IPO report 2018
Rising tide
March 2018
Foreword

Rising tide

Initially expected to be one of the more muted years for equity capital markets in Australia over the last five years, 2017 may have just silenced a few critics. The local IPO market delivered more than a few surprises, with the largest number of ASX listings since the global financial crisis (GFC) and a remarkable performance overall. By the end of the calendar year, 115 companies had successfully listed, compared with 94 in 2016.

The largest listings for the year (other than listed investment vehicles such as Magellan) included Netwealth, which nearly doubled its issue price at year-end, Bingo Industries and Moelis Australia. The dominant sector by far was financial services, accounting for nearly 47% of the listed market capitalisation, and interestingly, 2017 also saw the resurgence of junior miners and energy companies with energy and resources accounting for 37 listings and 11.8% of the listed market capitalisation.

In terms of sizable deals, investor caution was often cited as being responsible for the $6.7 billion of capital raised, which was down approximately 15% on the prior year, and private equity firms were largely absentees as they embarked on their investment phase. However, the year also saw a significant rise in corporate M&A, with the first half seeing a number of assets where takeovers were priced above mooted IPOs, a trend that continued later into the year.

Fast forward to year-end, and Australian stock markets were buoyed by confidence with the ASX 200 breaking through the much awaited 6,000 points ‘psychological barrier’. Although increasing levels of volatility in the new year tempered the resurgence in optimism temporarily, the market remains buoyant with a pipeline of IPO candidates for the foreseeable future.

Emerging companies dominate the board

The year was dominated by small cap ASX listings, with approximately 75% of IPOs under $75 million in market capitalisation at the time of listing. And even though these listings represented only 12% of the total capital raised in 2017, it is important to recognise the value these growth companies bring to the Australian market and the economy. The ASX continues to demonstrate that the IPO market is a true barometer for and engine of growth, giving a number of these talent-rich companies an avenue for raising capital and delivering future earnings growth and employment.

Fast to year-end, and Australian stock markets were buoyed by confidence with the ASX 200 breaking through the much awaited 6,000 points ‘psychological barrier’. Although increasing levels of volatility in the new year tempered the resurgence in optimism temporarily, the market remains buoyant with a pipeline of IPO candidates for the foreseeable future.

The ASX continues to be a magnet for inbound listings of foreign domiciled businesses, as it offers, and is supportive of, a main board IPO at an earlier stage than many other major markets. 2017 saw an increase in foreign listings, with $512 million of new capital raised by 25 international businesses, with a total market capitalisation of $1.7 billion. The largest listings within this group were Oceania Healthcare (NZ dual-listed), San Francisco-based Credible Labs, China-based Eagle Health and Retech Technology, and the German-based construction technology company Pyrolyx AG.

Globally too, the Asia-Pacific region has been the clear stand-out region and performer, accounting for over 50 per cent of the listings around the world, driven by investor confidence on the back of economic growth, supportive macro-economic fundamentals and momentum in equity markets.
Deloitte is proud to have supported the most successful listings on the ASX this year, ranging from the largest private companies taken public (Netwealth, Bingo Industries, Moxes Australia and New Energy Solar) to a number of equally noteworthy emerging companies and technology players (ELMO Software, Big River Industries and Audinate). The start of 2018 has also seen medicinal cannabis and nutraceuticals start-up Elixinol Global list, and there is a significant pipeline of opportunities ahead for the year.

Economic fundamentals remain in favour in 2018

For all the headlines and political ructions, the global economy saw a relatively strong year in 2017. Global growth was its strongest in several years, with the IMF forecasting growth of 3.6% in 2017 and 3.7% in 2018 amid a synchronised upswing in major economies. That says the global economy looks to be finally normalising after a series of shocks that began with the GFC and then, in quick succession, the Eurozone debt crisis and geopolitical shocks in the Middle East, Europe and Asia.

Stronger economic growth, and lower unemployment, are certainly positives for the IPO outlook in 2018, which should see capital raising volumes comfortably exceed 2017 if the large mooted floats, including Latitude and Colonial First State, together with the new kid on the block that is disrupting the small business lending space, Prospa Advance, take off in the first half. All eyes are on Latitude in particular, which will not only test the market appetite and investor confidence in large floats, but also reflect the attitude of institutional investors to private equity-backed assets.

