The Australian Finance Podcast Episode Transcript

Episode: Who's who in the IPO Zoo (inside an Initial Public Offer)
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Speakers: Kate Campbell & Owen Rask
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Episode transcript:

Owen:
Kate Campbell. How are you doing?

Kate:
Good. Thanks, Owen.

Owen:
That's great to hear. It's a bit overcast here in Melbourne. On Wednesday, October 13th is when we're recording. Most people probably don't know this, in fact, we would imagine most people don't really care, but we record almost all of our podcasts on a Wednesday to try and get them all done on the same day. And it's a heap of fun. We do it in the morning on Wednesday. And so here we are. And today we're talking IPOs. Your favourite topic, Kate, I'm led to believe is on IPO. No. She shakes her head. So tell us a little bit about, just to start off with, why are we even talking about IPO's? Why is this a thing that people talk about?

Kate:
Yeah. So IPO is just shorthand for initial public offering, and it's really the process a company goes through when it wants to go from a private business, like that cafe you see down the street, to becoming a listed business that you can buy on the stock exchange. And so when you think about Telstra or BHP, these are all public businesses that you can just create a brokerage account and go and buy shares, like you would in ETF. And so it's quite a popular topic and we get questions about it every time there's a new hyped up IPO that comes about. And so, what are some of the recent ones? Airtasker, Booktopia, Adore Beauty. IPOs are happening on a weekly basis. And most of them you don't hear about because they're really small companies and they're probably not companies you'd want to be investing in anyway. But we thought we'd do this episode because every time one of these hyped up IPOs comes out, we do get a lot of questions.

Owen:
Yeah. And as you're about to find out, IPOs are one of those concoctions by financial professionals that basically are designed just for maximum excitement. So the reason why you hear about IPOs is because the people that organise them, the groups of people behind the scenes that organise an IPO are extremely well incentivized to make sure everyone knows about it. Because if everyone knows about it, then everyone wants to get excited and buy the shares. Which then pushes up the price, which means bigger commissions, which means that when the stock finally hits the stock market and you can see it on the public market or the ASX or the share market, as we know it, then it jumps and people fall in love with this idea of quick profits. This get-rich-quick scheme. Right, Kate?

Owen:
They think, I'm just going to buy this exciting new thing and everyone's going to make money, including me, on the first day, because the thing's going to pop. So there are many reasons why we as investors and I guess just the general investment community get excited about these types of things. Quick question for you, Kate, maybe just straight off the bat, are IPOs, initial public offerings, which we heard about in the Wolf of Wall Street, by the way, are they a get-rich-quick scheme? Do they work for us?

Kate:
I wouldn't say they work every time. There's a lot of companies that list that are pretty bad companies at the end of the day, that you don't want to really touch with a 10 foot pole, and a lot of the time the reason a company is listing, is not the reason maybe they’re telling you in their public marketing material and so, there’s a lot of reasons why companies list and we can talk about that a bit later, but sometimes it is a marketing

scheme by the company, sometimes the numbers aren't really what they say they are and so you may be buying into something that you wouldn't have bought normally if it was listed but you sort of got sold intot he hype and excitement of something, and so I think thats really important to just sort of know from the outset that a lot of people involved in the IPO process are getting paid a lot of money, from, like we'll explore some of the individuals and what their role is, but from the large institutional banks and brokerage firms to the lawyers writing the prospects to the accountants and auditors. Even like the ASX, because they're getting paid massive listing fees. There's a lot of money to be made throughout the IPO process that isn't really involved directly in what the company is doing. It's quite a lucrative industry bringing a company from private to public.

Owen:
I just want to double click on something you said there, which is the reason why most companies go public is probably not what you think, at least not what you're led to believe. So when most people think about an IPO, what they're thinking about is from the perspective of buying shares. So you think I'll buy shares in this company because it sounds exciting. Airtasker, everyone uses Airtasker, I'll buy shares in that company. And that's what you think. But the real reason, and I'm going to pull down the curtain on this one, is that at the end of the day, I would say 99% of IPOs happen because the person that owns the company or the people that own the company want to sell it and they're looking for someone to sell it to. That is basically it. So let's use an example.

Owen:
Let's say that me, I own a private business. And let's say my business grew and I'm thinking, oh, I'd really like to retire now. But I've got all of my money tied up in my own business. How do I get some of the profit and some of the, I guess, value of that business? How can I release that so I can then go and retire with that money? Now, there are a few options that you have. One of them is you find a private buyer. So you go to another business that you might want to sell to, like a competitor. You could find another investment firm like a hedge fund, like a private equity fund or some type of investment firm that might want to take on your company and they give you a cash settlement.

