlier, PE floats delivered returns averaging c.8% by the close of the year, a strong result in light of the overall ASX performance for the year.

Private equity outlook

Looking ahead in 2015, it is likely the current trend for PE-backed IPOs will continue. In the early weeks

Figure 12: Performance of 2014 PE-backed IPOs to 31 December 2014



Source: Thomson Reuters

of Q1 2015, a number of PE-backed companies announced plans to list. Among these is accounting software firm MYOB. If brought to market for an anticipated $3.0bn, the MYOB listing would be an almost doubling of the US-based private equity firm, Bain Capital's investment, following the company's sale by Australian private equity firm Archer Capital in 2011.

PE firms that were prominent in the IPO market in 2014 look set to continue their activities in 2015. Positive performance records in the past year may also encourage other PE firms to exit (Figure 12).

Mergermarket also recently highlighted a number of PE-owned companies in the consumer sector that are ripe for an exit based on the life of the fund / stage of investment, including CHAMP Ventures' holding in women's fitness apparel retailer Lorna Jane, Catalyst's potential listing of Adairs Retail Group and Quadrant's investment in Independent Pub Group. Together with announced deals, such as Quadrant Private Equity's anticipated listing of Icon Cancer Care and Super A-Mart, these suggest that the strength of the private equity-backed IPO market will continue in 2015.

Private equity firms that were prominent in the IPO market in 2014 look set to continue their activities in 2015

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