Weighed against this however, is a potentially less accommodating post-GFC monetary policy environment across many advanced economies going forward. In the aftermath of the financial crisis, major central banks undertook unprecedented policy measures, with a long period of zero (or negative) interest rates, combined with quantitative easing. This has been a supportive environment for asset prices and the financial sector more broadly. While global monetary conditions remain largely accommodative, policy positions are gradually being tightened – however these moves to slowly normalise interest rates have failed to unsettle financial markets.

With the downturn in mining investment basically navigated, the Australian economy is forecast to see a gradual pickup in growth and inflationary outcomes going forward. Recent employment growth has been robust and growth prospects have also been buoyed by significant infrastructure spending in key states, a lower dollar, Asian economy demand for service exports, and resilient commodity prices due to strong demand from China.

According to Deloitte Access Economics, Australia is set to enter a near-term sweet-spot of continued record-low interest rates combined with improving economic performance – and so remains an attractive investment destination across multiple sectors, from tourism and international education to resources and healthcare – and supportive of related IPO activity.
Class of 2017

115 new listings

$6.7bn of new capital raised

Additional market capitalisation of $11.1bn

86 small cap listings

86 Netwealth, FinanceAsia IPO of the year

10.4% Small cap stocks up nearly 70% at year end

25 foreign-based firm listings

Weighted average performance of 36%

Day 1 weighted average returns of 11.4%
The 115 listings during the year had a total market capitalisation of $11.1bn and $6.7bn of capital raised. Of those, 29 exceeded $75m in market capitalisation whilst accounting for 87% of all new capital raised. The weighted average performance of all listings in 2017 was 36%, the strongest performing year for IPOs in the last five years.

A new high water mark was set for listing volumes, with 115 initial public offerings floated in 2017, compared to the previous record of 97 in 2015. Average capital raised was down from $84.1m in 2016 to $57.9m in 2017, reflecting the 86 small cap listings.

New listings were dominated by the financial services industry, with firm value at listing of $5.2bn added to the ASX, representing 46.8% of the total listings. This included the listing of Moelis Australia early in the year, and then Netwealth (provider of investment and wealth management services), which had a market capitalisation of $879m and raised $264m in new equity.

Commercial services ($1.8bn), energy & resources ($1.3bn) and healthcare ($1.0bn) rounded out the other large contributing sectors in 2017.

Another trend witnessed on the back of strong equity markets was the listing of investment companies and funds, the largest of these being Magellan Global Trust (which invests in global blue chip stocks). Magellan had an enviable track record with its unlisted managed fund that outperformed the index by 5.9% since its inception in 2007. The newly listed trust in October 2017 raised $1.5bn in capital.

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Netwealth and Moelis Australia both experienced positive post listing gains through to the end of December 2017 of 96.8% and 186.0% respectively.

Thirty five small cap exploration firms attracted funding through equity markets in 2017. These included the strongest performing new listing of 2017, Ardea Resources Limited (focused developer and explorer of cobalt and zinc-gold deposits).

Ardea’s share price has soared by 850% since listing through to December 2017, following updates on its cobalt and zinc-gold drilling operations, the commencement of pre-feasibility studies and the completion of drilling phases at existing quantified deposits.

Wattle Health Australia Limited (infant formula product producer) was a close second, with share price appreciation of 815% since listing. These returns were predominantly attributable to post listing announcements including successful acquisitions, new distribution agreements with Australian Pharmaceutical Industries for their premium infant formula range and nomination for a brand slot accreditation with the China Food and Drug Authority.

On the flip side, IT service management company ServeTech Global Holdings and copper and gold miner Magmatic Resources Limited suffered share price losses of around 90% from their issue price.

The table above shows the weighted average performance of 2014 to 2017 listings, through to December 2017. The class of 2017 was one of the best performing on record, with the highest number of new listings (115) and weighted average performance of 36.0%. This year, the weighted average performance on Day 1 of listing returned 11.4% compared to 9.5% last year.