Owen:
The other way you can do it is you can, if you're big enough, you go to an IPO. There is something in between called crowdfunding, which we'll cover in another episode. But basically you could go through an IPO process. And this is a process where, let's say, again, that you have a private business, you then go and you speak to an accountant, you speak to a lawyer and they say, okay, yep, we're going to get all the books looking

good, we're going to audit your accounts, and then we're going to speak to the lawyers who can draught up all the documents and send that off to the ASX. The ASX will then approve you to be permitted on the ASX. Then you can speak to a broker and the brokers ... And there are some of these brokers out there and they host podcasts. The brokers, then it's their job to go and sell that company in tiny little pieces to all of their clients and to get as much fanfare in the media and elsewhere as possible.

Owen:
So that when in it comes time for the IPO day, the company that's selling has many different investors who have committed their money. Joe Bloggs from WA has put down $2,000 for this IPO through his broker. And Stacy, whatever her phase is, from Darwin buys $5,000 through her broker. And then all of a sudden, if everyone puts in a little bit of money, you can quickly sell a $100 million business or a $500 million business. And then on day one on the stock market, those two people could sell or they could keep holding their shares. The fundamental difference between what we're talking about here and when you buy shares on the stock market. So let's say if you go and buy shares in BHP today, the money does not go to BHP, it goes to whoever you bought the shares from. Whereas in an IPO, the money goes to the current owners of the shares.

Owen:
So that might be an individual investor. So if I owned a company and you wanted to buy it from me, I would be getting that money because I currently own the shares. So it's different. It's not like it's going straight through the exchange, it's going to some sort of private investor. Oftentimes what happens in Australia is it's a private equity company, like a big investment firm that owns a private company and then sells it to smaller investors like us. So I hope that backpedalling just explained a bit of the process. You basically have a private company that's going to sell to many individual shareholders and it's typically owned by someone. And the primary reason is money, it's not because they want to do you a favour.

Kate:
No.

Owen:
They want to sell their shares.

Kate:
Yeah. The IPO is definitely not geared towards the person participating's favour. It is trying to make money for the people going through the process and all of the different participants involved. And Owen, have you ever invested in an IPO?

Owen:
Never. No. I've never. Well, so let's just be clear. I've never bought a company stock before it's listed. I prefer to wait until it's listed, which we'll get to in a little bit. But basically I think that there's no reason to rush an investment decision. This is a bit of hearsay, I don't really have anything to back this up, it's just my belief. Is that the first one to two years of investing after an IPO is very, very, very volatile. So it can be because these companies are adjusting to public life, all of a sudden these private companies now have to report to shareholders every quarter. They have to hold their hand on their heart and say, no, this is the truth. Whereas when they're private companies they can do and say, and whatever. They get away with it because it's their own business.

Owen:
But in the stock market, it's a totally different thing. So companies struggle to make that adjustment. Also, sometimes companies are ... you are in an IPO, you are buying from someone who knows more than you do. So for example, on the stock market, basically we only get annual reports, half yearly reports and any type of presentations that the CEO or management team do. But in a private company, those management teams and whatever, they can talk and say and do whatever they want. They could tell their next-door neighbour how much money they make and where their revenue comes from and whatever. As soon as you hit the stock market, it's like this opaque window slam shut in your face and you only get past little bits and dabs here and there through the window.

Owen:
And so what basically it means is that in an IPO, you are buying from someone who knows everything about the company and you know only what they're telling you. And that creates what we call information asymmetry, which is where you're buying from a very informed seller, and so you want to be very informed as well. And sometimes the best way to ... I find the best way to get over that is just to wait a little while, see how the company goes on the stock exchange, until everyone's operating on the same information. Probably the biggest one, which is a really interesting thing just as to where these two worlds collide, was Medibank IPOed, I think it was in 2015. So it's going back a little while. But Medibank, you would know, is the big health insurer that was sold by the government onto the stock exchange.

Owen:
And the price of the IPO was set at a certain level. And basically, we did our own valuations as analysts, when I was at a former company that I was working for. We did

our own valuation of Medibank and our valuation for Medibank was 5% higher or 10% higher than what the offer price was, the price at which they were selling shares in the IPO. And from that point on, I knew that basically every meaningful IPO is priced to perfection. So the government was selling those shares at that time, because the government owned Medibank. And from that point on, I knew that they do all of these things on purpose and they price it just under a fair valuation, so they want you to buy shares. And then hopefully on the first day, the share price pops a little bit, it jumps up a bit. So then the government looks like the good guys for giving you a good deal.

