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Half-time lead
Deloitte 2015 IPO market update

September 2015

In collaboration with

MERGERMARKET

First half at a glance

Following a year of record listings, initial public offerings (IPOs) on the ASX have settled into more modest territory in the first half of 2015, with a growing appetite for stocks that offer a balance between income and capital returns as market volatility rears its head once again.

At the close of the first half (1H15), floats on the ASX raised $2.5bn (with market capitalisation of $5.4bn) through 30 IPOs. While this exceeded the 22 listings for 1H14, funds raised failed to surpass the $4.6bn of that period ($8.5bn market capitalisation including Spotless Group, Genworth, Asaleo and SG Fleet), a drop of 53% in average listing values.

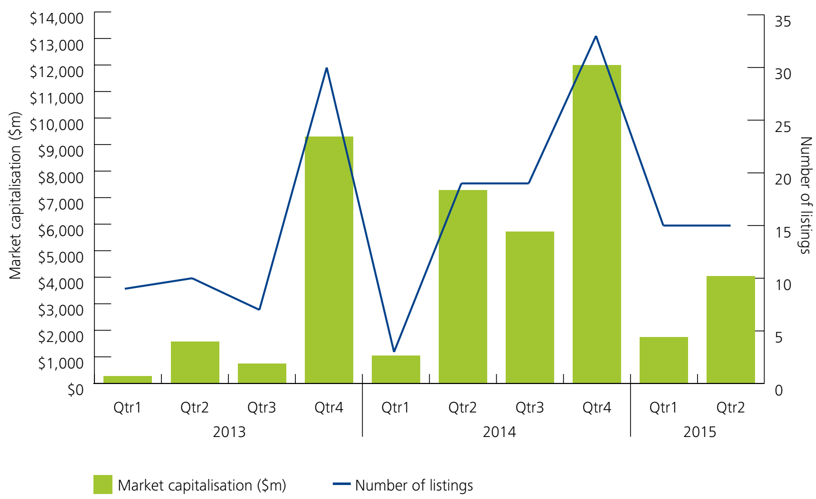
Despite these differences, half-on-half year comparisons show that debut growth improved, with 1H14 listings achieving average returns of 7.3% and 1H15 returning 19.1%. Additionally, ASX performance to June was up 0.4% in comparison with the same period last year. There were a further 18 listings over the course of the last two months to the date of this report, including Costa, Pepper Group and Amaysim, that continue to exceed market expectations.

With market fundamentals largely unchanged (albeit with fewer behemoth listings such as the $5.7bn Medibank IPO in November 2014) IPO proceeds should find it easier to meet their targets going into the second half of 2015, which is expected to see a number of sizeable listings, including Link Market Services, Genesis Care, IDP Education and Wellard Group.

"2014 listings have continued to build on their performance and significantly outperformed the ASX. Despite global volatility, we are seeing strong investor confidence given the quality of IPOs — you only have to look at the 1H 2015 listings and their impressive performance."

Ian Turner, Head of Transaction Services

ASX public listings



Macroeconomic overview

As the global experiment with cheap credit continues, the macroeconomic environment remains one of opposing forces when it comes to listings. Although the US is edging closer to its first interest rate hike, that does not appear to be true of Europe or Japan, and much of Asia is busily easing policy.

