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REPORT

GO PUBLIC? A GUIDE FOR BOLD COMPANIES

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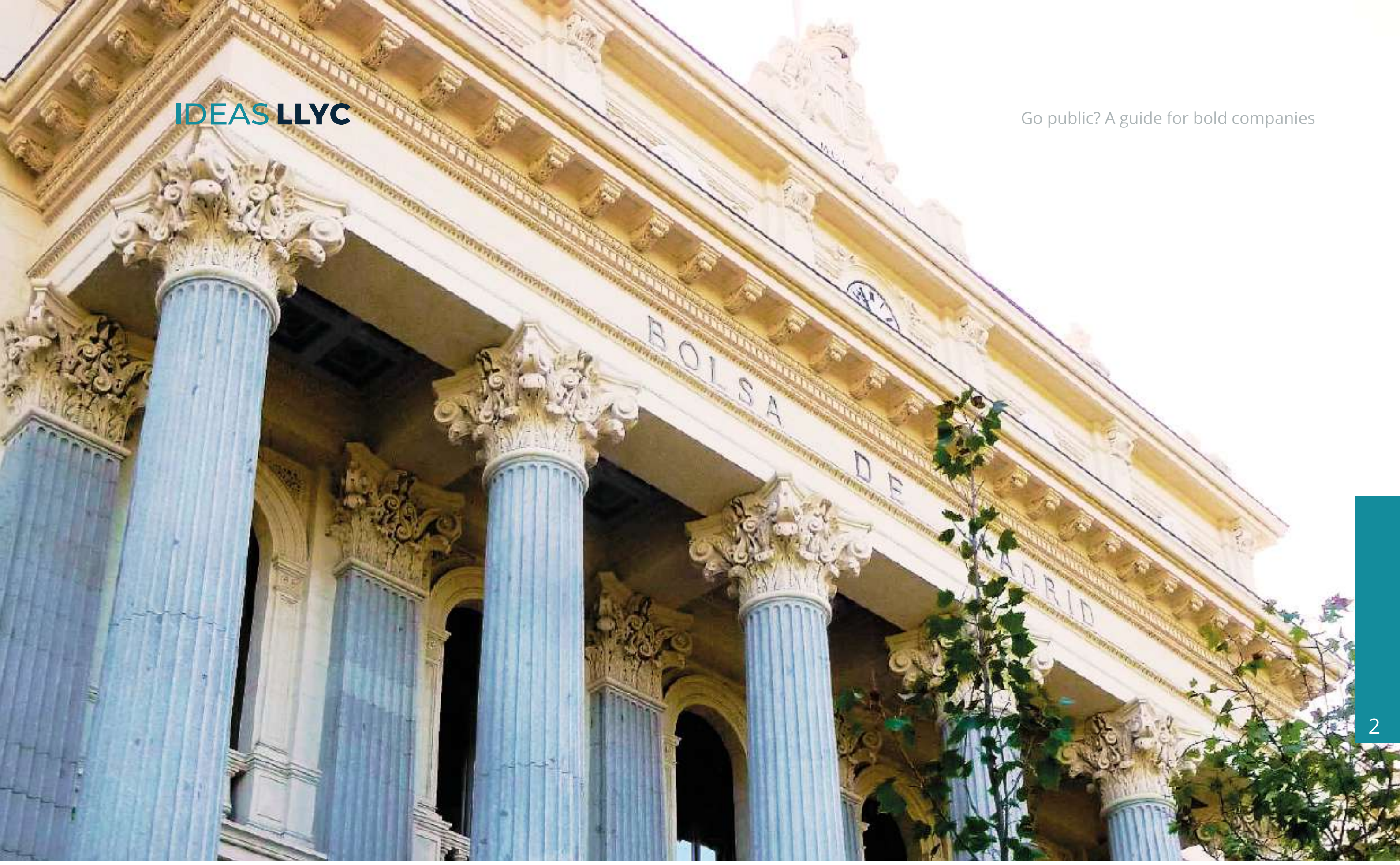
LLORENTE Y CUENCA



INTRODUCTION

Drought. This is the word that best defines 2019 in terms of stock market listings. In the year just ended, **no company managed to make its debut on the Spanish capital market,** at least as regards the Continuous Market. The only exceptions to the general lull were Holaluz on the Alternative Stock Market (MAB) and Grenergy Renovables migrating from the MAB to the Continuous Market.

This scenario leaves the **meagre balance of 44 million euros** obtained by the electricity distributor as the total amount placed among investors, according to data from Bloomberg (which does not include capital increases or listings). To find a similar situation, **we must look back to 2013,** when the total amount was zero and the only two transactions that took place that year did not bring in any new money to the debutant companies.

