

TRANSFORMATION PROCESSES OF THE IPO MARKET: UKRAINIAN AND WORLD EXPERIENCE

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Abstract. The study of IPO as a source of financial resources meets the current needs of the corporate sector in conditions of disintermediation and securitization trends of the financial market. In developed economies, there is a process of shifting the emphasis in the direction of capital attraction precisely on the stock market segment of the financial market, which has a number of advantages over the banking system that are also connected with the innovation and investment development of the national economy. The formation of the proper basis for the development of IPO market determines the timeliness of the consideration of this issue because it didn't obtain a sufficient spread. The emergence of new instruments is the feature that characterizes the modern stage of the development of the Ukrainian and world economy. Their application is a condition for the further development and use of the potential opportunities for the improvement of economic systems. Enterprises are able to meet current market needs and challenges due to orientation to modern trends and timely reaction to the latest achievements. One of them is the IPO (initial public offering), which is the primary public offering of shares. Participants of the Ukrainian market face a number of obstacles during IPO on the domestic and foreign stock exchanges. It necessitates a comprehensive review of this issue for a further developing of this method of accumulating financial resources. The *purpose* of this article is to identify the IPO market as a system of interrelated components that form its essence, and on the basis of a generalization of the constraining factors of development – providing recommendations on the perspective lines of improving the IPO market, taking into consideration the peculiarities of the Ukrainian and world stock market. *Methodology.* Analytical market reviews, materials of periodicals, resources of the Internet are the informational and methodological basis of the investigation. To achieve the goal set, the following general scientific and special methods were used: economic and mathematical methods, structural-logical analysis, analogy, synthesis, comparison and integration, factor analysis. *Results.* The factors that should be taken into account by the issuer for the success of the IPO procedure are justified. Problematic aspects and directions of their elimination are determined for every concrete stage of the IPO. The model for the domestic companies to enter the IPO market is proposed that has a special significance in the context of increasing the volume of financing innovative activity. Directions for reforming the regulatory and legislative framework are considered. *Practical implications.* Directions for improving the process of passing through the IPO stages can be applied by issuers, taking into account the peculiarities of the domestic and world stock market. *Value/originality.* The biggest part of the scientific works is devoted to the theoretical aspects of IPO, clarifying the essence of this process, structuring its participants, the advantages of carrying out. At the same time, a part of the works is devoted to the consideration of IPO as an instrument for attracting financial resources by corporations. The authors reviewed IPO in a system that combines the above aspects with its procedure stages and propositions to cancel out constraining factors that have a place on each step of IPO. The presented integrated approach will allow expanding the use of the IPO in the financial market as a source of financial resources for the corporative sector. It is also important to consider the impact of the planned

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legislative reforms on the development of the IPO market in Ukraine. Taking into account all the components of the IPO market and existing features of the IPO within the framework of the national financial market and world stock exchanges will highlight directions of the IPO market spread.

Key words: IPO, emission, securities, stock exchange, listing, innovation activity.

JEL Classification: G15, O16

1. Introduction

Innovative development of the corporative sector is based on the capital raising on the stock market in the developed economic systems. Realization of the IPO didn't have widespread use in the modern economic situation in Ukraine that causes an actuality of its basis formation.

Interest in the emission of shares as a source of capital raising is gradually growing after the crisis of 2013–2014, which differed in the absence of the IPO of Ukrainian issuers. The definition of ways how to eliminate the factors constraining the implementation of the IPO requires a detailed consideration.

Theoretical basis and practical aspects of IPO market development were reflected in the scientific works of V. Kublikov, M. Sokolov, M. Stefanishin, J. Lerner.

J. Lerner and M. Stefanishin paid attention to the IPO main stages in their works. Such researchers as V. Kublikov and M. Sokolov focused on the main trends in the development of the IPO market and peculiarities of privatization of state enterprises with the help of the IPO financial instruments.

The development of an integrated approach to reforming the IPO market, which is based on the interaction of all its structural elements, the specifics of the procedure on stock exchanges, remains an insufficiently developed scientific question.