Owen:
So you can see how all these things trickle on. And that just reminded me, from all those years ago, that the other person on that side of the trade probably knows more than you do. Sorry, that was a very long-winded answer to a very simple question. How about you? Have you ever invested in IPO?

Kate:
No. No. I have invested in a few private companies through crowdfunding platforms, just companies I was interested in in certain ways. But that's ... Yeah.

Owen:
Which platforms do you use to do that? Sorry.

Kate:
I think it was Virtual and Equitise. Yeah. There's a few.

Owen:
Yeah. They're the big ones.

Kate:
Yeah. Somewhere a few years ago. I mean, most of the companies are still going, but-

Owen:
You say that with a laugh.

Kate:
Yeah. One was a travel card company. So yeah, that has had a challenging year. But it was more something I did with money I was happy to lose, because I knew the people involved or I had some interest in that company. And so that's even riskier because there's a chance that the company will never list or never get sold or just run out of

money to keep going. And so at least with the IPO, if they end up postponing the IPO or they just decide not to do it, you haven't necessarily invested money into it.

Owen:
Yeah. Because you've committed it, but it's not set in stone. Okay. So can you explain ... there was something really interesting, which you came across in your research for this, which was basically ... So if you think about it, we're investors, we're looking to buy shares of really interesting companies. But from the other side of the table, there are people who, they're not buying shares, they're selling them, so they want to present that company in the best possible light. You found a really interesting thing about the story that those sales people and those brokers and investment bankers, et cetera, want to tell. Can you tell us what they're trained to say?

Kate:
Yeah. So pretty much every law and accounting firm that's large that you've heard of under the sun has a whole heap of resources to help companies that are private at the moment and want to go public. And they have mega, like 30-plus page detailed guides on the whole IPO process. So if you are interested in IPO, that's probably a good thing to read because you can see it from the company's perspective and all the different hurdles, regulatory requirements they have to go through to eventually list. And the interesting thing I came across was, in one of the large accounting firms, it had a guide on writing your story in terms of, how are you going to convey the company's story from inception? How did the founder start it in the garage and took this company from zero employees to 1000 employees with profits and products and all sorts of things.

Kate:
As a company, they want to curate this story because it gets them news articles, it gets them picked up by different outlets and it'll hopefully generate enough excitement that you as an investor want to get involved before the company's gone public. And one of the interesting things I saw, it had a whole list of common characteristics for writing a strong equity story from a company's point of view. I mean, I looked at it from a writing perspective and it was interesting to see that advice and having ... Your company's story needs to be compelling and telling investors why it's an attractive investment opportunity. And so just to keep in mind, this is what these large companies and legal firms are telling a company that they need to make their story sound like. It needs to be really clear, so investors can understand why the company is growing and is a good company to invest in.

Kate:
It needs to be differentiated and show why this company is different to its competitors that are listed. And it also has to be convincing, which that's always a good one because they're trying to convince you as an investor that this is a company you want to invest in because of their track record, their contracts and their clients, their financial data. And so they'll use everything possible, they'll use every statistic in the book to try and tell you that this is the company you want to invest in, this is the place to be, this is the future.

Owen:
There was one more on there, which I thought was really interesting, which is make it believable.

Kate:
Yeah.

Owen:
And it goes on to say, "It is very tempting to try and big up your story for the IPO. Resist this temptation, because promising too much before an IPO can lead to problems delivering on that promise when the first set of results come along. That let down is difficult to recover from." Which makes sense. You do see companies come to the ASX and they promise things or they have these big expectations around growth and whatever. And then all of a sudden, a year in or two years in, they don't really get anything from that. They don't deliver on those expectations, they don't meet those expectations, they push them further back, they drop them from their presentations.

Owen:
There's a lot to go on here, Kate. I think what we're trying to explain is basically there are two sides to this table. There is the people that are buying and there is the people that are selling. Tell us, who else is on that selling side? So we're on the buying side. Most of the listeners, all of us here today, we are buying shares because we're interested in these companies. And there are so many IPOs at the moment, which is a totally different thing in itself. But, who are the key players in this market that we need to know and what do they do?

