

The Future of Equity Capital Raising

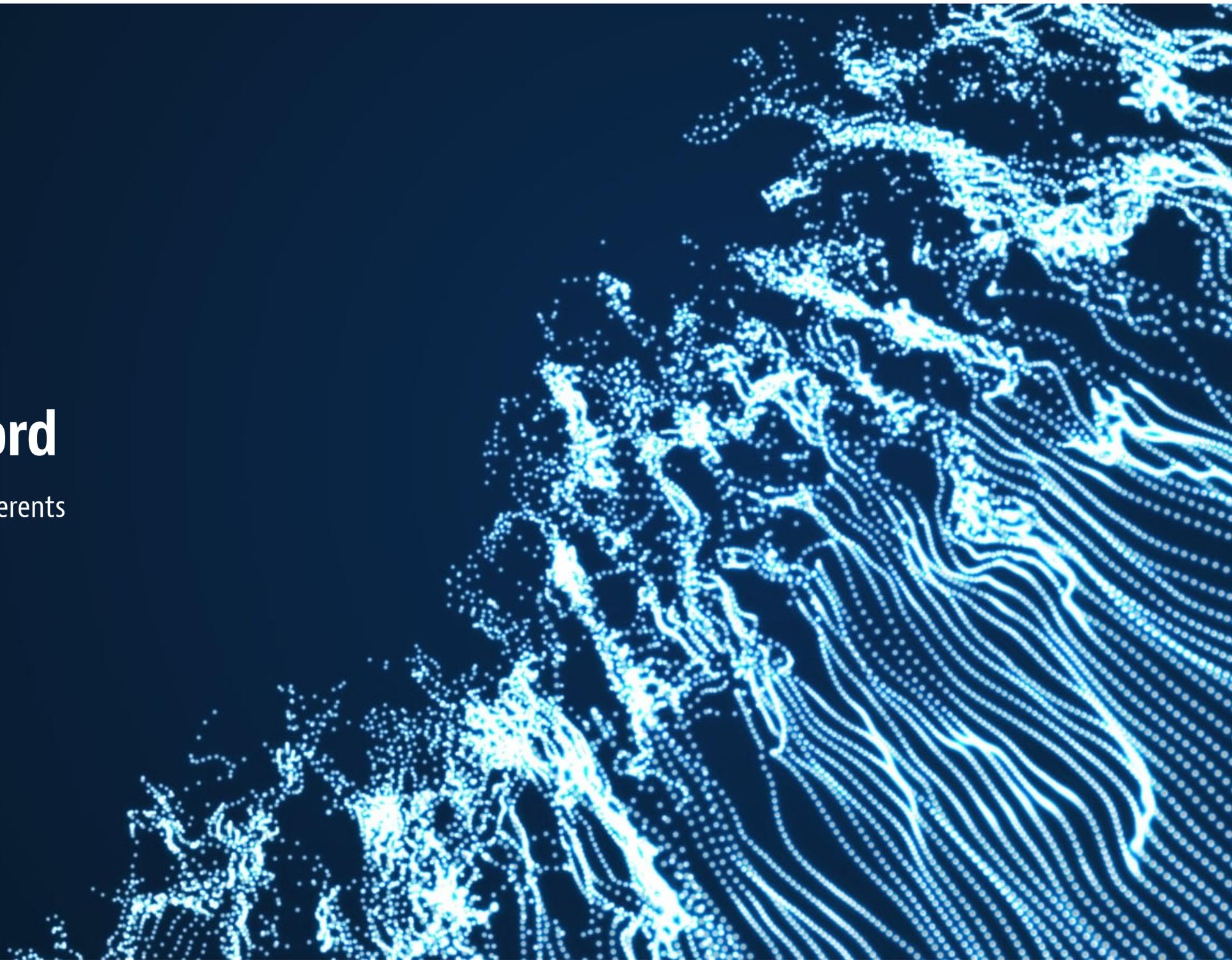
How Private Capital is Reshaping Public Markets

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POWERHOUSE**

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Foreword

By Koen Vanhaerents



Despite a bull run of a decade, the global markets are now at a unique set of cross-roads. Macroeconomic and geopolitical turbulence continue to prolong investor and market caution across all regions, and yet, some industries and countries are showing exponential economic growth, and look set to continue to do so.

While the future IPO pipeline remains robust, the sands of equity capital-raising are experiencing a shift. In this forward-looking report, we explore the changes that have already begun to emerge and those we expect to see in the longer term.

Technology, private capital raising and the role of the exchanges are all set to change the traditional route to IPO and role of the public capital markets. Emerging technologies, such as AI and blockchain, are expected to influence the way in which markets will work and may result in the creation of new platforms for allocation of capital across asset classes. The rise of private capital due to higher returns and less regulation is set to challenge the role of the public capital markets in the period to come.

With stock exchanges re-examining the role they have to play in offerings, modernising their regulations, and positioning themselves as credible alternative exchanges, we are now seeing the beginnings of rivals to the traditional go-to venues of NYSE, Nasdaq and London.

Looking five, ten, twenty years down the line, one thing remains certain – equity markets will remain unmoved, albeit not unchanged.



Koen Vanhaerents

Head of Global Capital Markets, Baker McKenzie



Introduction and Key Findings

Assessing the outlook for equity capital markets and the IPO market.

Throughout 2019, equity capital markets will continue to be stalked, and perhaps even held hostage, by some of the same macro-economic and geopolitical risks that conspired to derail benchmark indices and IPO activity at the end of 2018.

From the threat of a prolonged global trade war and its impact on the global economy, to the impact of rising interest rates and potential economic disruption from Brexit, equity capital markets could again be buffeted by the volatility these risks provoke.

But looking beyond what could happen this year, indeed, taking a three to five year view, what is the outlook for equity capital markets and for the IPO market in particular? Moreover, to what extent is the IPO market undergoing change? What are the factors driving this and what in turn does this mean for companies going public in the future?

Some answers have already begun to emerge. The magnitude and availability of private capital has, for instance, been an important factor in increasing the age and size of companies before they list. And there

are strong signs this trend will continue, giving rise to even older and larger companies floating in the future.

There are also some interesting trends – both developed and emerging – around where and how companies list, and the role of new technologies in the capital raising process too.

Indeed the total value of cross-border listings last year rose to over \$60bn – the highest since 2014 – with the US, Hong Kong and UK the favoured destinations and Chinese companies, particularly from the technology sector, being a key driver of activity. It's a trend that is expected to continue to grow over the longer term, supported by, among other factors, intensifying efforts by exchanges to adapt and adjust their listing rules to better compete and win more IPO business.

The advance of technology will surely also help enhance the role of the exchange and transform the IPO process too. Some exchanges are already exploring the use of blockchain-based post-trade settlement infrastructure for small and medium sized companies. And at the front-end, investment banks' ability to make best use of new technologies – from advanced data analytics to virtual reality – could help re-shape and enhance established listing processes, benefiting issuers and investors. These are just some of many factors driving change and potentially creating a new issue market in the future that is different to what it is today.

While the future IPO pipeline remains robust, the sands of equity capital-raising are experiencing a shift.

Koen Vanhaerents - Head of Global Capital Markets, Baker McKenzie

In order to assess and understand some of the underlying dynamics shaping the IPO market, we surveyed 353 senior executives from public and private companies across industries globally to capture their insight on the topic.

A series of in-depth interviews with equity capital markets bankers, company finance and stock exchange executives as well as lawyers, were also conducted to provide further insight and opinion on the trends and developments they are seeing. What we found is that while there is a healthy pipeline of potential IPOs, there are some interesting trends to have emerged and are emerging around when companies go public, why, where and even how.

Key Findings



A promising IPO pipeline for the future

83% of 200 executives from private companies said their company is considering a partial or full IPO, with most of them (65%) stating this may happen sometime in the next three to five years.



Valuation and liquidity most important in deciding where to list

66% of executives from private companies said valuation and liquidity was the most important factor in selecting which exchange to list on, followed by the strength of the local regulatory regime (55%) and peer group performance (34%). Executives from public companies take a similar view although they rank analyst and investor coverage (39%) as more important than peer group performance (22%).



