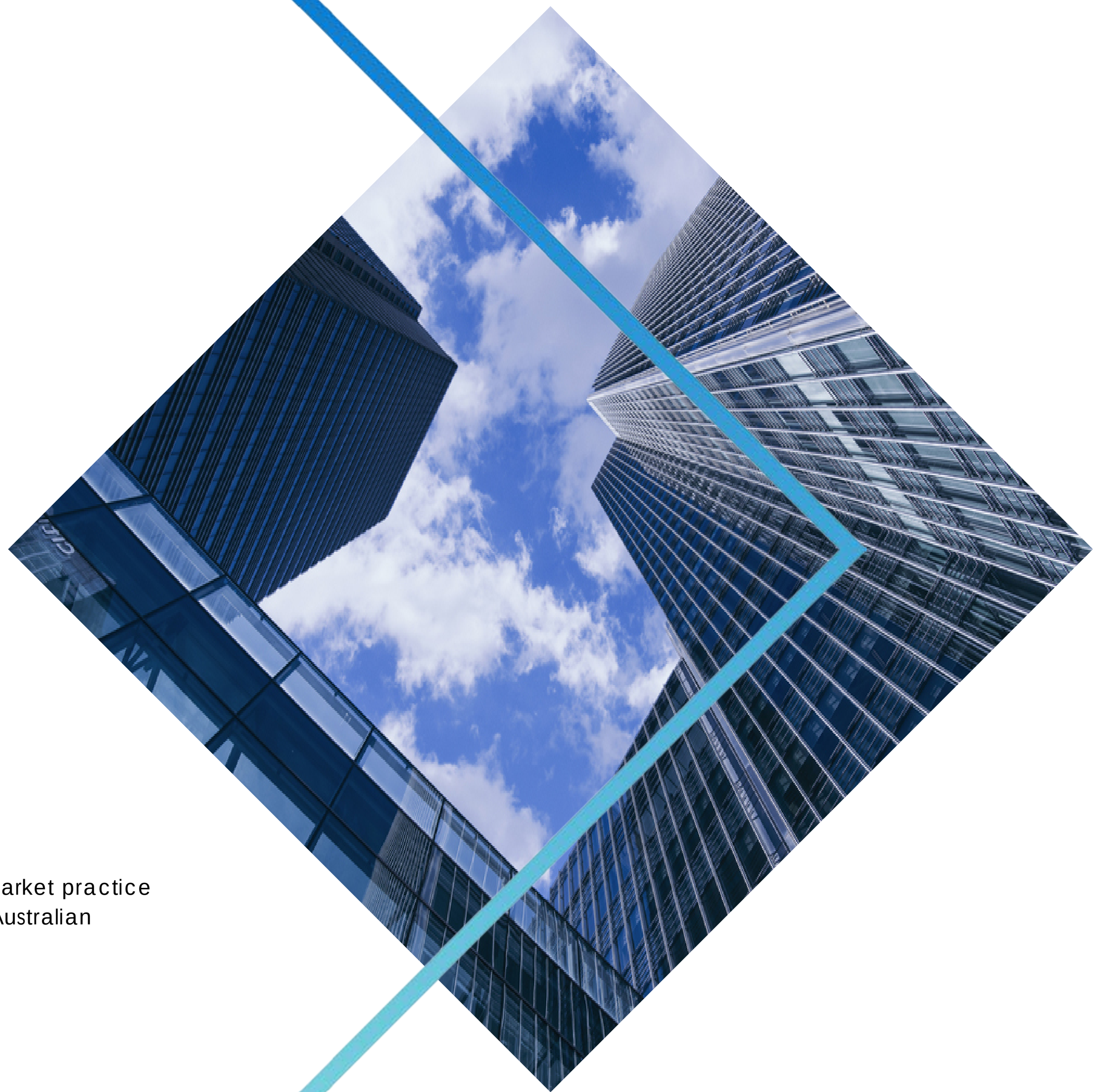
ASIC
Australian Securities & Investments Commission



Allocations in equity raising transactions (summary version)

Report 606 | December 2018

About this report

This report highlights some of the key findings from our review of market practice for the allocation of securities in equity raising transactions in the Australian market. Read the full report for detailed information.

Australian market for allocations

> Australia has an active market for raising equity capital. From 1 July 2014 to 30 June 2018, ASX figures reveal that a total of $267 billion of equity capital was raised by companies listed on ASX.