2. Factors of successful Initial Public Offering (IPO)

Based on the pluralism of the scientific approaches, the world exchange practice and the domestic regulatory and legislative framework, IPO should be viewed as a procedure of obtaining public status by a company that includes operations of organizational, legal, financial character involving both professional and collateral participants of the stock market and groups of interested investors who are not known in advance according to the announcement of stock trading in the mass media. The choice of a professional trade organizer is one of the key decisions that the issuer must take in the process of attracting financial resources within the IPO. It is based on the factors that should be taken into account for the success of the securities placement:

- Issuing volumes according to the IPO prospectus should correspond with the stock market capacity.
- An effective demand and correspondence of the issuer's goals and the investor for searching for strategic or portfolio investors.

- Transparency and availability of information for investors, counterparties and its comparison possibility in the question of concrete issuers on the stock exchange. Peculiar features of sector profile of issuers that are represented on the determined stock exchange.
- Listing criteria of the stock exchange.
- Evaluation of compliance with the declared free-float level by the stock exchange in order to ensure favourable conditions for the secondary securities market.
- The similarity of the legal environment of the national stock market and the foreign trading platform that is chosen for IPO in order to enhance the issuer's image and to attract capital cross out of the national borders.
- Determination of the prestige of the IPO on a concrete stock exchange.
- The presence of "lock-up" limits, which are a preventive tool to protect the issue price from fluctuations and sometimes are an indispensable condition that can be put forward by the underwriter in accordance with the practice of security issue on a certain stock exchange.
- Compliance with the principles of liberalization and the availability of the characteristics of an integrated financial market to overcome regulatory and legal restrictions for foreign direct market participants.
- Features of trading operations on the stock exchange.
- The period, during which the company acquires the status of the public.
- The cost of services of professional and collateral participants of the stock market. Stock exchanges charge listing fees using a variety of methods: volume of shares offered, value of shares offered, market capitalization or flat fee.
- The need to present the financial statements of the issuer in accordance with the accounting standards that are fixed in the legal environment of the functioning of the stock exchange (IFRS, US GAAP, HKFRS, PRC GAAP).
- The tax burden on the issuer.

3. Comparative analysis of listing standards and fees

Estimation of the company's potential compliance with the listing criteria set by the stock exchange is one of the key factors that should be taken into account in the process of IPO (Table 1). The table shows the main requirements for issuers within the listing procedure on the main stock exchanges that were the largest financial centres for IPO in the first three quarters of 2017: 105 successful placements were made on the Hong Kong

Table 1

Comparing stock market listing standards and fees: a regional aspect of IPO (created by the authors considering (EY Global, 2012))

Exchange listing standards	Americas region		EMEA region		Asia-Pacific region	
	New-York (NYSE)	NASDAQ (Global Select Market)	London Stock Exchange (main market)	Warsaw Stock Exchange	Hong Kong Stock Exchange	National Stock Exchange of Australia
Time line of going public	3 years	2 years	3 years	3 years	3 years	2 years
Income, revenue and profits	Revenues (most recent fiscal year) US \$75 million	Revenue >= US \$110 million (previous fiscal year)	-	-	Aggregate profit of at least HK \$50 million in the last three financial years	Positive financial result in the last two financial years
Market capitalization	Revenues (most recent fiscal year) US \$75 million	Revenue >= US \$110 million (Previous fiscal year)	US\$1.2 million (GBP700,000)	US\$10 million	US\$25 million	AUD \$0.5 million
Number of float shares	5,000 shareholders for foreign issuers	1.25 million shares	25%	5-10%	25%	25%
Equity market listing fees	US \$ per share: 0.001-0.005	US \$125,000-225,000	GBP 6,389-369,689	PLN 8,000-96,000	From HK\$ 150,000 to HK\$ 650,000	US \$0.08 per share
Annual exchange fees	US \$ 0.001 per share, minimum US \$ 38,000	US \$35,000-99,500	GBP 4,200 - 41,400	PLN 9,000-PLN 70,000	From HK \$145,000 to HK \$1,188,000	From US \$8,000