Kate:
Yeah. So I guess the first place to start is the actual company IPOing and their main reasons for doing that. And looking into the board and the founders and the CEO, and they potentially already have a stake in the company. They may have a considerable amount of their net worth tied up in that company. And just looking at, why now? Why is

the company choosing to do it? Is it just because their timeline's been sped up because everyone's wanting to invest in IPOs during 2021? And so they've gone, hey, let's just do it now because the money is there, the market. At the moment, we're in a record bull market. And so people are excited about investing in new companies and there's a lot of money available and no one wants to keep their money in the bank. And so other reasons for IPOing right now, valid and just like, do you like the company? Do other people like the company? And looking in that broad picture of, why now and what are they doing it for and how are they being incentivized?

Owen:
Yeah. And I think that's a really important one. So if you look, some companies will say legitimately that they want to IPO for reasons other than financial reasons. So for example, most founders ... not most, but many founders will sell some of their shares, but not all of their shares during an IPO. But some companies, like say a banking company or a company that deals with overseas clients, typically what happens in that situation is they want to IPO into the ASX because the ASX is a reputable stock exchange. And so if they're audited and they have the oversight and regulation of the ASX and the Australian government, what actually happens is their customers see them as more reputable. So companies might do that. So if you're a bank and you're not on the stock exchange, you're probably viewed as more risky than a bank that is on the stock exchange, for example. Even though they're both regulated by APRA, there's a perception that because you're a public company, you're more reputable.

Owen:
So there's plenty of things to consider with the IPO. But most of the time, you just got to follow who is selling. Just find out who is selling. That's typically disclosed in the prospectus, which we'll get to in just a moment. But for example, in a lot of small IPOs, like under 100 mil, they're just rubbish IPOs, to be honest. Not all of them, but many of them are just rubbish, like concoctions of investment banks and whatever, and individuals who are trying to sell a really poor quality company and just try and exit that position.

Kate:
The interesting thing was, when I was ... because the ASX have a list of all of the upcoming IPOs on their end. And I saw there was around 30 companies listed, and majority of them had the words metal mining or mineral in the company names. So it's quite interesting. You see a lot of these smaller IPOs are in particular areas or exploration of different mining areas. And so yeah, [crosstalk 00:21:38] it's not a broad, diverse spectrum of different companies, there's a lot in particular sectors.

Owen:
Sometimes, particularly with those junior mining companies, what happens is the IPO stages when they can get money into their company, to then go and fund the exploration. So their business model is pretty shaky and they pretty much just need the money so they can keep exploring, which is pretty risky, obviously. So a lot of those smaller companies are very ... You have to keep your wits about you. It is the wild west of IPOs, if you think about it that way. The other thing that you'd probably want to consider, and I'll just try to be concise on this one, which is basically, I said, who is selling? Sometimes it's the founder, sometimes it's a group of people, but sometimes it's a private equity company. And this might be one of the big financial firms you read about in the AFR or on the news or whatever.

Owen:
And these companies typically buy companies before they're on the stock exchange. They might, say, spend $200 million on a company, so a pretty big company and they go and buy them. And then what they do is they use their expertise as investors and investment bankers and they strip out costs, reinvest into the certain parts of the business, make it look good, and then bring it back to the stock market.

Kate:
Almost like renovating a house. Flipping it-

Owen:
Exactly. Flipping.

Kate:
... buying it, renovating it, selling it on.

Owen:
Yeah. Perfect analogy. So they're like the flippers and they bring you that house back to a state where it's acceptable, and then they put it back on the stock market. And then sometimes that's fine, sometimes they leave it and they didn't do all of the work properly. But that's often the case. So a PE or a private equity company is often one of the sellers in these types of situations. How about, can you explain brokers and an underwriter, Kate, what are those two things?

Kate:
Yeah. So the company itself won't do all the work of trying to find people to buy parcels of shares. So they'll get a broker, maybe a lead broker. So that could be something like Macquarie Bank. There's a few other brokerage firms. I don't know if Bell Potter do it.

Owen:
Yeah, I think they do. I think they participate. Yeah.

Kate:
Yeah.

Owen:
But all of the big brokers will do it.

Kate:
Yeah. [crosstalk 00:23:57]. There's a few small boutique brokers I've come across that just specialise with those 10 to $20 million IPOs. And so you want to find out who the brokers are. And if you look at the prospectus, so once the company decides it's going to list, they'll issue a whole heap of materials and documents, usually on their website. You can scroll down to the footer and it will say investor centre or public relations or something like that. And then you can look at the prospectus and find out who's the broker. So who's running the show and who's trying to sell this. Because if you are interested in an IPO, that's one way to get involved. Is by getting in touch with the particular lead broker or the other brokerage firms involved.