It seems clear, therefore, that the existing political and economic uncertainty has infected the capital markets, to the extent that stock market flotations have become a rare occurrence, taking us back to times not been seen since the height of the financial crisis. The situation in the rest of Europe was not much better. The amount taken up by the market fell more than 25 % in Europe last year, from over 28 billion euros in 2018 to 21.6 billion, again according to Bloomberg data. If we look at global indicators, the Global IPO Trends 4Q 2019 study, prepared by EY, reveals that a total of 1,115 IPOs for 198 billion dollars were registered last year, which represents a year-on-year fall of 19 % and 4 % respectively. Without the major IPOs of Saudi Aramco, Uber, Alibaba Group Holding and Postal Savings Bank of China, the fall would have been much deeper.

The question now is whether the reticence regarding IPOs is temporary or will it also be with us in 2020. Right now, **the only confirmed launch is Línea Directa** but it will do so through a listing and therefore bypasses the need to sell the company to investors. We will have to see if other candidates the market has been talking about (Ibercaja, Wizink, Mediapro, Europastry, Soltec, Vips ...) decide to take the plunge. Of course, if they finally do, in recent months lessons have been learnt that they should take into account if they want a successful operations.

1. MAIN TRENDS IN THE CAPITAL MARKETS

The alternative market as a preliminary step

On March 30, 2012 the then little known Ibercom debuted on the MAB with a capitalization of 763.7 million euros. After its merger with Más Móvil Telecom 3.0 in 2014, and just over seven years since its stock market debut, the resulting company, having gone to the Continuous Market and now named Masmóvil, joined the Ibex 35 with a market value of more than 2.5 billion euros. This progress, culminating last October, is already seen by some companies as a model to be replicated, to the detriment of less manageable alternatives such as the result of facing a Public Offer for Sale (OFSale) or Subscription Offer (OFSubscription) directly on the Continuous Market.

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Operations seen in Spain last year followed Másmóvil's example. Grenergy Renovables, a company focused on building and running photovoltaic plants, last December moved to the Continuous Market after four years trading on the Alternative Market. During this time it succeeded in multiplying its value by 13, going from a capitalization of 31 million euros to one of almost 400 million. Holaluz, recently incorporated into the MAB, intends to follow the same model and even speeding the process as the green energy distributor plans to take the plunge this year.

It seems that opting for a stage-by-stage process in the capital markets is a growing trend, something that was also at the origin of MAB itself, although, so far, only Másmóvil and Grenergy have actually taken this step. For the moment, it is only working for companies with a certain profile. This is the case of the three companies mentioned above. They are all young organisations with an incipient and relatively disruptive business models for their sectors and ambitious expansion projects. Faced with this situation, their management teams seek to **finance growth, but without losing control, in the hope that a subsequent opportunity will allow them to maximise company value.** By that time, they expect their structures to be ready to assume the greater obligations of transparency and good corporate governance required by being listed on the Continuous Market. This year may be when some MAB companies decide to make the leap to the Continuous Market, although it is important that they make good use of their time on that learning platform and plan their move in detail to a more demanding market, also in terms of information (from presenting half-yearly reports to quarterly ones, for example).

Dual track as a tool for maximizing valuations

Low interest rates have put the cost of funds at an all-time low. This has made financing in the debt markets more affordable than ever and has generated a **flood of liquidity** to venture capital firms voraciously seeking **investment opportunities.** This, together with the high volatility of the international financial markets and lock-up clauses agreed (in the case of an IPO) by shareholders planning to sell and global coordinating banks, has favoured the **rise of dual track operations** (initiating a parallel and simultaneous process of going public and selling privately), which maximises the sale price obtained by a company's shareholders.

However, it is true that the **most recent processes have almost always ended in a private sale.** At a time of excess liquidity as now, and with a mature economic cycle that is close to changing direction, institutional funds are under **increasing pressure to broaden their portfolios.** As a result, they end up assuming higher valuations than can be achieved through block placements in an increasingly volatile capital market.

This method is being **widely used by companies where there is a clear controlling shareholder.** who can use a bilateral negotiation to place significant packages or reach agreements with immediate effect on managing the company to its advantage. A recent and very significant example was the cancellation of Cepsa's IPO after Carlyle's acquisition of 37 % of the company from Mubadala Investment Company, the Abu Dhabi sovereign wealth fund that controlled 100 % of the company.

Listing, an emerging trend as an alternative to IPOs

Listing is one of the ways companies go public, such as OFS or OPS. The main difference is that **in a listing the company goes public without any shares changing hands** until the company is already trading.