Recognising the tentative emergence of IPO alternatives

65% of executives from all companies (public and private) expect to see a higher volume of direct listings (free of traditional investment bank underwriting support) in the future. In addition, almost all (94%) executives expect to see equity crowdfunding become more important to start-up companies seeking to raise capital for growth and development.



The rise and fall of public and private markets

84% of executives from all companies believe some form of shift – specifically from public to private markets – is underway in where companies source equity capital from, with most of them (53%) believing a shift is only temporary. Most executives in Europe and Asia see the shift as potentially marking the beginning of a longer term trend.



The impact of private capital on IPOs

84% of all executives believe that companies are waiting longer to go public compared to the past. And close to half (48%) of private companies believe the amount of private capital available is an important factor in determining when they might list, ultimately enabling them to stay private for longer before they list. Most private companies in Europe and Asia believe this.



Understanding the key benefits of public markets

Most executives from public and private companies believe the most important benefit of public equity markets is the efficient allocation of capital (55%), followed by enabling companies to repair balance sheets (50%), and the promotion of transparency and high corporate governance standards (44%).

Future of IPOs

From established to emerging trends.



After a bull run of more than a decade, global equity markets are at an interesting juncture, potentially either trending higher on improved economic and geopolitical sentiment or falling on a mix of macro-risks and concerns.

The jury is still out on which direction equities will take and when. But certainly the market correction and volatility of last year at the very least reflects economic growth and stability concerns, and the late stage in the cycle that global financial markets are in.

The future is, therefore, far from certain. But there are strong signs of resilience and in equity capital markets, the signs are strongest for company IPOs.

Indeed companies globally raised just over \$200 billion through IPOs last year – the highest annual total value since 2014 – and this despite a five-year high of 173 pulled or postponed transactions due to the market volatility at the end of last year. Year-on-year the number of IPOs was down on 2017 but the total capital raised was up due largely to some 40 IPOs from unicorns, or high-growth

private companies valued at \$1bn, and mega-fundraisings such as the \$21bn float of SoftBank Group Corp's telecoms subsidiary – one of the largest IPOs of all time.

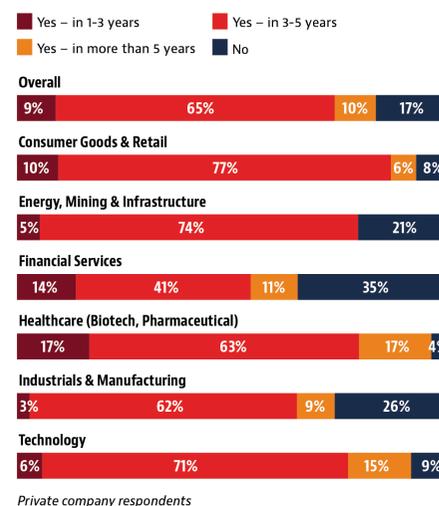
A healthy IPO pipeline

What's promising for 2019 is that there are mega-fundraisings in the pipeline and the list of unicorns planning to go public is long and includes global brands from Uber, Airbnb and Pinterest, to Peloton, Slack, WeWork and Ant Financial, Alibaba's digital payments arm.

Supporting this is the success of most IPOs so far this year, including the \$623m New York Stock Exchange listing of denim clothing company, Levi Strauss & Co. Importantly, the larger \$2.4bn IPO on Nasdaq of ride sharing company, Lyft Inc., shows the depth of investor demand for technology unicorns.

Looking out longer, the pipeline of potential transactions looks to be pretty strong too. Some 83% of executives we surveyed from 200 private companies across industries globally, said they are considering a listing, with most of them stating in the next three to five years.

On the supply side then, there is reason to be optimistic about the future.



Is your company considering an IPO (partially or fully) in the future?

What's interesting are some of the underlying factors and new developments that are impacting the IPO market, and what this means for how it evolves.

The magnitude of private capital available and being invested in companies is one such factor, ultimately enabling companies to grow larger and stay private for longer before they go public. At the same time, the tentative emergence of so-called direct listings [see *Direct Listings: The Next Big Thing?*] has at least raised questions about the extent to which this alternative to traditional IPOs can grow. By region and industry sector, there are some interesting trends developing too.

83%
of 200 private companies
considering an IPO

Larger, older companies raising more

For Doug Adams, Co-Head of US Equity Capital Markets at Citi, there's no question that there has been a significant increase in the capital companies have raised in private markets, particularly technology companies. Uber, for example, raised nearly \$13bn privately from venture capital and private equity firms, sovereign wealth funds and corporations between 2010 and 2016.

However at the lower end of the scale, Adams says that the individual private fundraisings for start-ups or high-growth companies has on average more than doubled to \$50-\$75m today from what it was a few years ago, reflecting what he calls the 'SoftBank effect'.

Japan's SoftBank Group Corp, a holding company mainly engaged in telecoms, technology and internet related businesses, has risen to become one of the biggest investors in high-growth companies. This includes investing in Uber, primarily through

Smaller public companies typically experience greater market volatility, so by staying private longer companies are mitigating this risk.

Doug Adams - Co-Head of US Equity Capital Markets at Citi

its \$100bn Vision Fund, which was formed in 2016 with backing from Saudi Arabia and Abu Dhabi's sovereign wealth funds.

Adams argues the depth and availability of private capital has had two main knock-on impacts – companies are in general waiting longer and becoming larger by market capitalisation before they go public. He estimates that the average market-cap of companies has grown to between \$750m-\$1bn from about \$450m-\$500m a few years ago, and says that this increased size matters. "Smaller public companies typically

experience greater market volatility, so by staying private longer companies are mitigating this risk," explains Adams.

IPO size on the rise

Importantly, staying private for longer also allows a company's management to focus on growing the company in the way they want to grow.

"Some unicorns have very ambitious growth plans which staying private longer can help them achieve," says Jackie Lo, Partner at Baker McKenzie. "Before going public, some of these companies constantly re-invested to grow, which they would not have been able to do to the same extent under the scrutiny of public markets."

Leverage is an important issue in the public-private market debate as well, says Samuel Losada Borrajo, Head of Equity Capital Markets for Europe, Middle East and Africa at Bank of America Merrill Lynch. "If a company remains private, it can run higher leverage, and therefore if it is growing, the returns for

investors are magnified," he says. "When they come to the public markets, however, they typically need to bring that leverage down, which is another reason why shareholders may decide to keep a company private for longer."

Global data on the average length of time companies wait and how much private capital they raise before going public is hard to come by. But recent analysis by US law firm Wilmer-Hale on the US IPO market is instructive. For instance, their analysis shows that between 1996 and 2017, the amount of time more than doubled from three to seven years, while the amount of capital raised prior to an IPO has risen from \$10m to \$100m.

Interestingly, one of the net effects of this seems to be how much capital companies ultimately raise when they float. Indeed, according to global IPO data from Refinitiv, a data provider, the average size of an IPO has increased from \$89m between 1996 and 2005, to \$166m between 2006 and 2018. In

the US market specifically, the average size of an IPO has increased from \$125m to \$257m over the same 20-year period.

There are multiple factors that determine the size of a company's IPO. And certainly the growth in the number of mega-IPOs (\$1 billion and over) in at least the last five years, has impacted this long term average. But, deal size does appear to be rising in step with rising levels of private capital investment.

Some unicorns have very ambitious growth plans which staying private longer can help them achieve.

**Jackie Lo -
Partner at Baker McKenzie**

Tech sector blazing a trail

If staying private for longer and growing larger before listing is one trend impacting the IPO market, what other trends have emerged or are emerging?

From a sector perspective, the main growth story has been the extent of IPO activity from technology companies. Last year, for instance, the technology sector was not only one of the most prolific by the number of IPOs but one of the leaders by total value of capital raised.

Indeed some of the largest listings last year came from Chinese technology companies, including the IPOs of smartphone maker Xiaomi, Foxconn Industrial Internet, food delivery platform Meituan Dianping, and video and music streaming companies iQIYI Inc. and Tencent Music Entertainment Group.