Netwealth was awarded the FinanceAsia IPO of the year for 2017.
Financial services was a key driver of IPO activity in 2017, with 17 new listings, total new capital raised of $4.2bn and sector weighted average performance of 33.5%. Boutique investment bank and asset manager Moelis Australia, and wealth management firm Netwealth underpinned these returns, with share price appreciation of 186.0% and 96.8% respectively. Digital disruptor SelfWealth, which offers low cost online broker services for self-directed investors also performed strongly, returning 45.0% to December 2017 since listing in late November.

Commercial services was the other dominant sector of 2017, raising $866m in new capital from 11 issuances and achieving weighted average performance to date of 48.3%. This outcome was driven by Bingo Industries which accounted for 50% of new capital within the industry, raising $439.5m, and industrial additive manufacturer Titomic Limited (which specialises in 3D metal printing) which achieved substantial share price growth of 567.5%.

Bingo Industries remained heavily involved in transactions, undertaking a secondary raising of $120 million in December 2017 to fund the acquisitions of National Recycling Group and Patons Lane, pursue additional organic redevelopment opportunities and repay debt used to fund its Has-a-bin acquisition in September 2017.

Energy and resources led the charge in terms of volume, with 37 new listings, representing 32% of all IPOs by number in 2017 and weighted average performance of 44.6%. Sector activity was characterised by small cap listings, with 35 issuances having a market capitalisation of less than $75m. The two larger listings, Windlab Ltd and New Energy Solar, had market capitalisations of $134.3m and $505.8m, and raised $55m and $200m respectively.

The property and construction sector was subdued relative to last year, only accounting for 1.7% of all IPOs by number and 3.7% of capital raised. The sector raised $247m in equity capital through two new listings, but was the only sector to experience negative weighted average share price performance in 2017 of -15.4%.
Emerging companies

- New capital raised: $820m
- New market capitalisation: $2.2b
- Ardea Resources Ltd: 850%
- Resource and technology companies: 60%
- 75% of new listings by volume in 2017
Emerging companies continued to dominate listing volumes, as firms with a market capitalisation of under $75m accounted for 75% of all new listings in 2017 by volume.

Of the 86 small cap listings, 52 experienced positive share price returns, animal pharmaceutical company CannPal Animal Therapeutics Ltds share price was steady at $0.20 and 33 new Emerging Companies suffered negative performance since listing through to December 2017.

The grouping was strongly represented by the energy and resources sector, with 35 new listings which had a combined market capitalisation of $673.2m and new capital raised of $297.2m and the technology, media and telecommunications (TMT) sector with 17 new listings which had a combined market capitalisation of $548.0m and new capital raised of $148.0m.

Of interest in the TMT sector, delivery management software company Getswift was trading at $3.70 at the end of December 2017, up 1,750% from its initial listing price of $0.20 in December 2016. However the company's stock was suspended from trading on the ASX in early January 2018, amid governance concerns regarding potential breaches of its continuous disclosure requirements. Specifically, revised market announcements indicated that the majority of announced enterprise contracts (which drove initial share price gains in 2017) are still in pre-revenue generation phases. When the company exited its trading halt and resumed trading in February 2018, the share price tumbled 55%.

The top performers were Ardea Resources and Wattle Health Australia, which experienced share price appreciation since listing of 850.0% and 815.0% through to December 2017. The worst performers were Magmatic Resources and ServTech Global Holdings, which returned -89% and -90% respectively.

On a weighted average basis, 2017 small cap listings returned 60.3% through to the end of the year.

Emerging Companies (<$75m) - Share price performance to December 2017

Top five
- Ardea Resources Ltd 850%
- Wattle Health Australia Ltd 815%
- Cann Group Ltd 813%
- Alderan Resources Ltd 650%
- Elsight Ltd 635%

Bottom five
- ServTech Global Holdings Ltd (90%)
- Magmatic Resources Ltd (89%)
- United Networks Ltd (68%)
- Velocity Property Group Ltd (62%)
- Freehill Mining Ltd (62%)
The ASX continues to attract foreign-listed companies looking to tap equity capital markets and remains a capital hub for the Asia Pacific region, with eight new Asian-based listings in 2017 representing 32% of foreign listings by volume.