Kate:
And they will be the company responsible for sourcing ... mostly, for large IPOs, it would be mostly large institutional banks and fund managers and things. So they'll be sourcing commitments from all sorts of different people with money that are interested in investing this company. And they've got to wrestle up business, they'll produce expert reports on this company saying that this is a fantastic thing that you want to be involved in or you're going to miss out. And so the broker is incentivized to make sure this IPO does really well. And then-

Owen:
And there's probably one ... Sorry, you go on.

Kate:
Oh, no. I don't know if we want to touch on underwriters.

Owen:
Yeah. I think that's an important thing too, because they're kind of related. Oftentimes the broker is an underwriter or sometimes it's someone different. [crosstalk 00:25:27].

Kate:
Oh, yeah. The underwriter is a little bit of an insurance scheme because people want their IPOs to do well. So they're going to agree to take up any shares that aren't taken up in public during the IPO, and they'll be paid fees for doing this. So this will also be included in the prospectus. Would all IPOs have an underwriter?

Owen:
I don't know if they do. I actually don't study them that closely, to be honest. But I don't think they would, because some of them probably don't need them. Some of them will be oversubscribed, for example. But actually that brings us to an interesting point, is that if you want to get in on an IPO, I should do air quotes, in on an IPO, for anyone that's watching the video, typically you can't get in on the good ones. Just keep that in mind. All the good ones are reserved for the clients, the loyal clients of the brokers. So that's why the good ones tend to be oversubscribed. Because that means that there is more demand for the shares from investors than there are people selling in the IPO.

Owen:
So typically that's reserved. But sometimes there's a shortfall, what we call a shortfall. Which is where the company says, we want to sell our company and we want to raise $100 million during the IPO. We want to sell $100 million worth of shares. But there's only $80 million of people that want to buy. Of all the investors, only $80 million comes in as offers. If that's the case, there's $20 million left over, that's a shortfall. And that's where the underwriter would step in typically. So the underwriter would say, yes, we'll take up that $20 million and then we'll just sell it on the stock market. And sometimes this isn't always, I believe, this isn't always a single firm or a single investor, it can be a group of people that are aligned with the broker, so high net worth individuals.

Owen:
For example, who might say, yes, we'll contribute to being the underwriter. And in return for giving that insurance to the company, they take a fee. And you've written in our notes here that it's typically around 2.5% for a medium or large IPO, or it could be closer to 5% for a small IPO. So this is basically an incentive for the underwriter to make sure the deal gets done. And that's basically it, it's like insurance and you collect it later. But another thing that they get and often the brokers get as well, which has always been super conflicted in my mind. Oftentimes the brokers get options in the shares of the companies that they IPO. So they'll get some weird incentive that's kind of like, it is aligned, but it's not really aligned.

Owen:
So it might be like, for example, let's say the IPO price is a dollar, they might get options for every 100 shares that they sell to clients. They might get one option that becomes a share at a $1/20. If the share price hits a $1/20, your option becomes a share and you can sell that. And so for the broker, there's a huge incentive to get the share price to go up as quickly as possible. And so this is where, particularly in small IPOs, this is where it can become very, very murky. Like, who are they actually working for? And we don't say all this stuff to scare you, it's more so just that you're aware of what actually goes on in the industry. This stuff actually happens, this isn't just us making it up. So that's underwriters and that's brokers. One final party, Kate, which I'll throw it over to you as our resident legal guru. Lawyers, what role does a lawyer have to play in IPO?

Kate:
Yes. So for lawyers, IPO is a very lucrative business and there's a lot of money to be made because there are a lot of documents and things that are required. So from preparing the IPO documents, which might be ... There's a whole range of documents because a private company might not have all these company documents they need. They might need to have particular statements on employee trading, they might need to create statements on their approach to environmental matters. There's a whole heap of documents that a company needs when they become a public company. And so the lawyers will be doing everything from liaising with the stock exchange and our regulator, ASIC, writing the prospectus, conducting legal due diligence on the company. So that is why if you want to learn more about IPOs, every big law firm under the sun has a whole resource section and PDFs and all sorts of things to help you learn about the IPO process. Because the law firms want to attract all of these new companies that want to list to them because there's a lot of money involved in preparing all these documents.