Such high levels of activity are expected to continue, not least because of the bulging pipeline of tech unicorn IPOs to come. But the tech sector is not expected to dominate. Last year there were three other key sectors – industrials, healthcare, and financial services – that mainly helped drive the number of IPOs and total capital raised to over \$200bn, and these industries will likely continue to support the pipeline of new

issuance in the future. This is supported by our survey. Just over 90% of executives from private technology and healthcare companies we surveyed - the highest across sectors - said they are considering an IPO for their company in the future, and most of them in the next three to five years.

Where companies list

This provides some visibility on which sectors IPOs in the main are likely to come from. Just as important though, is where, or on which exchanges, companies plan to list. What factors, for instance, determine where a European, US or Asian healthcare, fintech or manufacturing company lists where it does, and are those factors changing?

For Clive de Larrabeiti, a Director and Corporate Finance Adviser at Pineapple Power Corporation [See Case Study], a special purpose acquisition company focused on acquiring renewable or clean energy companies to help develop power generation projects in developing economies, there was one location in particular that stood out for

its planned listing. "Smaller exchanges have sprung up with cheaper listings and more relaxed regulatory environments but London has the reputation," he says. "It's expensive but it's worth it, for the concentration of capital, transparency and regulatory reputation. It's where you go if you want international investors to take you seriously."

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**Clive de Larrabeiti -
Director and Corporate Finance
Adviser, Pineapple Power
Corporation**

Our survey shows that valuation and liquidity together with the strength of the local regulatory regime, extent of analyst coverage and size of investor base are among the top factors determining on which exchange companies choose to go public.

And for private companies specifically, the share price performance of their peer group matters too. By sector, only executives from financial services, industrials and technology companies said that the cost of establishing and maintaining a listing is a top three most important factor when choosing which exchange to list on.

To be sure, the costs of listing, the sector-focus of the exchange as well as the efficiency or speed of the process are all important. And so is listing in a country that is in or close to a company's biggest growth market.

"Companies think about what exchange will get them the best valuation on day one but also which will give them investor interest from day two and beyond – so for many companies that will mean their local market or a market aligned with their business strategy," says Ivy Wong, Partner at Baker McKenzie. "For example, if a company's growth story is around China, listing in Hong Kong makes sense.

Or you see specialisation of exchanges – Australia and Toronto for mining, Hong Kong for branded consumer goods and those focussing on China."

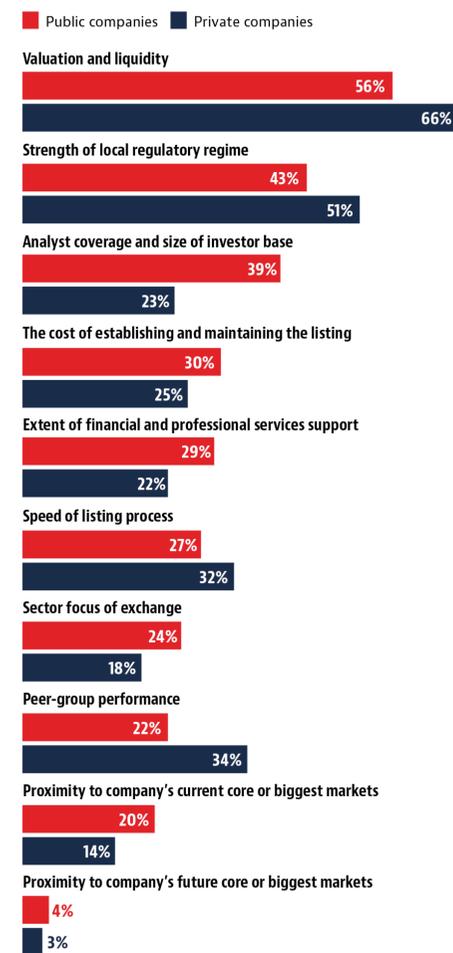
It is partly for these reasons – companies seeking a listing in a foreign country that represents a core growth market for their business, or an exchange in a foreign country that specialises in listings from their industry – that cross-border IPOs are flourishing. Also important for companies is being able to access deeper pools of international capital, and listing in a country where there may be fewer regulatory restrictions than in their domestic market.

Indeed last year over \$60 billion was raised by companies through cross border IPOs – the highest total value since 2014. Leading the way are New York (Nasdaq and the New York Stock Exchange), Hong Kong and London, which continue to be the most favoured destinations for companies seeking a foreign listing.

Partly driving this are new listing regimes in Hong Kong, for example, which make it easier for technology companies in particular to list.

Also important is the continued growth in Chinese-domiciled companies listing in the US, a trend which has been accelerating since 2014 when Alibaba raised \$25bn – the world's largest IPO – through its listing on the NYSE.

But perhaps the growth story over the past five years, which, in turn, has profound implications for the future of the global IPO market, is the growth of IPOs on exchanges in Asia-Pacific.



Most important factors when choosing a stock exchange to list on

Challenging New York and London

Just over \$80bn from 815 deals was raised by companies in Asia-Pacific last year – about double the total value of capital raised via IPOs in the Americas and Europe – extending a trend in the region’s global leadership in number of deals and total proceeds since 2014, according to Refinitiv.

Neil Mitchell, Head of Equity Capital Markets for EMEA at Credit Suisse, anticipates higher volumes in Asia-Pacific and the Americas to persist relative to Europe, largely because of the far stronger economic growth fundamentals in those regions.

The outlook for the European IPO market over the next couple of years does look challenging, but there is cautious optimism in the short term.

“2018 was a challenging year for the IPO market, essentially due to subdued market sentiment and market uncertainty, which kept investors away,” says Alain Baetens,

Head of Large-Cap Listings at Euronext. “A large number of intended IPOs – 64 across the EU – had been cancelled or delayed, which is five times more than the year before.

Markets globally are still in a waiting mode for structural good news, but we see a number of IPOs emerging, especially among SMEs. In fact, the pipeline across all markets and regions we cover is building up, and once investors do gain back risk appetite for equities, we should see good dynamics on IPO transactions. The only question is when.”

Asian exchanges were also impacted by pulled IPOs but not to the same extent. In fact, the new issue activity on the Hong Kong Stock Exchange last year was stellar, enabling it to regain the top position globally from the NYSE as the number one exchange by number and value of IPOs.

Koen Vanhaerents, Head of Global Capital Markets at Baker McKenzie, says that the phenomenal growth of the IPO market in

Asia-Pacific will likely continue, and predicts that the Hong Kong, Singapore, Shanghai and Shenzhen exchanges will together develop to become key competitors to London and New York within the next 10 years.

\$80bn

total capital raised via IPOs by companies in Asia-Pacific

Direct Listings

The next big thing?



The listing of Swedish audio streaming platform, Spotify, last year represented a novel approach by a large company accessing public equity markets for the first time.

The direct listing – an IPO alternative to going public without the traditional marketing and underwriting support of investment banks – on the New York Stock Exchange, valuing Spotify at close to \$30bn, is believed to be the first of its kind by a large company.

To be sure there have been a few direct listings in the US and particularly on Nasdaq before, but mostly by small-cap companies from the biotech and life sciences sectors. Direct listings by large-cap companies from other industries are extremely rare.

However, with US technology unicorn Slack planning its own direct listing later this year, capital markets practitioners are now asking whether a trend is emerging.

Interestingly, the public and private company executives we surveyed seem to think so –

almost two-thirds (65%) of them said they expect to see a higher volume of direct listings in the future, with European executives most bullish on growth.

This could of course mean anything from one, two or up to 20. But irrespective of the volume, it is clear that company executives believe that appetite for direct listings is rising.

One of the main reasons why direct listings may be an attractive option to a company is the potential for lower costs, as fees paid to advisers are typically lower than for a traditional IPO.

That's because in a direct listing, a company's private shareholders directly sell some of their stakes to investors on the open market, which differs from a traditional IPO, where investment banks are essentially paid a fee

for lining up large institutional investors to purchase shares at a set price from the company and its early shareholders.