In a listing all investors, (of any kind), who want to buy shares of that company have to wait until it begins trading to buy them in the market in the same way they would buy shares of any other traded company. Unlike OFSale/OFSubscription operations, **there are no lock-up clauses, and the owners of listed shares can sell their shares immediately** after they begin trading, and the process to get listed can be shorter (bureaucratic) and less expensive. However, not in all cases, of course, listing can also be a good alternative to going public.

All **depends on the goal** that each company has for trading on the capital market (obtaining funds, greater fragmentation of the shareholder base, improving corporate image, providing liquidity for previous shareholders...). If the company, for example, has just finished a round of fundraising, does not need additional capital and is generating cash flow, then a **direct listing may be the most appropriate option.**

Although in Spain there have been few cases of direct listing in recent years (Amrest, Berkeley Energy, Grenergy in the transition from MAB to Continuous), there is a tendency in other more mature markets for some companies (Spotify, Slack...), **often the so-called "Unicorns"** (originally, B2C technology companies that achieve a one billion dollar valuation in one of the stages of their capital raising process), **choose this alternative to start trading in the secondary market,** since they do not seek to obtain new funds as a priority objective, such as Spotify or Slack. Even though they not only choose the listing option, Uber and Lyft, for example, taking the OFS route, attracting 8.1 and 2.3 billion dollars respectively.

Ever tighter windows of opportunity

The "natural" windows of opportunity are those **periods that are ideal for an IPO.** These windows have traditionally been between Easter, the summer months and Christmas. That is, those weeks outside periods where trading volume tended to be significantly reduced and which, therefore, made a sale difficult. In that scheme of things, **the norm was to target three opportunities** a year: February-March, May-June and September-November.

Subsequently, this theoretical recommendation **has had to adapt to other external factors** (political crises, regulatory shifts, key decisions by institutions or trends in macroeconomic data). Investment banks considered that these factors could impact on the markets and, consequently, make it harder to attract investors. As a result, time frames considered suitable for carrying out each OFSale or OPSubscription were further reduced.

As if this were not enough, we are now witnessing a new turn of the screw, with the VUCA environment in which organizations and society in general now have to operate. This is particularly relevant in the case of IPOs, with the instability of the current economic environment as well as the existing political uncertainty shortening the windows even further. **In 2018 the pre-summer window disappeared** and operations were only recorded in the early part of the year (Metrovacesa in February) and in the period before Christmas (Solarpack in December). According to leading analysts, windows were **compressed again in 2019** due to trade tensions between the United States and China, doubts about the Eurozone economy and the pending challenge of Brexit. This meant that the only opportunities came **at the year end,** with the debut of Holaluz (late November) and Grenergy Renovables trading on the Continuous Market (early December).

As a result of the narrowing windows of opportunity, and the new VUCA context, Dealogic data show a total of **217 IPOs were cancelled** globally in 2019, **34 more than in 2018** (in Europe 21 have been cancelled). These figures represent **a return to the levels of 2012, when the global economy was just beginning to wake up from the financial crisis** while in the Eurozone the debt market crisis continued to wreak havoc.

This new context means that **debutants will have to be very strict in complying with the legal calendar if they want to exploit their chosen window of opportunity.** It is very important that they have the necessary flexibility to adapt to **potential future events** that may force them to change their plans. They must **properly manage the market's expectations for each potential event.**

"In 2019, only 44 million euros were placed among investors, the lowest figure since 2013, when the two operations that took place did not lead to the entry of new money in debutants."

Excessive media attention and increasing influence

The scarcity of IPO operations has **triggered media interest** among those adventurous few who announce their intention to trade their shares. Companies with a potential capitalization of less than 50 million euros, such as the recent case of Holaluz, attract a lot of **attention, probably disproportionately.** This **can be positive in certain cases,** putting upward pressure on their valuation, but it can also generate tension through **demands for greater transparency,** a situation for which not all companies are prepared.

In fact, this pressure is not only aimed at companies that have taken a firm decision, but **also affects all those that may have the intention** of taking the leap, even if they eventually change their mind or delay the decision. Rumours have been rampant about candidates being given a valuation range or specific changes to their management team. All this **before any official announcement is made.**

This voracity can often lead to **distorting market expectations,** with the consequent impact on the company that could ultimately affect the success of the operation.

Taking all these factors into account, communication should be considered an important element in defining an IPO strategy, regardless of the type of operation (OFSale, OFSubscription or listing).