Value of an allocation

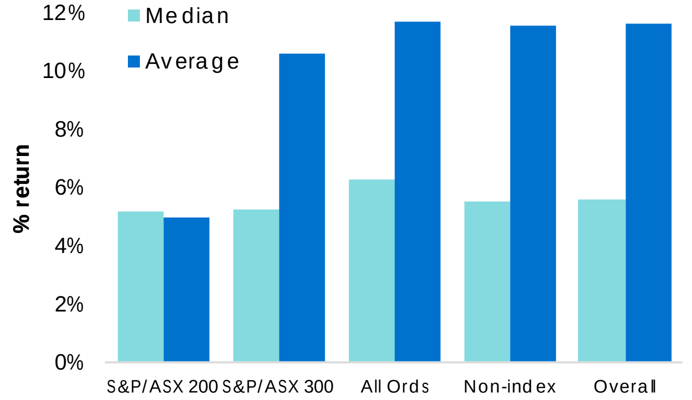
Initial public offers

- We analysed almost 300 initial public offers (IPOs) that raised above $5 million for issuers that listed on ASX in the period 1 July 2014 to 30 June 2018.
- The issue price was compared to the volume weighted average price for the first day of trading (1D VWAP) following listing.
- Our analysis revealed that, for our sample set overall, the median security price increase was 5.6% and the average security price increase was 11.6%. See Figure 1.

Placements

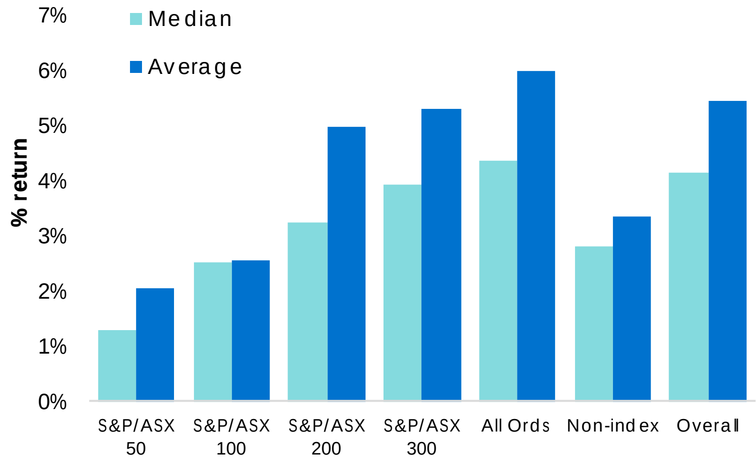
- We analysed the security price performances of the 200 largest placements (by amount raised) in the period from 1 July 2014 to 30 June 2018 for entities listed on ASX.
- The price at which placement securities were issued was compared to the 1D VWAP following announcement of the placement. Our analysis reveals that, for our sample set overall, the median security price increase was 4.1% and the average security price increase was 5.4%. See Figure 2.

Figure 1: IPOs: 1D VWAP security price performance post listing



Note: See Table 1 in the appendix for data shown in this figure (accessible version).

Figure 2: Placements: 1D VWAP security price performance post announcement



Note: See Table 2 in the appendix for data shown in this figure (accessible version).

What we did

Receiving an allocation can provide a benefit to investors in both initial and secondary equity raising transactions. A fair and efficient approach to the allocation of securities in transactions promotes market integrity, improves market efficiency and increases investor confidence.

Background

In 2017–2018, we undertook a review of allocations in equity raising transactions. The review built on our earlier work on handling confidential information and managing conflicts in the provision of sell-side research (see Report 486).

Focus of the review

Our review focused on:

- how licensees make allocation recommendations and manage conflicts of interest
- licensee engagement with issuers and the involvement of issuers in allocations
- messages to investors by licensees and issuers
- allocations to parties connected to the licensee.

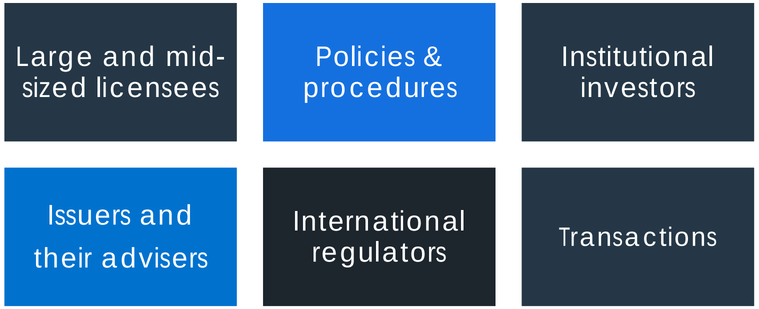
This report highlights some of the key findings of the review. The full report also includes observations and better practices relevant to both licensees and issuers.