For Spotify, the company did use investment bank advisers – Goldman Sachs, Morgan Stanley and Allen & Co – and paid a fee to them for the advice and service it wanted from them. But Spotify probably saved a substantial amount that it would have otherwise paid to its advisers had it taken the traditional full package of underwriting and execution services.

Advantages such as these are no doubt interesting to companies planning to list, but there are a number of challenges and market risks.

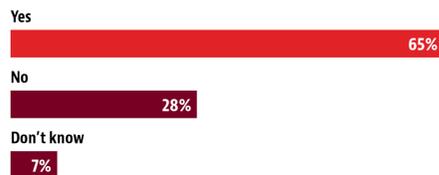
For instance, there are risks around the pricing of, trading in and performance of the shares. This is because the company is not drawing on the traditional support of long-hold institutional investors and investment banks armed with research to support and generate demand.

These challenges may be surmountable by well-known companies such as Spotify, but it's unclear how broad the appeal of direct listings is to companies, small to large, across industries. So far with Spotify and Slack, it at least looks as if any large companies that are choosing this listing route could be peculiar to the technology sector.

Indeed Craig Coben, Vice Chairman of Global Capital Markets at Bank of America Merrill Lynch, says expectations around growth in direct listings should be treated with caution.

It might work for well-known companies like Spotify, but it's not going to work for just anyone as it misses out on the fundamental work of introducing a company to market.

**Neil Mitchell -
Head of Equity Capital Markets
EMEA, Credit Suisse**



All respondents

In the future, do you expect to see a higher volume of direct listings?

He says that these listings are driven by a number of specific factors, such as liquidity, which can vary widely from one market to the next. "The US has the depth of liquidity especially for these high-growth stocks, which is not something we have in Europe."

Mitchell at Credit Suisse is just as cautious. "It might work for well-known companies like Spotify," he says. "But it's not going to work for just anyone, as it misses out on the fundamental work of introducing a company to market."

Christopher Bartoli, Head of NA Capital Markets at Baker McKenzie, is equally sceptical and recalls that companies have tried to buck the traditional IPO system before.

"15 years ago, Google did a reverse Dutch auction IPO instead of a traditional IPO and people thought that might become a trend, but it didn't," he says. "You may see some direct listings occasionally, but given the strength of the relationships investment banks have with companies while they are privately raising capital, we expect the traditional IPO process to be the primary mechanism for companies going public in the US for the foreseeable future."

Capital market practitioners may not be as optimistic about the rise of direct listings as the company executives we surveyed. But, even Coben notes that while there are no signs of them in Europe yet and he doesn't expect to see them emerge anytime soon, "you can't exclude anything" either, he says.

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**Christopher Bartoli -
Head of NA Capital Markets at
Baker McKenzie**

Impact Assessment

Risks and rewards of regulation and rule change.



There are myriad factors impacting the IPO market at a regional level, some of the most important include tax and regulation and changes around the listing process. The upshot is in large part positive but the impact can be negative too.

For instance in the US, Bartoli at Baker McKenzie, says while the US Administration's 2018 corporate tax cut was a financial boon for companies, it also at a stroke reduced the need to raise capital. He adds that over the longer term, IPO volumes in the US are lower historically compared to other jurisdictions partly because of the cost of complying with the regime for US public companies.

What's more, the arrival last year of the European Union's Mifid II [Markets in Financial Instruments Directive] – the most far-reaching reform of European equity capital markets in at least a decade – should make investing in and raising equity fairer, more efficient, transparent and competitive, but it could bring some negative consequences too.

One concern, for instance, is that as a result of Mifid II, the visibility of and market liquidity around small-cap companies could fall significantly, potentially making it less attractive for small companies to go public in the first place. This is because under Mifid, investment banks and brokers are essentially banned from providing stock or investment research to asset managers for free, a service which has supported the visibility of small-cap companies. This concern has not become a reality yet, but it has not gone away either.

Other key regulatory developments include the introduction of new provisions on the availability of information in the UK equity main market IPO process last year by the UK's financial regulator, the Financial Conduct Authority (FCA).

The changes are intended to improve the range, quality and timeliness of information made available to the market and, in particular, to restore the centrality of the registration document or prospectus in the overall process.

Such reforms are broadly seen as force for good, but there are concerns too that it might increase costs for companies, lead to delays in the IPO process and open it up to greater risk of confidentiality breach.

Public equity markets are still one of the most efficient ways of allocating capital in modern society. We need to optimise it without losing investor protections.

**Koen Vanhaerents -
Head of Global Capital Markets,
Baker McKenzie**

Rule change to better compete

As the regulatory framework evolves, exchanges are adapting to better compete too.

Indeed the Hong Kong Stock Exchange last year approved the biggest change to its IPO rules in two decades. Technology firms that have shares with different voting rights are now allowed to go public in Hong Kong, overturning rules that barred the likes of Chinese tech titan Alibaba from considering the exchange before. The step could be a landmark for Hong Kong's efforts to be the leading home for international Chinese listings and a trading hub that rivals the US.

When it comes to enhancing the IPO process, exchanges are, however, somewhat restricted in their reforms by regulation. "There is only so much the exchanges can do," explains Lo at Baker McKenzie.

"Look at Australia and the US, the Securities Acts in those countries drive the requirements so exchanges can't change the process too much. And when everyone can remember the global financial crisis, regulators won't win fans by relaxing regulation."

Efficiency versus investor protection is always the balance that regulators have to strike, says Adam Farlow, Head of EMEA Capital Markets at Baker McKenzie. Vanhaerents agrees, adding: "Public equity markets are still one of the most efficient ways of allocating capital in modern society. We need to optimise it without losing investor protections."

In truth, investors hold back change too. "The issue is that investor expectations are in tension with what companies want – investors want time to understand the deal while companies want speed," says Farlow.

"There is also the concern of litigation risk – capital markets bankers and lawyers want to keep their clients out of the dock, so they prioritise diligence. Eighteen months ago, a change was made so that 20%, rather than 10%, of capital can be raised without a prospectus but few companies are doing it."

Streamlining the IPO process is needed, and particularly in Europe.