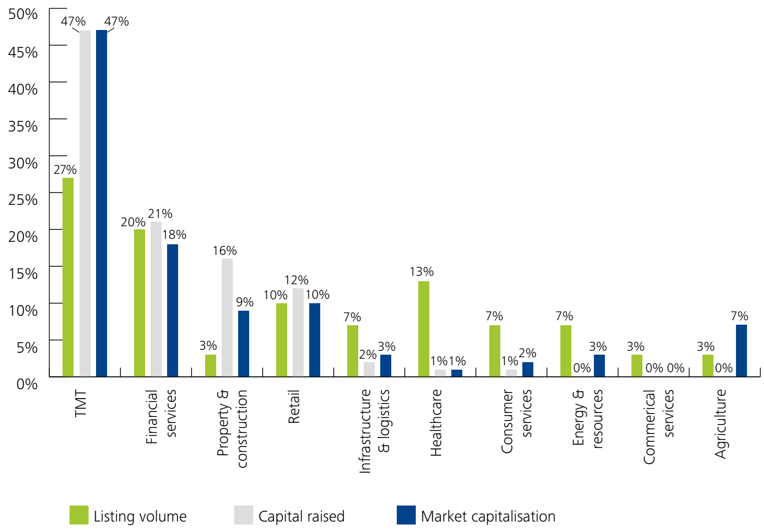
Low rates will not be here forever – although change is not imminent and cheap credit will be around for a while longer yet – but when they do unwind, it will be a wild ride for many markets. The Reserve Bank of Australia may not cut again in this cycle, as it is a bit spooked by housing prices. Also, low interest rates continue to support equity, amplified by the dollar, which has made the Australian market more attractive for foreign investors. On the other hand, a modest Australian economic outlook will dampen future cash flow expectations of companies relying on domestic demand.

Expected US interest rate rises in the foreseeable future are likely to see a shift in global funds back to the US. While such capital flight is unlikely to affect Australia as much as other nations, it will play a role in increased financial market volatility that is starting to emerge.

CFOs of Australia's largest listed companies, however, appear to weigh the positive factors most heavily. The Deloitte CFO Survey[1] has reported a more positive outlook in the last six months, with significant improvement in net optimism. What's more, 20%

[1] The Deloitte CFO Survey targets the CFOs of major Australian listed companies. It has been conducted on a quarterly basis since Q3 2009. http://www2.deloitte.com/au/en/pages/about-deloitte/articles/cfo-survey-2015.html

ASX listings by sectors (1H15)



of CFOs expect to increase equity issuance in the next 12 months, while more than half of respondents perceive equity to be an attractive source of funding – a substantial improvement compared to this time last year.

Tech's time to shine

The technology, media, and telecommunications (TMT) industry led listings for 1H15, accounting for 47% of listing values, and 27% of all IPOs. Favourable conditions are adding to confidence among tech companies and financial sponsors that an IPO presents an attractive option to raising growth capital and establishing a profile on public exchanges. TMT activity was led by the $2.1bn listing of accounting software developer MYOB Group, followed by the floats of billboard operator QMS Media and bespoke software developer Touchcorp. The remaining listings had an average market capitalisation of c.$50m, underscoring the trend of young, small-cap technology firms finding their place on the ASX. While investor appetite for tech runs high, buyers are cautious and may limit investments to tech firms with robust operating models, profit history, and strong balance sheets, as opposed to early-stage companies.

Trending sectors: Financial services and property

Financial services stood out for its 21% share of listing values. With six IPOs, the sector had the second largest number of listings by industry, and one of the largest IPOs for the half year with the $550m float of Eclipx Group.

Property and construction companies also received strong investor support, with the sector accounting for 16% of listing values. Public listings are being driven by companies looking to profit from macro-trends in the economy, primarily Australia's property boom and ageing population.

Gateway Lifestyle, a developer of modular estates for the elderly and those approaching retirement, buttressed IPO figures in the sector with its $500m listing. The company's chief executive said fragmentation within the industry gives the company abundant opportunity to acquire properties and developers, providing ample scope for growth and expansion, a trend likely to encourage activity from other companies within the industry.

Performance update: The class of 2014

Following our 2015 IPO report, the majority of listings for the class of 2014 continue to show impressive growth. The top ten IPOs [overleaf] based on share price performance at December 2014 have for the most part continued to significantly increase gains into 1H 2015. The average performance of all companies that listed in 2014 during the first half of 2015 was 12.7%.

Listings of healthcare and financial services companies, two stand-out sectors in 2014 with average performances of 11.4% and 16.4% respectively, posted striking differences in returns at the close of 1H15.