Foreign companies seeking access to capital for growth are drawn to the profile and good standing of the ASX being one of the most prominent exchanges in the region, Australia’s stable political environment, the deep level of trading liquidity afforded from large institutional support, and the robust compliance and governance structures in place.

The ASX has also been a magnet for new listings from the USA, with seven new listings representing 28% of foreign listings by volume in 2017, which raised $1.17bn of new capital and had a total market capitalisation at listing of $501m. The USA-based listing sub-group achieved weighted average share price appreciation of 32.5%, driven by metal mining company Alderan Resources and loan comparison firm Credible Labs Inc, which were up 650.0% and 10.7% respectively at year-end.

New Zealand was another source of foreign-listed companies in 2017, raising $214m in new capital and achieving weighted average share price performance of 14.8%. This was substantially driven by the listing of healthcare company Oceania Healthcare, which raised $200m in new capital and returned 19.6% since listing through to the end of December 2017.
<table>
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<th>Country</th>
<th>Number</th>
<th>Market capitalisation</th>
<th>Capital raised</th>
<th>Weighted average</th>
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<td>5</td>
<td>326</td>
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<td>(25.9%)</td>
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<td>Chile</td>
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<td><strong>1,719</strong></td>
<td><strong>512</strong></td>
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What were the critical ingredients to the successful listing of Netwealth in November 2017?

A strong historical track record and bright prospects as a disruptor in the wealth sector with significant long-term growth opportunities were fundamental. This was supported by an experienced and skilled management team and board of directors and the commitment of the major shareholders to the business. Early scoping of the IPO process with tier-one advisers and supportive equity market conditions were also important contributing factors to a successful listing.

What were the key readiness steps undertaken by the business in preparation for life as a public company and did the longevity of the board prior to IPO assist with preparations?

Operating in the financial services sector under the regulation of both APRA and ASIC, Netwealth’s corporate governance standards and operations were already akin to those of a listed company with a board of directors (majority independent) who had a very good understanding of the business. A board with a combination of business, legal, accounting, and investment banking skills and public company experience meant there was a good understanding of the magnitude of the requirements of an IPO. For Netwealth, experienced advisers were appointed early in 2017 and a timetable with key milestones was agreed.

A combination of both the longevity of the board and skill set positively contributed to the IPO process.

Non-executive director perspectives: Tim Antonie

Tim Antonie
Netwealth Group Limited non-executive director

Tim is currently also a director of Breville Group Limited, Premier Investments Limited and Village Roadshow Limited.

We recently reflected on the successful initial public offering of Netwealth Group Limited in November 2017 and asked Tim for some of his insights and perspectives.
After accepting the role, I recommend attendance at due diligence committee meetings, carefully reading all reports and future versions of the prospectus and supporting documents before approving the release of the prospectus and accompanying documents to third parties.

As an experienced non-executive director, what advice would you give to a board of a private company considering an initial public offering and what are the key challenges commonly underestimated?

My one piece of advice is never underestimate the resources and time required to prepare and execute an IPO.

To ensure you can achieve this, appoint quality and experienced advisers, agree scoping and timing, critically assess whether you have the internal resources and systems to achieve this timetable while running the business on a day to day basis, and do not fall behind the timetable.

One key aspect to this is the early development of a detailed business plan and financial forecasts. To provide sufficient time for review and consideration, it is fundamental that this occurs around four months prior to finalisation of the prospectus.

Following on from the previous question, for a non-executive director joining a company relatively late in their IPO preparation, what are the key aspects to consider?

Given the legal responsibilities of a non-executive director I would be very reluctant to join relatively late in the process.