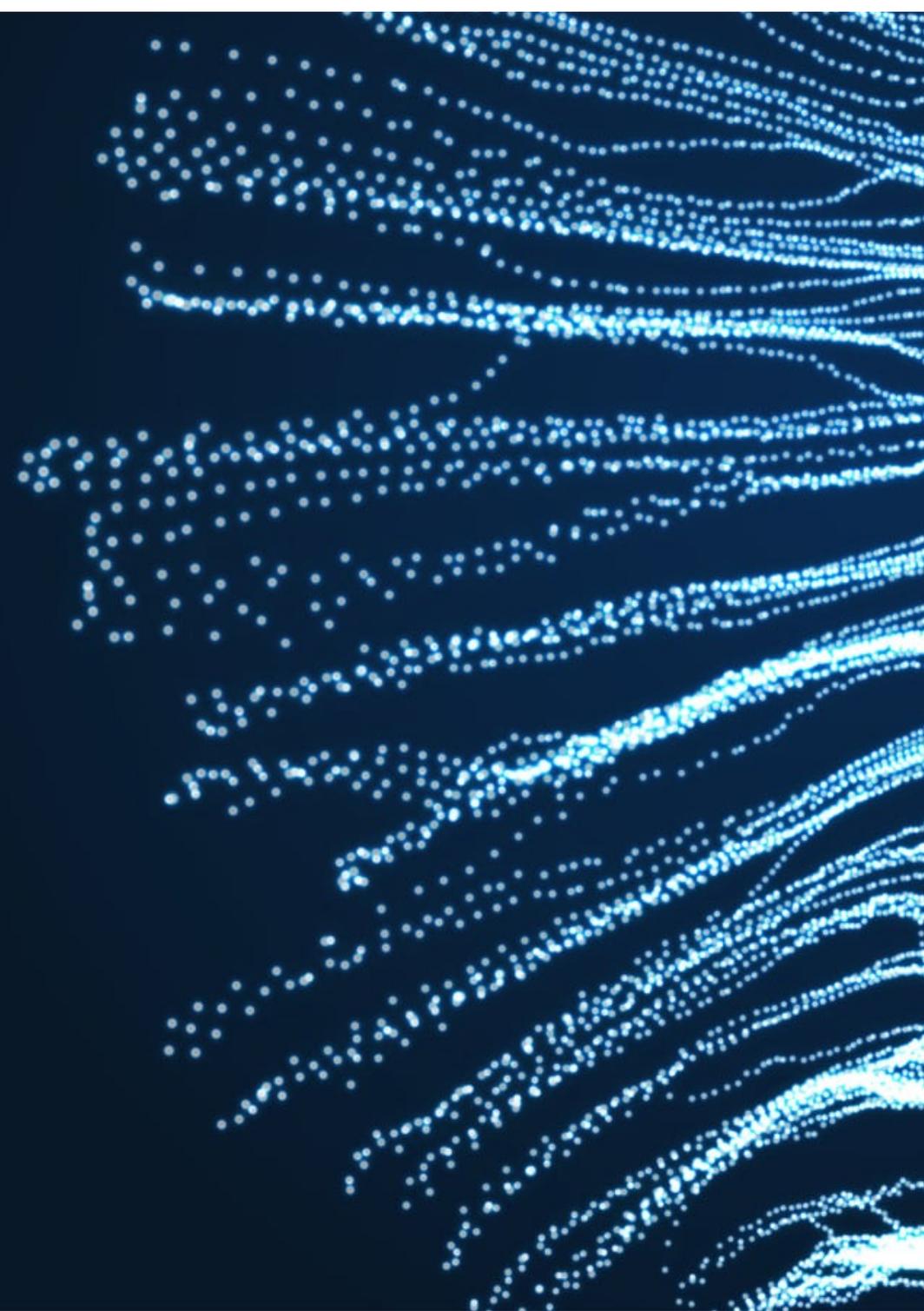
"We've been thinking a lot about the challenges and when we compare Europe with the US, where the process is more streamlined, there is a belief that the traditional IPO process here [in Europe] is due an update," says Mitchell at Credit Suisse. "We are hearing that from both sides – issuers and investors – and they are actively discussing it. Any changes should be beneficial for all, and could drive higher volumes and more successful IPOs – which will be good for issuers, financial sponsors and investors."

We've been thinking a lot about the challenges and when we compare Europe with the US, where the process is more streamlined, there is a belief that the traditional IPO process here [in Europe] is due an update.

**Neil Mitchell -
Head of Equity Capital Markets
EMEA, Credit Suisse**

Shifting Sands

The rise and fall of public and private markets.



Public equity capital markets have been around for more than 400 hundred years and their importance to companies, investors, economies and societies at large is unlikely to change in the next 50 years.

But look a little closer and there is some evidence to suggest that public equity markets are being squeezed on two sides, while at the same time private capital markets are growing from strength to strength. At the end of 2018, for instance, private market assets under management broke through \$5.5 trillion for the first time, according to data provider Preqin and research by the CFA Institute.

It's too simple to say private markets are in the ascendancy, to the detriment of public markets. However, Coben at Bank of America Merrill Lynch does believe that "we are beginning to see some form of shift between public and private markets."

The company executives we surveyed see this too. So what's going on? First, public equity capital markets are being squeezed on

the new issue side. For instance, while the annual value of IPOs globally has risen exponentially since records began in the early 1980s – peaking in 2007 when a record \$314 billion was raised – the number of IPOs each year since 1996 has not breached 2,000, which was achieved for the first time in 1993.

In fact, there were a record 3,000 IPOs globally in 1996 – the highest annual number on record – and since then the annual numbers have broadly halved.

Why this has happened is due to a number of different factors. Rising mergers and acquisitions activity – greater numbers of private companies simply being acquired by other companies or private equity firms – the historically low cost of debt financing and the robust growth of private markets have been important.

Considering M&A activity specifically, the numbers are striking. In 2016, for instance, some 5,000 private companies in the US were acquired – more than double the number 20 years ago, according to data from Dealogic analysis by EY, the global professional services firm.

Combined, such factors as the low cost of debt financing and the growth in private markets, have not only enabled companies to stay private for much longer before they go public, but enabled some to stay private.

Second, public equity markets are being squeezed on the other side – the number of listed companies and volume of outstanding shares. M&A activity together with de-listings have, for instance, continued to reduce the total number of listed companies in the US, Europe and UK over at least the last decade. At the same time, companies have been buying back a record value of shares, accelerating the phenomenon known as de-equitisation or the shrinking of investable equity.

In fact, last year was a record year for the total value of announced buybacks of US shares, breaking the \$1 trillion mark for the first time. And since 2011, global non-financial companies have bought back \$4 trillion of their own shares, according to research by Citi. The net effect is that public equity markets are slowly shrinking – not enough new shares are being issued to offset those being withdrawn from circulation.

We are beginning to see some form of shift between public and private markets. A key factor is the emergence of enormous pools of private capital commanded by sovereign wealth funds, family offices and others.

**Craig Coben -
Vice Chairman of Global Capital
Markets, Bank of America
Merrill Lynch**

A new public private partnership

Public equity markets are facing a number of challenges, while private markets have been growing to a record size. Several factors have helped, including “the emergence of enormous pools of private capital commanded by sovereign wealth funds, family offices and others,” according to Coben.

Indeed sovereign wealth funds may be relative newcomers to investing directly and indirectly in high-growth companies, but in recent years they have made a splash. The Saudi sovereign wealth fund’s \$3.6bn stake in Uber in 2016 and more recently its collaboration with SoftBank on the \$100bn Vision Fund – a tech-focused venture capital fund – is a powerful example of this.

Family offices – the investment arms of wealthy families – have also been increasing their direct investments in emerging companies. But that’s not all. So too have large global companies (Google Ventures,

Unilever Ventures) and institutional investors such as insurers and pension funds, intensifying the competition for venture capital firms and private equity funds which have been aggressively financing emerging companies for decades.

If there is one key reason behind this, it’s simply that these investors are hunting higher rates of return, thanks in large part to a decade of historically low interest rates and low levels of economic growth in the advanced economies of the world.

This raises the question of whether a shift is only cyclical or potentially structural and long term? Over half (53%) of the companies we surveyed believe it only temporary, although most Europe and Asia-based executives see the shift as the beginning of long term trend.

However, Coben at Bank of America Merrill Lynch says shifts like this can reverse pretty quickly. “And to be sure,” he says, “there is quite a lot of runway before the public

markets disappear. They have been around for over 400 years. And by the time we retire, there will be a pretty robust equity capital markets pipeline”.

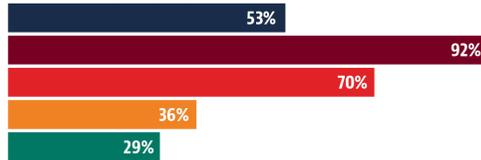
Mitchell at Credit Suisse agrees, and argues that while private equity investment in particular is partly responsible for helping contract public equity markets, it also feeds new issue supply. “Everyone is mindful of the massive amount of money private equity has at its disposal, so we’re expecting more public to private transactions,” he says. “But that is money looking for somewhere to invest – its market forces not a decision to ‘go private’. These companies often go public again. And in the new economy space we are seeing a lot of private market fundraising but some of those are now coming to market.”

Private and public markets will continue to evolve with the companies, and we see a potential amalgamation of public and private funding platforms. We need to create a seamless pathway between private and public fundraising channels.