Owen:
Absolutely, there is. And that's totally reasonable. As a business owner myself, not that we would, but if we did want to IPO our business, it would be so hard to do it without the help of a good lawyer, accountants, brokers. It would just be basically impossible. I don't think I've seen anyone trying to do it themselves. But crowdfunding is trying to fill that void a bit. But yeah, so lawyers are [inaudible 00:30:47]. One final thing I want to add on brokers is, oftentimes, once this company hits the stock exchange, what you'll find is that the brokers release research reports. So let's say we run Rask Brokerage and I'm the guy that led the IPO and I've got this company onto the stock exchange. And then I go, hey, Kate, you're an analyst at Rask Brokerage, can you go and research the company that we just IPOed and then put out your research report?

Owen:
And then people on internet forums and whatever go, oh, Kate from Rask Broker research just put out a new price target. We should go and check that out. Oh, the price target says it's 20% higher than the current price. And then meanwhile, everyone back at Rask Brokerage HQ are thinking, oh, there's no surprise there, the price is a little bit higher, it's Kate's price target. Now, there are rules around what can and can't be said here. So I'm just being cynical and a little bit facetious, but I want to make the point that oftentimes when you hear broker upgrades price target or broker valuations or broker forecast, this and that, it actually comes sometimes from the same company that benefited from selling the company. So it becomes this whole circle that feeds on itself. Again, this is not about IPOs in particular, but just about everything in general. Okay, so-

Kate:
Yeah. Because a broker needs to look good after the IPO. A broker doesn't want to be the lead broker behind an IPO where the company share price drops 50% in a year. That doesn't look great on the broker. So it's just about following the money and knowing what the incentives are. And I think that's what you're going to touch on next, with looking at a few other numbers behind the IPO.

Owen:
Yeah. So this is the thing. So basically, you have written some things in here, which are some insider jokes in our industry. But IPO, as we know, stands for initial public offering. But basically, it can also stand for, it's probably overpriced, imaginary profits only and insiders private opportunity. There are many ways that you can take this. But basically what happens is, when a company lists on the stock exchange, it has to issue something called a prospectus. And a prospectus is, all of those parties that we just talked about contribute to this. And it basically is a big document, even bigger than an annual report that breaks down everything about the company, it's industries, some of the key risks, the story, the products. They sell the financial statements, the notes.

Owen:
And to be honest, I think prospectuses are the best type of document in the market. So if you are an analyst and you want to learn about a company, you could probably read one prospectus instead of four annual reports, and you'd have a better understanding of the business. Because annual reports assume that you know what the company does already. And so that's why if you've ever picked up one of those, you're like, what are they talking about? Profits up, down. I just want to know what the company actually does. Well, if it's IPOed recently, you could just read the prospectus, which will tell you everything. From how it started to what industry it operates in to the growth of that industry and what products they sell. The prospectus is the thing you want to look at.

And in there, you'll learn all about the financials. And so there are heaps of different things you can look at in there. This idea of lipstick on a pig, Kate, which is sometimes the financials, even though they're audited, they are presented in the best possible way.

Kate:
Inflated a little bit. There's been a few examples recently of companies that have inflated their pre IPO profits and what was said in the prospectus.

Owen:
Yeah. It's not necessarily outright lies, it can just be stretching the truth. SO it can be things like, we came across one recently that we're researching, which is one of the biggest ones in Australia in recent times. And basically they said, oh this is an Australian business and we're really good at this Australian business, but we also have an overseas business. And this other company, this research company which we paid has done a research report for us to tell us how big that market is, so we can then tell you how big it is. So take it from them, because they're a third party. Yes, we paid them, but they've done the research. And so then that goes into the prospectus. And so when we went back and checked those numbers for ourself, we noticed that it was probably like 10 or 20% bigger than what we thought it was.

Owen:
So they've stretched that a little bit and then they stretch this a little bit and then they stretch that. And all of a sudden it looks like it's really, really, oh, great, all of a sudden it's a growth company. And I'm not saying that that's wrong. That's good that they have growth ambitions or whatever, but you've just got to be aware that even in the prospectus there are things that you should second-guess pretty much all the time. Just second-guess. So some of the things-

Coming back to telling the story in the marketing, they're going to show everything in the best light. They're not going to tell you about all of the warts underneath.