Scope of our review

We reviewed the policies, procedures and practices of a range of large and mid-sized Australian-based licensees. We also reviewed a range of initial and secondary market transactions to see how allocations occurred in practice.

We engaged with licensees, institutional investors, independent corporate advisers, issuers, industry associations and international regulators.

Figure 3: Scope of our review



> 'Licensees should review our report and consider whether their controls, including policies, procedures and monitoring, are appropriate and sufficiently robust to meet legal and regulatory requirements.'
>
> **Cathie Armour** | ASIC Commissioner

How licensees make allocation recommendations

> Licensees consider a range of discretionary factors when making allocation recommendations to issuers.

The licensee's terms of engagement with the issuer set out the role of the parties and how allocation decisions are made. Generally, this is a collaborative process, with the issuer's board of directors being responsible for approving the issue of new securities.

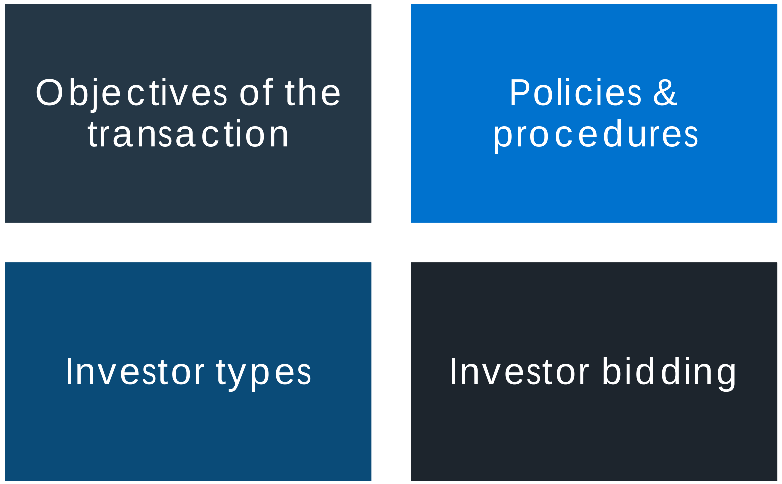
We observed no material difference in the approach to allocation recommendations where a transaction was underwritten. We did, however, see examples of more favourable allocation recommendations for investors who acted as sub-underwriters.

A number of licensees have policies and procedures that set out criteria relevant to making allocation recommendations to issuers.

These include acting in the best interests of the issuer, considering the likely impact on the after-market and the level of interest the investor has shown in the transaction.

Licensees consider the type and nature of an investor when preparing allocation recommendations. This may include the suitability of the investor for the issuer, the treatment of existing security holders and the ranking of the investor by the licensee.

Figure 4: Factors considered by licensees in making allocation recommendations



ASIC recommends

Licensees should have a policy and procedures that set out their process for managing allocation recommendations for transactions, including the role of compliance.

The objectives of the issuer should be the primary consideration when making allocation recommendations.

See Report 605 for further information on better practices.

Licensee engagement with the issuer

> Issuers typically become most actively involved in allocations when the licensee provides them with the allocation recommendation for their review and approval.

We noted that, while most issuers are interested in the outcome of allocations, some issuers have little involvement and rely on the allocation recommendation provided by licensees.

When pitching for a role, we observed that licensees typically only provide a broad overview of their approach to allocations to the issuer. A detailed discussion on allocation usually occurs after the licensee has been appointed by the issuer.

Following marketing and the bookbuild for a transaction, the licensee provides the issuer with an allocation recommendation. This may result in amendments to the final allocation recommendation.

Once the final allocations are agreed with the issuer, the board of the issuer approves the issue of new securities to those investors.

ASIC recommends

We encourage licensees to:

- engage with the issuer at key points during a transaction
- identify and manage conflicts in relation to allocations—for example, disclosing them to the issuer and explaining how they are to be managed
- have a reasonable basis for allocation recommendations and ensure they are consistent with the issuer's objectives
- ensure information provided to issuers is accurate and not misleading or deceptive.