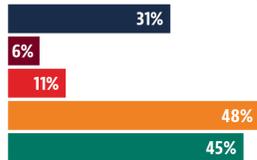
**Chew Sutat -
Executive Vice President, Head
of Equities and Fixed Income,
Singapore Exchange (SGX)**

■ Overall ■ North America ■ South America ■ Europe ■ Asia

Yes, but it is only temporary



Yes, we are at the beginning of a long-term trend



No, but this could happen in the future



No, I expect public markets to remain dominant



All respondents

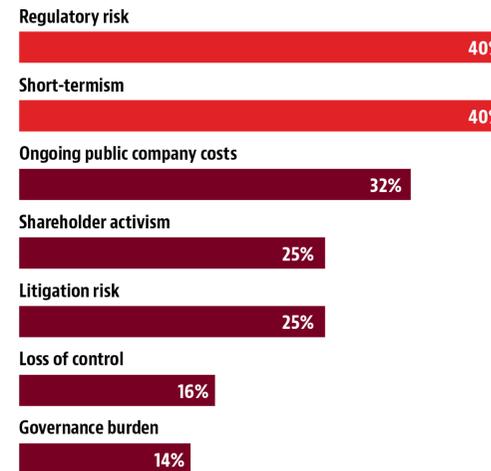
Do you believe a shift – specifically from public to private markets – is underway in where companies source equity capital?

For world stock exchanges, that is good news. But they are not being passive observers to what’s happening. “We recognise that the crux lies in companies having different capital raising needs at different stages of growth” says Chew Sutat, Executive Vice President, Head of Equities and Fixed Income at SGX, the Singapore Exchange. “We ensure that we are able to support and help improve access to capital by collaborating with like-minded private fund-raising platforms and stakeholders, by lending our infrastructure and network where appropriate, as well as exploring more ways to connect companies in nascent stages of growth with investors.”

Sutat adds: “Private and public markets will continue to evolve with the companies, and we see a potential amalgamation of public and private funding platforms. We need to create a seamless pathway between private and public fundraising channels.”

The burdens and benefits of being public

While there has been a sense of growing frustration among some public companies with the rules, regulations and scrutiny they operate under, the benefits of being listed for most far outweigh the challenges and burdens.



Public respondents

What is most challenging or burdensome about your company being publicly listed?

Top among those are short-termism, regulatory risk and the costs involved in being a publicly listed company, according to the public companies we surveyed. Interestingly, Asian companies see litigation risk and shareholder activism among the top challenges too.

When you talk to some companies, remaining private is a very appealing proposition. But the scrutiny of the public market is fundamentally good in the long term for the company and for investors.

**Samuel Losada Borrajo -
Head of Equity Capital Markets
EMEA, Bank of America Merrill
Lynch**

Many of these challenges, including intense shareholder and investor scrutiny of a company's financial performance, can cause frustration at board level. But these issues are rarely so problematic individually or collectively to force a company to delist and go private.

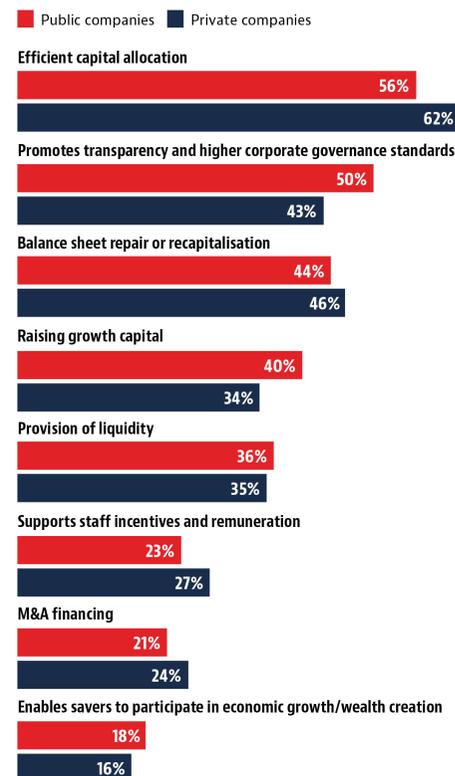
Indeed Mitchell at Credit Suisse says that while there are drawbacks to going public, there are also great incentives such as "greater organisational discipline, internal systems and accountability, free advertising and going public gives a seal of approval – those benefits won't change."

Coben at Bank of America Merrill Lynch agrees and says that it should not be underestimated how valuable being a public company is. "One of the key advantages of going public is that it gives the company that extra bit of credibility, which can be hugely important," he says.

What's more, Borrajo at Bank of America Merrill Lynch says that the scrutiny public companies are put under is ultimately a force for good.

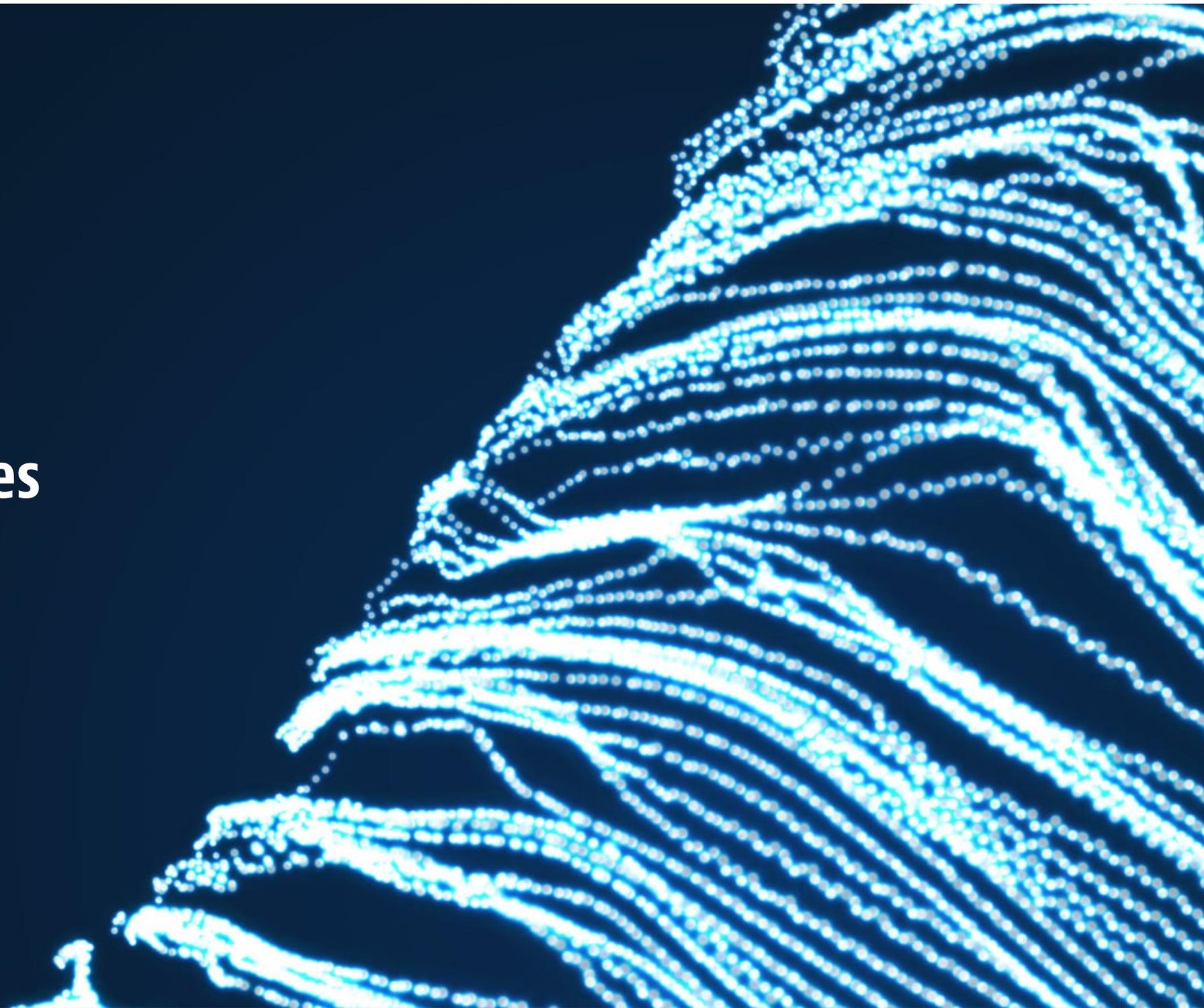
"When you talk to some companies, remaining private is a very appealing proposition. Part of that is due to there being less scrutiny, which means they can focus more on managing and growing the business in the way they want to," he says. "But the scrutiny of the public market is fundamentally good in the long term for the company and for investors."