"Raising their attractiveness (value) is one component to encourage investors, but companies that want to be truly effective will make the proposition simple with a well-articulated story to their business. Stocks that struggled to go public this year were typically not well understood by the market."

Tapan Verma, Director

The class of 2014 - Performance update, top 10 IPOs >$75m in 2014

Company name	Listing date	Industry	Private equity owner	As of 31 Dec 2014	As of 30 June 2015
Beacon Lighting Group Ltd	15-Apr-14	Retail		127.3%	203.0%
IPH Ltd	19-Nov-14	Commercial services		66.7%	123.8%
Bellamy's Australia Ltd	05-Aug-14	Retail		65.0%	337.0%
Mantra Group Ltd	20-Jun-14	Consumer services	CVC Capital Partners	61.1%	90.0%
Victor Group Holdings Ltd	09-May-14	TMT		40.0%	-
Pacific Smiles Group Ltd	21-Nov-14	Healthcare	TDA Asset Management	38.5%	80.8%
Burson Group Ltd	24-Apr-14	Retail	Quadrant	37.4%	86.8%
Genworth Mortgage Insurance Australia Ltd	20-May-14	Financial services		37.4%	18.5%
Isentia Group Ltd	05-Jun-14	TMT	Quadrant	35.8%	83.8%
Healthscope Ltd	28-Jul-14	Healthcare	TPG and Carlyle Group	29.5%	29.5%

While healthcare IPOs increased average performance to 29.2%, largely on the heels of growth in Pacific Smiles Group and Regis Healthcare, financial services saw industry and company gains evaporate.

Performance in tech IPOs continued to post growth from averages of 12.9% in 2014 to 26.2% as of 1H15, while an apparent boom in retail resulted in a dramatic increase from 10.4% to 79.8%.

2014 listings performance update, by sector

Sector	FY 2014	1H 2015
Commercial services	46.3%	98.1%
Retail	10.4%	79.8%
Infrastructure & logistics	(26.8%)	33.5%
Healthcare	11.4%	29.2%
Consumer services	33.1%	27.3%
TMT	12.9%	26.2%
Property & construction	17.9%	2.0%
Financial services	16.4%	0%
Energy & resources	(83.3%)	(11.2%)
Education	(35.3%)	(37.7%)

Listings in 2015

Despite the recent turbulence in global markets, there have been a total of 48 listings (36 in 2014) up to the date of this report, raising $4.4bn and representing a total market capitalisation of $8.4bn. Technology and financial services listings continue to drive investor appetite and represent 50% of all 2015 listings.

The IPO market continues to significantly outperform the ASX 200, demonstrated further by strong growth of stocks including Eclipx (34.8%) and the recent listing of Pepper Group (29.2%), amongst others.