We encourage issuers to:

- understand and engage with the licensee about allocations during a transaction
- ask the licensee questions about their allocation recommendation and how it is consistent with the licensee's allocation policy and the issuer's objectives
- scrutinise and query the basis of any advice or statements in draft ASX announcements about the transaction—in particular, about the nature and level of demand from investors. The use of overly expressive language should be avoided.

See Report 605 for further information on better practices.

Messages to investors

> Licensees and issuers often provide messages to investors about transactions, which can help them make investment decisions.
>
> We observed mixed practices. This is an area for improvement.

Messages from licensees

- Messages are often provided to investors about the level of demand and likely price at which securities will be issued.
- Messages are often provided when marketing commences and after allocations are determined. Some licensees also provide update messages during the bookbuild for a transaction.
- We observed mixed practices about the use of, content and distribution of update messages, including comments that a transaction is 'covered'.
- We observed a range of licensee practices when information provided in a previous message to investors is no longer correct.

Messages from issuers

- Some institutional investors expressed concern with statements in market announcements about the level and nature of investor demand. They cited examples where offers that were communicated as being 'heavily oversubscribed' traded at a discount to the issue price in the after-market.

Regulatory considerations

Poor conduct around messages provided to investors about the level of demand and extent of any scale-backs in a transaction may breach:

- prohibitions in Pt 7.10 of the *Corporations Act 2001*
- Pt 2 of the *Australian Securities and Investments Commission Act 2001* relating to misleading and deceptive conduct.

Issuers also need to be mindful of these requirements when making statements in market announcements about the level of demand for a transaction, and consider their continuous disclosure obligations.

> **ASIC recommends**
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> We encourage licensees to:
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> - have a process for approving messages to ensure they do not contain misleading and deceptive information.
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> We encourage issuers to:
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> - ensure that statements in market announcements about the nature and level of demand for a transaction are accurate and not misleading, and avoid the use of overly expressive language.
>
> *See Report 605 for further information on better practices.*

Allocations to parties connected to the licensee

> Allocations to parties connected to the licensee (including related investment managers, employees and principal accounts) raise significant conflicts of interest concerns.

Licensees are gatekeepers paid by issuers to manage transactions. In this role, licensees obtain significant information advantages over investors who bid for securities in transactions.

Allocations to employees and principal accounts can influence licensee decisions, which may result in advice to investors that may not be in investors' best interests.

Most institutional investors did not believe employees should receive allocations, given the information that licensees receive about the nature and level of demand for a transaction.

Related investment managers

Some licensees have related entities that manage funds on behalf of third-party investors.

From our transaction review, we observed it was not common for related investment managers to participate in transactions that the licensee was managing.

Most large licensees had a process—often reflected in policies and procedures—to manage bids and allocations to related investment managers.

Employees and principal accounts

We observed that large licensees do not allow allocations to employees and limit allocations to principal accounts to subscribing for shortfalls in transactions that the licensee has underwritten.

At mid-sized licensees:

- allocations to employees occurred in most transactions we reviewed but allocations to principal accounts were less common
- there was limited disclosure to issuers about allocations to employees.

> **ASIC recommends**
>
> Allocation recommendations to employees and principal accounts should be avoided as they present a significant risk of conflicts of interest to both the issuer and investors.
>
> Licensees that propose an allocation to employees and principal accounts need robust policies and procedures to manage conflicts.
>
> *See Report 605 for further information on better practices.*

Appendix: Accessible versions of figures

This appendix is for people with visual or other impairments. It provides the underlying data for Figures 1 and 2.

Table 1: IPOs: 1D VWAP security price performance post listing

Category	Median	Average
S&P/ASX 200	5.1%	5.0%
S&P/ASX 300	5.2%	10.6%
All Ords	6.3%	11.7%
Non-index	5.5%	11.6%
Overall	**5.6%**	**11.6%**

Note: This is the data shown in Figure 1.

Table 2: Placements: 1D VWAP security price performance post announcement

Category	Median	Average
S&P/ASX 50	1.3%	2.0%
S&P/ASX 100	2.5%	2.6%
S&P/ASX 200	3.3%	5.0%
S&P/ASX 300	3.9%	5.3%
All Ords	4.4%	6.0%
Non-index	2.8%	3.4%
Overall	**4.1%**	**5.4%**

Note: This is the data shown in Figure 2.