This is an important point and one supported by the executives from public companies we surveyed. The promotion of transparency and higher corporate governance standards is seen as a top-three important benefit of public equity markets, along with it offering efficient capital allocation and the ability to repair balance sheets.



Most important benefits of public equity markets

Case Studies



Case Study: Euronext

Next Generation IPOs: The Evolving Role of The Stock Exchange

Capital markets practitioners are not alone in having to adapt to a changing marketplace.

Stock exchanges such as Euronext are also looking at how to help companies understand the benefits of public markets and guide them through the IPO process.

“We are confident our model is right for the future but we need to be vigilant to ensure we are providing what companies need,” says Alain Baetens, Head of Large-Cap Listings at Euronext.

“We are implementing programmes to attract new companies, such as TechShare, an educational pre-IPO programme for tech companies. This has been running for a few years and we are now seeing the first

conversion cycle with companies from the programme now proceeding to IPO.

We have a similar programme for family businesses called FamilyShare.” Techshare was launched in September 2015 and so far 300 companies from across Europe have participated, with four having launched IPOs, including France’s Balyo, a technology leader in autonomous robots, which listed in June 2017, raising €46m.

Over the course of the 10-month programme, participants attend two seminars with leading business schools, as well as monthly interactive workshops covering topics such as why list, different steps to listing, valuation strategy, and financial communications. Participants also receive training sessions from bankers, auditors, lawyers, and investor relations experts.

Future generations and future-tech

FamilyShare is slightly different as each programme is tailored for just one company. It addresses the difficulties encountered by family businesses and the requirements of executives, family shareholders, the next generation, directors and key employees, tailored to the sector and requirements of each business. So far, 20 companies have participated and one has come to market – France’s Cogelec, provider of telephone intercom and access control solutions, which listed in June 2018, raising €39m.

Beyond working with companies to prepare them to IPO, Euronext also is looking at its infrastructure to make it easier to invest in and process listed and non-listed European small and medium-sized companies. In 2017 Euronext and eight partners – AFS Group, BNP Paribas, CACEIS, Caisse des Dépôts,

Euroclear, Europlace, OFI Asset Manager and Société Générale – founded Liquidshare, a blockchain-based post-trade settlement infrastructure connecting to asset managers’, broker-dealers’ and custodians’ information systems. It is now in the pilot phase with 15 market participants.

“We are actively looking at everything happening in the blockchain world,” says Baetens. “We see regulators looking at this space closely because there needs to be a legal framework to even the playing field and give alternatives like this the credibility they need.”

Case Study: Pineapple Power

A Different Type of IPO: A Bright Future for SPAC Listings

Among the many trends in IPO activity in recent years, one that doesn't attract much attention but is quietly gathering momentum is in listings of entities known as special purpose acquisition companies or SPACs.

These companies are essentially cash shells set up to raise funds through an IPO to finance future acquisitions and investment.

At its simplest, the main aim of a SPAC's management team is to acquire assets, which typically happens within 24 months after listing, to generate good returns for their institutional investors.

Such as has been the popularity of SPACs in recent years, listings have soared.

Indeed 2017 was a record year for SPAC IPOs globally, with \$15.1bn of capital raised in total from 74 such transactions, while last year saw \$12.7bn raised from 67 deals – the second highest annual total by number and proceeds on record, according to data provider, Dealogic.

Most SPAC IPOs occur in the US but their appeal globally is growing.

Adding to the pipeline of SPAC IPOs in the future is Pineapple Power Corporation, a UK company, formed as a SPAC, that is focused on acquiring renewable or clean energy companies to help develop power generation projects in developing economies in the southern hemisphere, particularly in Africa.

The power of London

The company plans to list in London, and was created to help address a specific funding issue renewable energy projects in developing economies can be held back by, according to Clive de Larrabeiti, a Director and Corporate Finance Adviser.

"Looking at emerging markets, we saw a gap in funding of renewable energy – development finance institutions and investment banks are happy to fund the debt side, but the equity component can prove more difficult to access." he says. "The local exchanges are not liquid enough, and renewable energy can have trouble accessing start-up capital."

That's where Pineapple Power Corporation comes in, in effect providing the equity capital to renewable energy projects. "Once you have the listing, you have very different

conversations; it opens up the debt capital markets in a significant way," explains De Larrabeiti.

As to why the company is planning to list in London, the global financial centres' reputation was important along with the concentration of capital, transparency and strength of regulatory framework. "It's where you go if you want international investors to take you seriously," says De Larrabeiti, who adds that Brexit hasn't diminished the UK capital's attractiveness.

"London is the marketplace of the world – Brexit hasn't changed our view of it as a global capital market," says De Larrabeiti. "With its infrastructure, that dominance won't go away, even with greater competition from Paris, Frankfurt and other cities."

Conclusion

The evolution of the stock exchange and the role of technology.



What the IPO market globally will look like in three, five, 10 or 20 years is hard to predict, but there is some certainty in knowing it will surely be different from how it is today.

In each of the past five decades, the IPO market has evolved and will continue to so long as the financing and investment needs of private companies and institutional investors keep evolving.

What will be interesting to watch is how private capital continues to impact the IPO and public equity markets, more broadly. The rise of private markets has already caused a profound change – companies are older, larger and raising more capital at the time they float than ever before. In the years to come, companies may be even older and larger when they launch an IPO.

To be sure, the abundance of private capital has provided companies with greater financial flexibility than they had before. But there are no signs yet that companies in large numbers are choosing to stay private instead of going public.

“When you look at public markets, they are reasonably steady,” says Adams at Citi. “Last year just over \$200bn was raised via IPOs, which is in line with the 10-year average. So it would be unfair to say there’s been a decline.”

Indeed, there are particular growth stories shaping the future of the global IPO market, and Asia-Pacific’s emphatic new issue growth, as well as companies from the region helping push annual cross-border IPO issuance to new highs, are perhaps two of the most powerful.

Evolutionary exchange

Partly supporting these two growth trends are stock exchanges, which are showing greater flexibility and adapting their rules and listing processes. “There is a greater willingness to tolerate flexible approaches like dual-class shares,” says Ashok Lalwani,

Partner at Baker McKenzie. “Singapore and now Hong Kong have relaxed their requirements for track records of profitability for early stage companies, particularly in the tech and life sciences sectors.”

The Hong Kong Stock Exchange also lifted restrictions on secondary listings by mainland Chinese companies so that those that went public in the US can “come home” to Hong Kong.

That’s not all. Asian, US and European exchanges are collaborating globally to strengthen their offerings. “Shanghai is upping its game with the London-Shanghai Stock Connect,” says Richard Taylor, head of corporate finance and capital markets at CLSA, the Asia-focused investment banking and investment group. “It allows Shanghai-listed companies to raise funds in the UK stock market while British companies can broaden their investor base by selling shares in Shanghai.”

■ Agree ■ Disagree

Compared to the past, companies today are waiting longer to go public



Companies today can raise all the capital they need to grow without going public



Increasingly companies do not choose to list because they need capital; they choose to list because their owners want a liquid market to exit their investment



All respondents

To what extent do you agree or disagree with the following statements:

When you look at public markets, they are reasonably steady. Last year just over \$200bn was raised via IPOs, which is in line with the 10-year average. So it would be unfair to say there’s been a decline.

**Doug Adams -
Co-Head of US Equity Capital
Markets, Citi**

In time, the hope is that through the standardisation of listing requirements and, potentially, the adoption of a 'universal passporting' approach, companies could target investors in multiple global jurisdictions, using offer documents approved by their national regulator.

Technology's role

Regulatory change will be important in enabling companies with greater access to global capital pools. But just as important in this is the technology infrastructure supporting it. "With technology, exchanges like ourselves can link and build liquidity pools across multiple venues and trading protocols, enhance transparency and price discovery, and develop a broader universe of global participants," says SGX's Sutat.