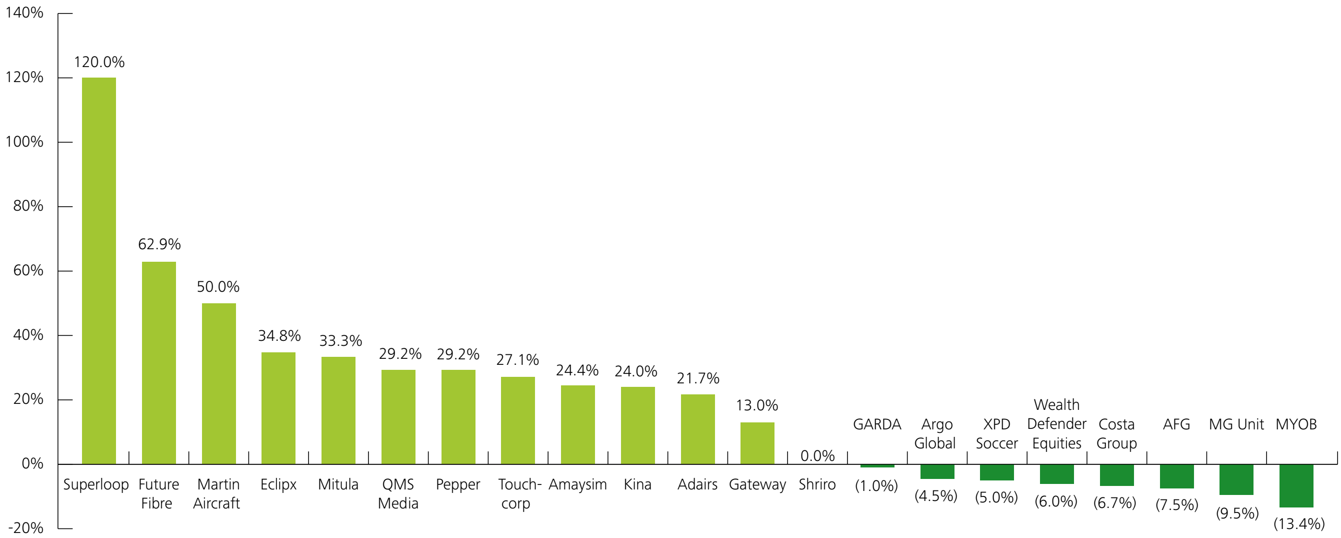
Of the 48 listings in 2015, 21 had a market capitalisation in excess of $75m, generating an average share price performance gain of 7.2%. In comparison, the ASX 200 has continued to be subject to market volatility on the back of international uncertainty, dropping 4.1% over the period to 21 August 2015.

Private equity steals the show

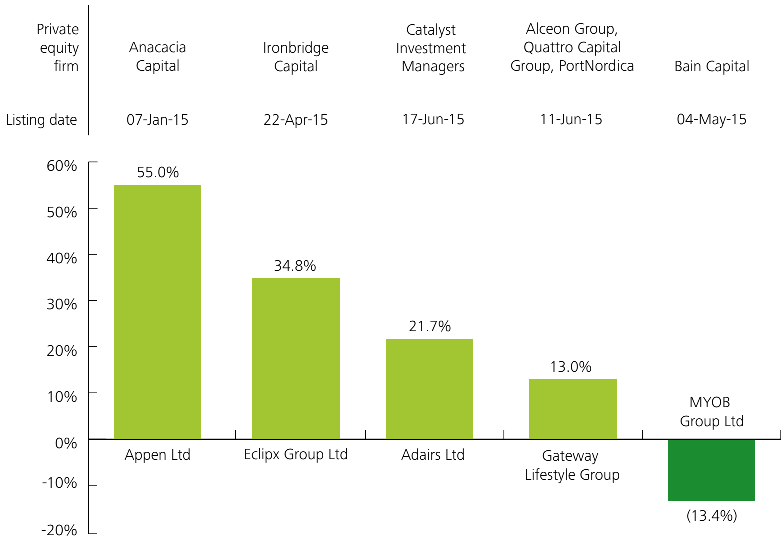
With just five floats during 1H 2015 with a market capitalisation of $3.6bn and accounting for 67% of total listing values for the half year, private equity once again shines. This surpassed full-year deal statistics for 2014, when private equity exits and equity sales via IPO accounted for 46% of listing values and 40% of volumes.

Performance of private equity-backed companies have, on the whole, witnessed positive growth, with average share price movement of 19.6% from listing date to the date of this report. Of the five listings, only accounting software company MYOB, owned by Bain Capital, saw a drop in the stock price, posting a loss of 13.4% since listing in May 2015, with concerns over the growing market share of Xero and other cloud-based platforms.

Performance of >$75m listings for 2015, to 21 August 2015



Private equity-backed IPO performance (21 August 2015)



Comparing exchanges: Hong Kong and Singapore

While the ASX continues to hold investor interest, Hong Kong has maintained its position as one of the top stock exchanges in the Asia-Pacific region by listing volume and value. In 1H15, the HKEx had 46 listings raising $22.2bn (HK$127bn), and expectations hold that these figures could double by year end. The exchange featured two of the world's top IPOs, in the listing of China-based Huatai Securities and GF Securities, and a promising pipeline is also forming as other Chinese financing service providers follow suit with plans to IPO in 2H15.