Stock Exchange and GEM (9.1% of global IPOs), the National Stock Exchange of Australia – 61 (5.3%), the London Stock Exchange – 50 (4.3%), the New York Stock Exchange – 52 (4.5%), and the NASDAQ – 59 (5.1%). Asia-Pacific exchanges continued to dominate the global IPO markets in Q3 2017, accounting for 65% of IPOs globally and 43% of global capital raised. IPO activity of the Americas region and the region of Europe, Middle East, India, and Africa (EMEA) was approximately on the same level according to proceeds – 28% and 29% (Global IPO trends Q3, 2017).

As a rule, the higher listing criteria for the issuer's company mean the longest period, during which the company is transforming into a public one: 12-24 months for an IPO in the Americas region, an average of 12 months for IPO in the EMEA region, Asia-Pacific region – 6-12 months. The mentioned IPO timelines should be considered for informational and comparative purposes only.

The actual IPO process and timeline can vary with the specific circumstances of an individual company.

Comparing the listing requirements of international stock exchanges with the Ukrainian stock market practice, we should note positive changes towards the transformation of domestic legislation in accordance with the world realities of doing business and compliance with the principles introduced by IOSCO.

In particular, it concerns Bill No. 5592-d of 03.10.2017 on simplifying doing business and attracting investments by securities issuers.

This law should become an innovation of the National Commission on securities and stock that will introduce compulsory passing of listing procedure by public corporations.

As a result, the market will obtain the higher quality of securities of the Ukrainian stock exchanges, the transparency of operations and be the basis for the inflow of new investments.

This reform will increase the productivity of post-privatization development of companies in the financial market of Ukraine.

The maximum approximation of the second level listing requirements of Ukrainian companies to the modern practice of stock exchanges in the EMEA region is proved by comparing such stock market listing standards as the timeline of going public (3 years), free-float level (10-25%).

4. Problematic aspects and directions for improving IPO market

An interest to the IPO of shares and Eurobonds as sources of attracting capital is gradually growing after the crisis of 2013–2014 that is characterized by the absence of initial public offerings of shares of the Ukrainian corporate sector on national and international stock exchanges.

The factors that hinder the development of the IPO market by the Ukrainian corporate sector are systematized in the PWC study.

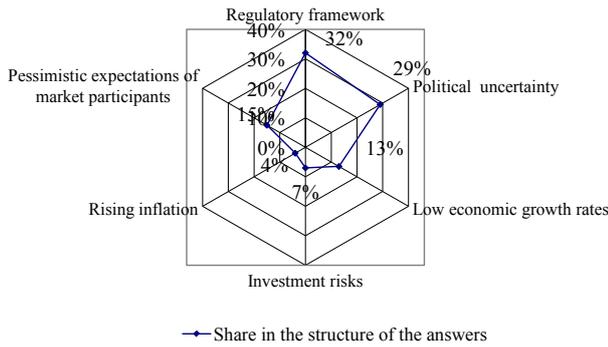


Fig. 1. The results of a survey of corporate sector respondents about the factors that hinder the development of the IPO market on stock exchanges of developing countries

The results of the investigation can be schematically represented (Fig. 1) (PwC. Capital markets in 2025: future of financial markets, 2011).

It is advisable to solve indicated problems with the participation of regulatory agencies, self-regulating organizations, and all interested participants of the stock market in accordance with the successful passage of the IPO stages (Fig. 2) (Created by the authors).

The existing culture of corporate governance, the high level of information protection on domestic enterprises in the issues of financial disclosure and an inefficient tax system are complementary to the above factors.