Owen:
Yeah, that's it. So there's a great writeup that we've got to accompany this podcast from Kate. But basically, you'll have everything that you would expect to learn about a company and its industry. Some of the things you'd be looking at are the financial statements, the cash flow, balance sheet, the income statement, all those things. And then you'll be reading the accounting notes, which is further down. And you want to pay particular attention to cash flow and you want to pay less attention to what we call proforma. So proforma is basically the company forecasting its results for the next year or two. That's valid. You want to know that they're forecasting results and they have a

good handle of where they're going to be in the next 12 months or two years. But you want to pay better, more attention to the financials that are already in front of you that are audited, because they're the most reliable.

Owen:
So you want to look at the audited financials. Particularly, I like to look at the cash flow statement because you can actually see what cash is coming in. There are some risks, there are many risks. The company will outline some of these in their prospectus, but you should definitely do your own, just like if you're doing your own due diligence on any company anywhere. Kate, I think that about covers it, because there's so much to do. I think one final tip that I'll have is that if you're going to invest in a company, any company, IPO or otherwise, and you think, oh it's a great company, it does this, that and the other, like Airtasker. Airtasker is a good example. Well, go and use Airtasker before you buy the shares. Figure out what it actually does.

Owen:
Do people like it? Do people use it? Don't just buy it because you can buy it, buy it because you think it's actually a good business. And go and use the product. If you can't use the product, jump on an internet forum or speak to someone in the industry. You'll always be surprised which family member knows someone that works in that industry, and you can just ask them about it and see what they have to say. Okay, Kate, we're recording this in October 2021. What are some of the biggest IPOs of the past year?

Kate:
Yeah. I checked around with our team as well, and some of the, I guess, most popular and largest IPOs this year have been Aussie Broadband, Cobram Estate, which is the olive oil company, Nuix, which is an interesting example of maybe things going wrong.

Owen:
Really horribly wrong.

Kate:
Booktopia and Airtasker. And even if you have a look, the ASX publishes research each year on their top 10 IPOs by capital raise. So that's another interesting thing. I'll link it in the show notes. But I think it's a good idea, if you are interested in IPOs, just to have a look at some of the historical IPOs, both good and bad. How has that story and narrative changed before the company went public? And after the company went public, how has the company dealt with it? What are some examples of the things that could go wrong? I mean, Nuix is a good case study for some of that. When the regulator gets

involved and potentially people are under investigation and the numbers weren't quite what they were supposed to be.

Owen:
And that was like a historical issue, which probably would've been quite hard. Some of that stuff may have been quite hard to detect. And the irony is that Nuix specialises in software that helps ASIC detect fraud and negligence and all different types of things from data sets and analytics. So that's the irony of that one. But on the whole, me particularly, I've been quite scathing of IPOs, just because I can't ... Look around you, I don't think there are many people in Australia that have something negative to say about IPOs, because it's like a selling craze and the finances-

Kate:
There's so much money involved in the whole process. You are-

Owen:
But I'm here to tell you, it doesn't work all the time. So-

Kate:
Yeah. And I think some questions we get a lot is just, how can I get it? I'm seeing this company I'm really interested in, it's listing next month, how can I get involved? And unfortunately, as we mentioned earlier, for most of us as little retail individual investors that don't have millions and millions of dollars, we are not wholesale investors, we're not institutions, we're not fund managers. So often, for the really good IPOs, we just can't get involved. And we have to wait until the company lists, which isn't so much of a bad thing. You might miss out on a 50% first day rise in the share price. But if it's a good company, over time, then you'd be wanting to have a look at it anyway. And the other thing is looking at the prospectus, so a smaller IPO.

Kate:
Having a look what the broker is, and you may be able to, as a retail investor, open a brokerage account with this particular broker to get involved in that IPO. And there's also some smaller platforms, Fresh Equities, Equitise and OnMarket, which they're generally quite small IPOs. But you can actually get involved through their platform quite easily in some companies and maybe just have a look and see what kind of companies are listing through these platforms.

Owen:
Yeah. I spoke to Johnny from Equitise quite a few years ago on the Australian Investors Podcast. I spoke to Ben Williamson from Fresh Equities in person, didn't speak to him in

the recording. A guy with a lot of integrity, in my opinion. Have you spoken to the team OnMarket before? For either this podcast or How to Money?

Kate:
No. No.