By contrast, IPOs in Singapore all but ground to a halt, with public listings raising just $1.1bn in 1H15. This was a year-on-year decline of 54%.

Asian issuers set sights on ASX

The Chinese government's freeze on IPOs on China's main exchanges and the aftermath over the last two months could cause some companies to reconsider their listing options in favour of an ASX listing when seeking to go public. This provides an alternative to smaller Chinese companies wanting to avoid the cost and free float requirements of other Asian exchanges. In some of Asia's larger exchanges, these figures can be quite high, with Hong Kong requiring 25% and Singapore ranging from 12-25%.

Listing on the ASX gives Asian companies global exposure, and a market and brand profile. It can also provide companies, especially smaller privately-held businesses from China and companies from New Zealand looking for a dual listing, with better access to debt markets and a boost to liquidity as an option for funding growth and broadening the potential investor and capital base.

Backdoor listings and reverse takeovers

A backdoor listing reduces the costs of becoming a public company. The listings are facilitated when an ASX aspirant strikes a deal with a failed or failing listed company looking for a way to repurpose its administrative shell to unlock some value for its shareholders.

Tax value considerations
Significant cash tax savings can be added through proper analysis of tax opportunities and risks associated with an IPO. To the extent any cash savings or tax benefits arise, it is possible to recognise them in the prospectus over the forecast period, which can impact the value proposition for the listed group.

A key consideration relevant to cash flows and forecasts is the treatment of transaction costs. Depending on the nature of the cost and listing structure, some costs may be immediately deductible for Australian income tax purposes (a 30% tax benefit for corporate groups), while others may be deductible over five years.

Transaction costs can give rise to immediate significant one-off GST cash refunds. As such, proper consideration can maximise GST recovery while also ensuring appropriate documentation for lodgement purposes.

Other tax benefits impacting the forecast period can include the resetting of the tax value of underlying tax advantaged assets (such as inventory or depreciable assets) to market value and/or tax attributes such as losses.

To maximise shareholder value, distribution strategies and the ability to best utilise franking credits (in terms of exiting shareholders or for investors over the forecast period) are also important and can be impacted by specific tax outcomes.

Incentive and share option plans
The value proposition for senior management and employees in relation to the listed group should be considered early on in the IPO timeline. Any plan should appropriately incentivise and reward key stakeholders, while managing tax outcomes and documentation requirements. This may include short term incentive plans such as bonus structures or longer term executive incentive equity plans.

There are a number of complexities with implementing incentive plans, which should be considered early to ensure appropriate design and implementation and disclosure in the prospectus from an accounting and tax perspective.

Unlike IPOs, backdoor listings are usually not noticed. Brokers rarely promote them and there is no central information source that tracks recent and upcoming backdoor listings or analyses their aggregate performance. They quietly list and stay below the market radar.

Tech companies are taking advantage of failing exploration/mining companies, utilising these companies as shells to facilitate a backdoor listing. This has attracted the Australian Securities and Investments Commission's attention, which is concerned about sufficient and appropriate disclosure.

Outlook: 2H15 and 2016
As 2016 approaches, global economic factors are likely to weigh heavily on investor sentiment whilst also posing challenges to company management. Despite volatility and pricing expectation gaps, there continues to be a very healthy pipeline of c.40 IPOs for the remainder of the year and into early 2016.

Sustained performance of 2014 and 2015 listings demonstrates the quality of stocks that are coming to market. As a result of resolutions over the Greek Crisis, a continuing low cash rate, restrictions and market intervention on the Chinese exchange, the ASX will in our view continue to prove an attractive proposition for growth and capital access — once the dust from the recent market volatility settles.

"It is encouraging to see that listings in the last two years have held their own, which reflects the quality that investors have come to expect. There's a lot of positive news coming out of this reporting season with the vast majority of 2014 listings exceeding their prospectus forecasts."

Ian Turner, Head of Transaction Services

About Mergermarket

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