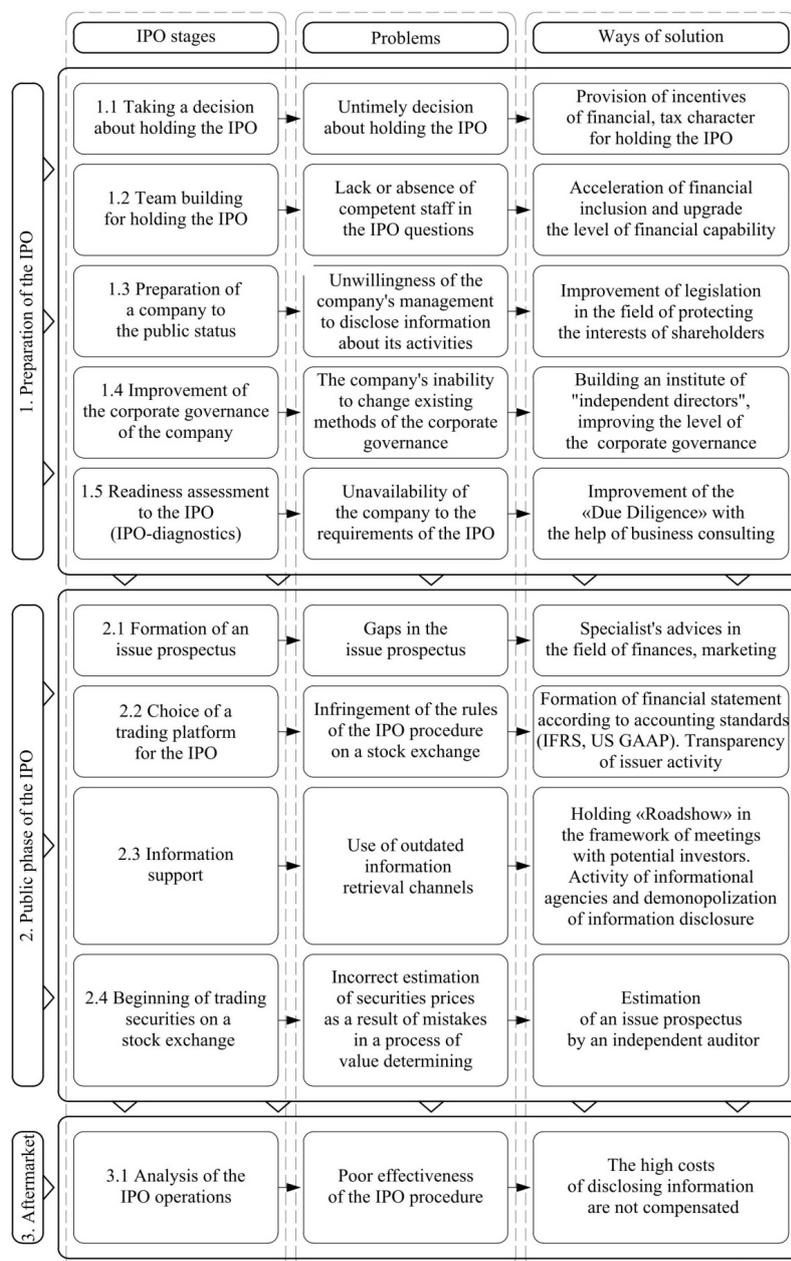


Fig. 2. Problem aspects and directions for improving the process of passing through the IPO stages

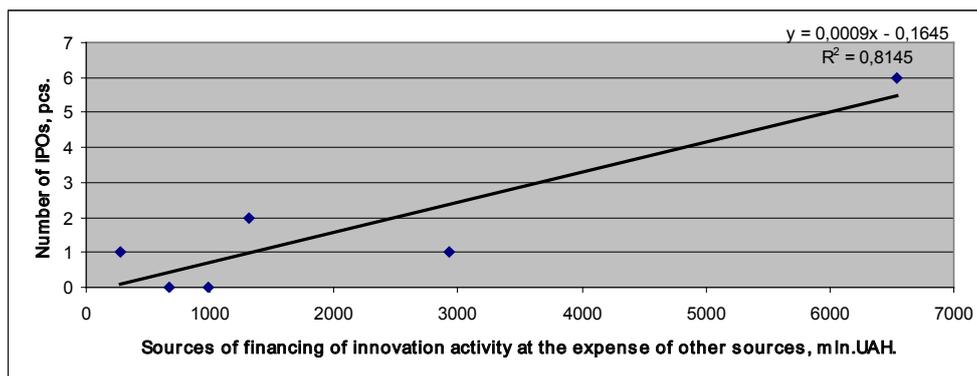


Fig. 3. Graphical representation of the results of the analysis of the relationship between the number of IPOs and other sources of financing an innovative activity