However, with that said, before I committed to the role and while not an exhaustive list, I would:

- Assess the value I can add to the board and the chairman’s expectations of me;
- Spend time understanding the process that the board has gone through in preparation of the business strategy and historical and forecast financial information;
- Take a view on the quality of the board and management team and the prospects of the business;
- Gain an understanding of recent financial performance and emerging risks through review of monthly management accounts and board papers;
- Review the company’s policies and procedures (particularly in relation to corporate governance and audit);
- Review the latest draft of the prospectus and due diligence committee minutes and meet with the external lawyers, accountants and investment banks; and finally, I would assess the director & officers’ liability insurance policy and director indemnities.

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One key aspect to this is the early development of a detailed business plan and financial forecasts. To provide sufficient time for review and consideration, it is fundamental that this occurs around four months prior to finalisation of the prospectus.
Aside from Latitude Financial Services potentially being the marquee listing of the year, we expect most private equity (PE) firms to be acquisition-focused in 2018, with a limited number of public equity market exits.

2017 saw only two PE-sponsored IPOs, Big River Industries listed by Amazilia Capital (who retained their investment stake through the IPO) and Oceania Healthcare listed by Macquarie Bank. In comparison, there were five PE-sponsored floats in 2016 and a significant number of PE exits via the public equity markets in the period from 2013 to 2015.

In 2018 we expect to see the majority of PE firms being acquisitive on the back of the significant fund raising efforts across 2015 to 2017 and a limited number of portfolio investments in the exit pipeline via IPO.

The most significant PE-sponsored exit mooted in 2018 is Latitude Financial Services, currently owned by KKR, Varde Partners and Deutsche Bank. With a potential market capitalisation above $4bn, Latitude Financial Services could be the largest listing of 2018 and a near term litmus test for other larger PE-sponsored exits.

Despite criticism of a small number of PE-sponsored IPOs in recent years, we expect investors to remain focused on the quality of the underlining business rather than the previous owner.

In our view, well-developed growth strategies coupled with proven management capability and demonstrated earnings and cash flow sustainability will remain priorities for investors in assessing future IPO candidates.

We also expect PE sponsors to retain considerable investment stakes post listing to demonstrate alignment of interests with investors, as is common in the United States and other sophisticated markets. 
1. Be prepared
Key trend to begin preparations for IPO earlier, including weighing up structuring options and up-skilling management team via IPO deal room.

2. Dual track process
Maintaining flexibility in the listing process and structural options via maintaining a dual-track trade sale workstream in conjunction with an IPO process, building competitive tension and driving deal value.

3. Increased rolled equity
Shift in the percentage retained by founders/cornerstone in the listed entity, potentially impacting opportunities afforded by some tax structures.
4. Float Co v Sale Co
We are seeing a continued preference for a ‘Float Co’ structure to be adopted. Of the Top 10 IPOs by market capitalisation in calendar year 2017, a clear majority favoured this approach.

5. Incentive plans
Increased focus on a divergence of incentive plan models to drive performance of employees and senior management post-listing.

6. Real time review
Increased activity by revenue authorities immediately following listing – focused on a range of taxes including stamp duty, GST as well as income tax outcomes.

7. Post-IPO dividends
Many companies indicate an intention to frank to the maximum extent possible and may specify a target net profit after tax payout as part of the listing materials. The average net after-profit dividend approximates 60-75%.

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Key tax considerations for incentive plans

1. A key aspect of an IPO process will be to ensure that the company incentive plans reflect market practice for a listed company.

2. Consider how to deal with any existing incentive plans leading up to and on and after IPO (e.g. whether private company plans will need to be closed out or amended or new plans introduced to reflect public company practice and ASX requirements).

3. Consider any costs to closing out or rolling over old incentive plans or introducing new incentive plans (e.g. whether any costs / payments on closing out will provide a future tax benefit to the listed group).

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1 Of the Top 10 corporate listings (excluding dual listings, stapled arrangements and listed investment companies).
4. An appropriate combination of cash and share-based incentives keep key management personnel focused on short, medium and long-term value delivery to company stakeholders.

5. Consider rewarding general employees with up to $1,000 in company shares at no cost and tax free as part of the IPO.

6. Rights to share plans for key management with performance and service hurdles keep participants incentivised both pre and post-IPO.

7. Allow management and senior employees to salary sacrifice up to $5,000 in return for company shares as part of the IPO.

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