2. KEYS TO MANAGING COMMUNICATION WELL AND SUPPORTING A SUCCESSFUL IPO IN THE CURRENT CONTEXT

Anticipate and create a favourable environment

Companies often start thinking about communication **just when they are going to make the public announcement** of their intentions or, worse, when they **receive a call from a journalist** who has found out about the company's plans. This means that when the news breaks, the market is unfamiliar with the company or, even if it already has a certain public profile, its previous story does not fit in with the new one. For this reason, **the weeks prior to the window of opportunity should be used to create a favourable environment** in order to facilitate the subsequent process. This is especially important if we consider that the opportunities for such operations are becoming increasingly narrow and exceptional.

Creating your own corporate narrative, defining the public profile of key executives, building a solid relationship with the media and generating balanced and accurate media coverage are tools to be activated as soon as possible. **Only a solid prior reputation base, capable of promoting market support, will bring success** in the face of potential moments of uncertainty or volatility.

"Communication should be considered an important element in defining an IPO strategy"

Encourage the media to be allies

OPS or OPS operations are legally regulated processes in which the information that must be conveyed to the market is at all times regulated. However, this does not mean that a fluid relationship with the media should be avoided.

Company history, the context of the sector and the technical and legal details of the process are some of the key issues, **knowledge of which provides value to journalists** who follow the company. **Proximity to the management team and equal treatment** are also factors that help to establish relationships and manage future crises (which will inevitably occur) within a context of high information intensity.

Turn the equity story into your main marketing tool

Based on solid financial information, the equity story must articulate a company history that justifies the differential value of its business model and conveys confidence in its future prospects. This content must also be accompanied by an **attractive and convincing** presentation. The use of audiovisual techniques, attractive graphic design or the development of disruptive formats are increasingly important elements in attracting attention.

Finally, it is important to note that the equity story should be **an asset to be exploited with investors, but also with regulators, media, institutions or any other key stakeholders** in an IPO process. Not only using clear language adapted to each of them, the discourse must also be consistent, well argued and credible. This is the only way to gain the market's confidence in processes that, if initiated with a previous MAB step, can take several months or even years.

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Prepare to manage leaks (and other risks)

Preparing for an IPO is an intense and demanding process for a private company unaccustomed to public scrutiny, one in which **sensitive information is shared with numerous stakeholders.** At certain times, milestones and next steps not yet disclosed (decision to list, prospectus, valuation range, cancellation or delay) are likely to be leaked and will need to be managed.

In this type of situation, the best solution is always to **prepare in advance.** Only **when you have already established a good relationship with the media** and/or opinion leaders, and have a defined action plan to manage each of these potential risks, will you be able to reduce the impact of the risks.

Prepare the ground for your future as a listed company: control the narrative, integrating or maximizing coordination of the IR and Communication functions.

Far from being the end of a process, **starting to trade shares is only the first step towards a much more complex stage.** From that moment on, investors and analysts, but also the rest of the company's stakeholders, will demand compliance with business plans (with firm ESG criteria) and the forecasts and commitments set by the company. A new phase begins in which **it will be key to establish a very fluid dialogue with the market,** both to convey the company's key messages as well as understand investor thinking and thereby identify and anticipate possible changes in their requirements.

In order to respond appropriately to all these requirements, it will be key to build an **investor relations area,** indispensable for strategic definition of the organization and necessarily coordinated with the communication area. In order to ensure a coherent story for all groups and stakeholders, it is essential that the company "controls the narrative". Much depends on ensuring that internal teams are integrated and well coordinated. When, in listed companies, the investor relations and communications teams work in silos, as is often the case, they present the company's narrative from different perspectives, ultimately confusing their audiences and diluting the story.

Managing a company's narrative begins with developing a single, integrated story and adopting internal processes that ensure both communications and investor relations teams communicate that story consistently. Therefore, far from being an administrative function, the Investor Relations area must **become an indispensable part of the value generation chain,** and serve as a link between the management team and the true owners of the company, its shareholders.

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Jorge López Zafra. Director of Corporate Finance. Jorge has over 20 years' experience in corporate communication. He is an expert in Strategic Planning, transactions (M&A), and capital markets and leads the LLYC Corporate Communication and Financial Department. He advises on communication strategies in a wide variety of mergers and acquisitions, IPO and secondary shares, restructuring, shareholder activism, litigation and national and international crisis situations. Before coming to LLYC he worked for Iberdrola for eight years, where he participated actively in strategy development and corporate communication project coordination (IPO, M&A, Integrations, JGA, other corporate business.) He has also held different positions in the company, as Director of Strategic Communication, Digital Communication, and Brand and Reputation Intelligence. He has previously held a leadership role at Llorente & Cuenca in advising on M&A transactions (such as acquisition offers of Gas Natural in Endese and Enel and Acciona in Endesa), flotations, and other corporate accounts.

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