The advance of technology will surely also help transform the IPO process too. Investment banks' ability to make the best use of new technologies could help re-shape and enhance established processes, benefiting issuers and investors.

For instance, advanced data analytics can be used to draw insights from unstructured data sources prior to an IPO, which could include sentiment analysis of social media to help understand how a potential transaction is being perceived, ahead of time and in real-time. Virtual reality could also enable broader investor access during the marketing of the IPO.

For now, however, investment banks are learning to walk before they can run.

Citi for instance is looking at how it can implement technology more in the capital raising process and the way in which its business is executed. "We're already using it [digital technology] to bring transparency to the book build process and share orders among firms," says Adams. "The private market doesn't currently provide the transparency or liquidity that many investors ultimately require — at some point many will likely need the exit provided by an IPO."

2019 and beyond

This point is important. There are a number of reasons why companies choose to list. Being able to raise capital efficiently to finance growth has been one of the most important. That is as true today, as it should be tomorrow.

But there are signs that some companies are not choosing the IPO route to raise growth capital. Indeed some 44% of the company executives we surveyed agreed that increasingly companies do not choose to just list because they need capital – they list because their owners want a liquid market to exit their investment.

Spotify's listing last year is a good example – the company raised no fresh additional capital through the transaction.

In an article he wrote last year, Barry McCarthy, Spotify's Chief Financial Officer, explained it thus: "We deliberately developed our company in a way that enabled us to go public without raising

additional money."

He added: "There is no reason that going public has to be part of a company's decision about how to finance its growth... Companies have more flexibility than they may realise when it comes to raising capital. And the same is true when it comes to going public."

With technology, exchanges like ourselves can link and build liquidity pools across multiple venues and trading protocols, enhance transparency and price discovery, and develop a broader universe of global participants.

**Chew Sutat -
Executive Vice President, Head
of Equities and Fixed Income,
Singapore Exchange (SGX)**

To be sure, Spotify's direct listing and reasons for going public are so far the exception rather than the norm. But it does highlight a broader truth that companies are not only choosing to finance themselves differently to the way they have in the past, they also have greater flexibility in how and where they raise capital and the way in which they list.

How this will play out over the coming years is difficult to read. The IPO pipeline across industries and regions looks healthy, and for most entrepreneurs, the allure of taking their company public will likely remain as strong in the next three, five or 10 years as it is today.

What is changing are the regulations, rules, processes and technology around the traditional company IPO, and the extent to which companies are drawing on private markets before they go public.

About the research

The Future of Equity Capital Raising: How Private Capital is Reshaping Public Markets was commissioned by Baker McKenzie and researched and produced by Thought Leadership Consulting (TLC), the thematic research division of Euromoney Institutional Investor PLC.

During the period of December 5 to December 20, 2018, TLC surveyed 353 senior executives from across management roles, private and public companies, industry sectors and geographies. Most of the respondents were Chief Financial Officers (23%), Chief Investment Officers (18%) and Finance Directors (16%). Other respondents composed Heads of Investor Relations (15%), General Counsel (11%), and Treasurers (10%).

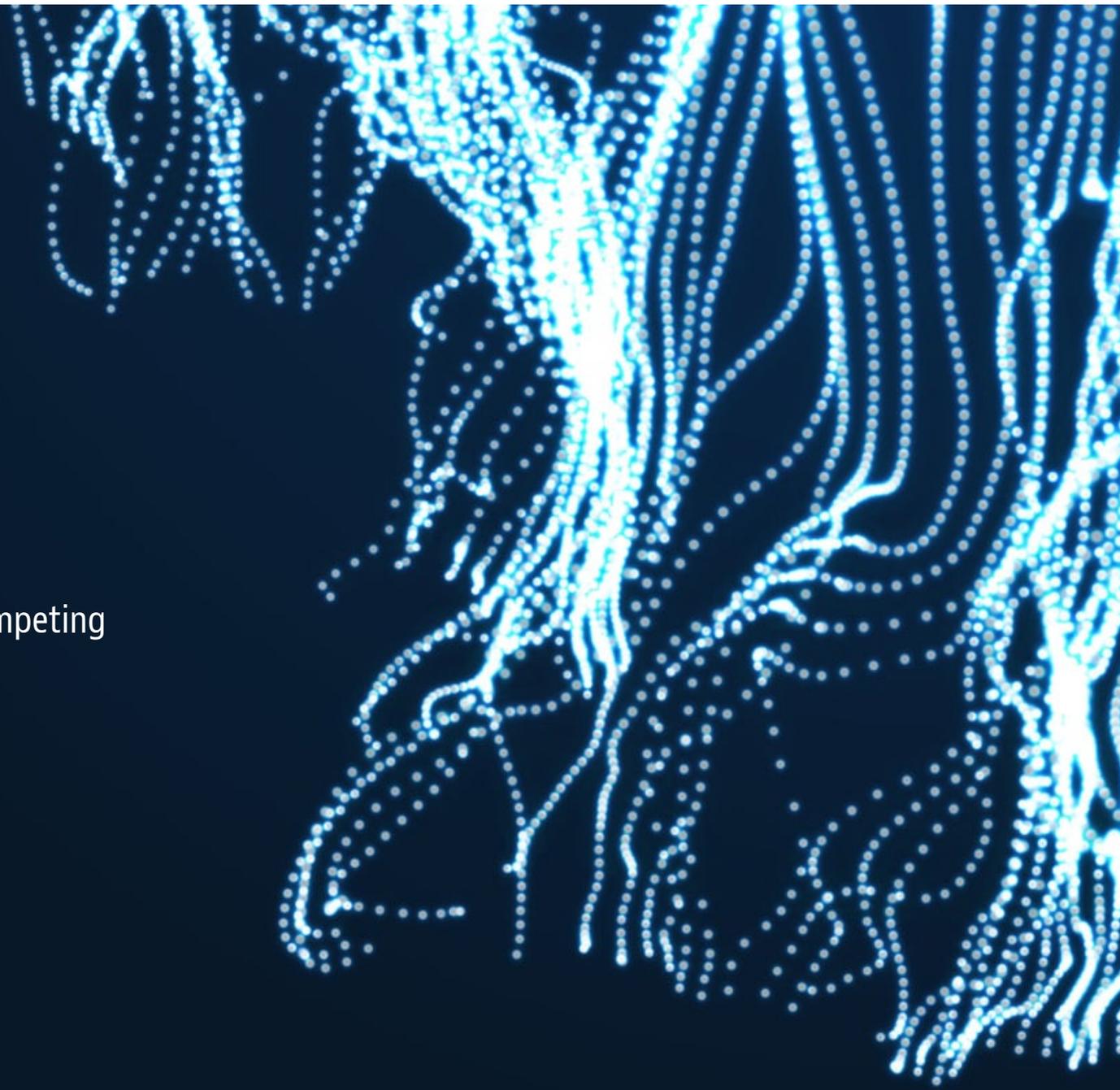
In total, 200 (57%) executives from private companies and 153 (46%) executives from public companies participated in the survey. Companies participating in the survey came from six industry sectors: consumer goods and retail (21%); financial services (18%); Technology (18%); Industrials and manufacturing (17%); Healthcare (14%); Energy, mining and infrastructure (13%).

By region, most executives worked for companies headquartered in Asia (30%) and Europe (30%), followed by North America (25%) and Latin America (15%). In addition, in-depth interviews with 12 capital markets experts were conducted throughout January, February and March, 2019.

[**DOWNLOAD APPENDIX**](#)

Key Contacts

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in the global economy



Key Contacts



Koen Vanhaerents

Head of Global Capital Markets

[Email](#)



Christopher Bartoli

Head of NA Capital Markets

[Email](#)



Ivy Wong

Partner

[Email](#)



Ashok Lalwani

Partner

[Email](#)



Adam Farlow

Head of EMEA Capital Markets

[Email](#)



Pablo Berckholtz

Head of Latin America Capital Markets

[Email](#)



Jackie Lo

Partner

[Email](#)

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