But, nevertheless, the main problem is to transform the regulatory framework, which must meet the current needs of direct participants on the stock market.

5. IPO as an innovative component of the economy’s real sector development

It should be noted that Ukrainian financial market lacks a properly formed segment of institutional investors. The result is the absence of “long” liabilities at the disposal of pension and investment funds, insurance companies.

The problem of improving the IPO market is especially acute because the accumulation of resources through the initial placement of securities is one of the effective ways of financing an innovative activity (Fig. 3) (Built on the basis of data of the official site of the State Statistics Service of Ukraine and National Securities and stock market commission, 2018).

The analysis proves that there is a close direct link between the number of IPOs and the source of financing an innovative activity that is called by the State Statistics Service of Ukraine as “other sources of financing.” The results demonstrate that the IPO is one of the sources of financing an innovative activity of Ukraine.

It should also be noted that most of the domestic companies that had an experience in holding IPOs used to issue corporate bonds earlier due to the peculiarity of the domestic corporate governance model, which has features of a debt nature that must be taken into account in the proposed model for the domestic companies entering the IPO market (Fig. 4) (Created by the authors).

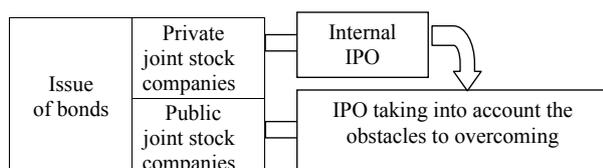


Fig. 4. Model of entering the IPO market by Ukrainian companies

6. Aspects of reforming IPO regulatory framework

Certain measures are taken to reform the regulatory and legislative framework for the development of the IPO market:

- Implementation and monitoring of the adaptation of IOSCO principles that are related to the activities of issuers in the direction of full, trustworthy, and timely disclosure of information, the equal rightness of investors, and raising accounting standards (National Securities and stock market commission).
- The enactment of the bill 5592-d by the Verkhovna Rada of Ukraine, which opens new perspectives and peculiarities of the recognition of the publicity of joint-stock companies, which should promote the expansion of the exchange register and become an investment incentive for domestic and foreign investors.
- The implementation of pension reform, which promotes the increase of the volume of assets at the disposal of institutional investors and is the basis for the formation an effective demand on the certain financial instruments on the stock market.
- Realization of the Complex Program of the Development of the Financial Sector of Ukraine until 2020 in the sphere of modernization protection of consumer and investor rights, as well as creating conditions for free capital flow (Resolution of the Board of the National Bank of Ukraine, 2015).

But, further improvement requires, firstly, mechanisms of protection the financial and economic security of the issuer in the process of acquiring public status by the company; secondly, further transformation of the listing criteria in order to approximate the current paradigm of estimating issuers in Ukraine to international practice, to promote the increase in the number of IPOs and the volume of attracted resources; thirdly, the approaches to the procedures “Due Diligence” and “Roadshow” in order to establish a weighted issue price for IPOs.

7. Conclusions

The results of the study indicate that IPO is a source of financing the investment and innovative activity of enterprises that has special features of realization at different world financial centres. The model of entering the IPO market by Ukrainian companies should be modernized to overcome the identified factors that

are specific on each stage of its implementation, taking into account the peculiarities of the Ukrainian market and focus on the leading trends. Reforming and implementation of innovations of the regulatory framework is the priority task for the modernization of the IPO market that is also the basis for protection of the interests of stock market participants.

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