LECTURE 1
OPTIONS TO RAISE EQUITY

- Unlisted firms
    - Private Equity Financing
      "Angel" Finance : Invest their **own money** into newly startup company
      Venture capital : Organizes & manages **funds** from investors (Not at once but in stages, mainly in high tech industries)
    - Initial Public Offering **(IPO)**
      Listing shares **first time**

MOTIVES FOR GOING PUBLIC

- Create public shares for use in future **acquisitions** (Acquire another co)
- Establish a **market price / value** for firm
- Enhance **reputation**
- Broaden base of **ownership**
- Minimize **cost of capital**
- Attract analyst's **attention**
- Debt is **expensive**

ADVANTAGES OF GOING PUBLIC

- Access to **additional capital**
- Allow venture capitalists to cash out
- Increase **customer recognition**
- Establishes **firm value**

DISADVANTAGES OF GOING PUBLIC

- Creates **substantial fees** (Legal, accounting, investment banking fees – 10%)
- Greater degree of **disclosure**
- **Dilution of control** of existing shareholders
- Special '**deals**' to insiders will be more difficult
- Managing **investor relations** is time-consuming (satisfy them)

PROCEDURES

1. Appointment of an **underwriter**
    - Acts as **intermediaries** between the firm & investing public
    - Manages process of IPO on behalf of the firm (method used to issue & market the securities, pricing & selling)
    - **Firm commitment contract** (If underwriters cant sell all shares, they have to buy them)
    - **Best efforts contract** (Issuing firm bears the subscription risk – small, unknown companies)

2. Prepare preliminary **documents,** undertake **due diligence** process (explore co in & out)
3. Institutional **marketing** program (Attract interest)
4. **Exposure** period : lodge doc with ASIC and listing application with ASX
5. Marketing & **offer** period (3-4 weeks)
6. Offer closes, shares **allocated**, trading commences

VALUING IPOs – PRELIMINARY VALUATION

- No **market price** (hard to determine)
- **Discounted cash flow** (DCF) analysis
    - **Present value** of cash flow over the life of the company
- **Comparable** firms analysis
    - Compare with publicly traded firms in the **same industry** that have similar risk & growth prospects (PE ratios, price/sales ratios)

VALUING IPOs – PROCEDURES

1) Fixed pricing
    - Traditional method
    - **Cant change** the price
    - Need to determine the final price early
    - Subject to market movement (**High risk** of under-subscription)
2) Book-building
    - More time, costly
    - Ask institutional investors to indicate quantity they would purchase & price, record it in a 'book'
    - **Lower** under-subscription risk (Lower price uncertainty)
    - **Investment banking** conflicts
3) Open auction
    - Investors submit their **bids**
    - Securities sold to successful bidders

COSTS OF IPOs – DIRECT

- Underwriters
    - In the form of a **spread** (Underwriters' buying price – offering price)
    - 7% of the proceeds (money raised through IPO) to the issuer
- Direct administrative costs
    - Management, lawyers, accountants
    - 1% of the proceeds

COSTS OF IPOs – INDIRECT
UNDERPRICING

- Issuing securities at an offering price **lower than the actual market value** of the security