Owen:
No. But we see them around a lot. They do a lot of good stuff in the market too. So that's one way you can get involved. Some people, you would have to go direct to the lead broker if you want to get involved. So if you say, oh Billy Bob's fun company is coming up for IPO and I want to invest in that. And the lead broker is ... I know they'll say Morgans. Well, you might want to reach out to Morgans and see if you can become a client of theirs. At the end of the day, we started ... You asked me a question at the top of the show and I asked you the same question, have you invested in IPO before? Both of us said no. And we've been investing for quite a while, me a bit longer than you, but I've never felt the urge to get involved.

Owen:
I think some of the really exciting companies that I really have wanted to invest in the past, companies like even like Snowflake in the US, which is super overpriced. Unity in the US. Atlassian, which we talked about just before we came on. It's an Australian company, but it's not on the Australian stock exchange. Heaps of these really interesting companies. Even like Aussie Broadband, for those of you that use that. I'm actually connecting to you, Kate, right now with the Aussie Broadband connection. They offered their shares to their customers first and it was oversubscribed. So they sold more than enough just to their customers, let alone investors.

Owen:
And so, I've always been excited by these companies, but I've always just thought, you know what, why don't I just wait until the second day and buy them on the stock market? There's no rush. I can pay, if I'm with a good broker, I can pay less than 10 bucks to buy them on the market on the day that they IPO or two days. I would probably wait. If you're going to buy shares, I'd probably wait a week or two, just because the first week is extremely volatile. Typically, [crosstalk 00:43:13].

Kate:
A lot of people that were involved in this whole process that are selling in the first week. So that's always something to keep in mind. And just always coming back to the, following the money and the incentives and being patient. They hype it for a reason. They write a compelling story. They have a lot of marketing material and investor events

and exciting things for a reason. And it's not always the truth behind the story. So just, be careful not to get caught up in the hype and the excitement of it all, because that's what the process is designed to make you feel.

Owen:
Yeah. Actually, speaking of interviews, I interviewed Rob from ... he's a co-founder of Cobram Estate olive oil, for the Australian Investors Podcast as well. It's been posted on Rask Media, if you're interested in what makes good olive oil. But also a good business, a family first kind of business. Check that out, there's an interview there. We talked about basically what Cobram Estate does-

Kate:
And that's a very freshly listed company, isn't it?

Owen:
Yeah. That's only in the last couple of months. And Locklin wrote about that for Rask Media as well. So you can see his take on it. And basically, the reason that they IPOed was because ... Cobram Estate have been around for quite a long time. And over the years, their employees had been getting shares to keep them with the business. In fact, I think the two CEOs of Cobram, this is how long-term focused they are. They got options to get shares in their company, but they wouldn't get them unless they worked at the company for 10 years straight. [crosstalk 00:44:50]. So it was a 10-year earnout, and they got the shares. But then all of these employees at Cobram wanted to sell, so Cobram had to make a choice. Do we try and find other investors in the market to try and buy their shares from the employees, or do we go into the stock exchange? And that's what they did. They went onto the stock exchange, and now their employees can sell their shares and other people can buy. And that's why they did it.

Owen:
So that was a really interesting story too, and that was a positive story from an IPO. And I just bring it up as a positive way to end this. But we've done some work on some of the recent IPOs as well. For example, we took a look at PEXA Group, which is the biggest property set on the platform in the country. So if you buy a house these days, there's about an 80% chance that if you buy that house, it will be settled on settlement date by the PEXA platform. So you don't have to walk up with a suitcase of money and a contract in hand, it's all done digitally. And that's PEXA that does that. So our team inside Rask Invest took a look at that, which is heaps of fun. And what we discovered was pretty interesting about that IPO too. So, Kate, there's a lot of good stuff to cover in this. I know you're going to accompany this podcast with a writeup and heaps of resources. Right?

Kate:
Yeah, absolutely. And so if you are interested in learning more, I've got a lot of links in the show notes. And as well, I'll put it all into an article for you to have a look at, because it's definitely worth doing the research, especially in this area.

Owen:
Yeah. And although we come across ... particularly me, but we try to be balancing this and try to just slow you down. Because remember, long-term investing in the stock market is not exciting. Typically, it's boring. It's exciting to learn about the companies, but typically it's boring. You don't need to rush, you can take your time and just slowly buy shares and buy ETFs and do all that over a very long period of time. And really boring, but sustainable businesses. So try to avoid some of the marketing and the allure of a short-term game. If you're going to do it, keep it as a very small part of a portfolio and just remember that your long-term retirement isn't going to be made or broken by one IPO. But just be sensible with your investing. Cool. Kate, as always, absolute pleasure. Thanks for joining me.

Kate:
Thanks for listening.