MINORITY SHAREHOLDERS WATCH GROUP
BADAN PENGAWAS PEMEGANG SAHAM MINORITI BERHAD
(Incorporated in Malaysia – Registration No.: 200001022382 (524989-M))

New Straits Times, Business Times – Thursday, February 10, 2022 **(A)**

DEVANESAN EVANSON

INITIAL PUBLIC OFFERINGS

MINIMISING INVESTMENT RISKS

IT is difficult not to draw comparisons between MR DIY Group (M) Bhd and Senheng New Retail Bhd in the sense that both are visible retail stores dealing with consumer products.

MR DIY was listed on Oct 26, 2020 at an issue price of RM1.60 per share. The counter closed at RM1.75 on its maiden trading day, up 15 sen, or 9.4 per cent, from its initial public offering (IPO) price.

On Monday, the share price closed at RM3.60, representing a surge of more than 100 per cent since its debut on Bursa Malaysia.

In contrast, Senheng's IPO had a dismal debut on the Main Market of Bursa Malaysia on Jan 25. At the end of its listing day, it was down by 20.1 per cent, or 21.5 sen, to 85.5 sen from its IPO price of RM1.07.

On Monday, the share price closed at 83.5 sen, a dip of about 20 per cent from the IPO price.

The market has a mind of its own when it comes to the valuation of a share.

The market's price discovery mechanism may not be fair by our standards and criteria but the market could not care less — it does not even know we exist.

It does not owe us a living, just like the investment banks and promoters and owners of companies that are going for IPOs.

During an IPO, most promoters and owners try and maximise the valuation of their company for themselves — they do not owe us a living.

Sometimes, they leave some money on the table and IPO subscribers make some money during the IPO.

Whether an IPO will make money or not is not easy to determine as those who subscribed to Senheng will attest to. But there are some things that we can take into consideration to minimise the risks of investing in an IPO.

> *The market has a mind of its own when it comes to the valuation of a share. The market's price discovery mechanism may not be fair by our standards and criteria but the market could not care less — it does not even know we exist.*

Guidelines

Valuations are a guide but even this is not an exact science.

MR DIY was valued at 31.6 times its earnings per share of 5.06 sen for the financial year ended Dec 31, 2019.

Senheng, the consumer electrical and electronics retailer, was based on a trailing price-to-earnings (PE) ratio of 28.8 times based on its calendar year 2020 earnings.

On paper, Senheng went to the market on a lower valuation.

One should compare the IPO company's PE ratio based on the IPO price with the average PE multiples of the existing listed companies (its peers).

If a listed company is trading at a lower PE compared to the PE of the IPO company and the average PE of its peers, then it makes sense to invest in that listed company as it is undervalued as opposed to subscribing to the IPO.

Sometimes, it is better to invest in the devil you know than the angel that you do not know.

Apart from valuations, the other investment considerations are the listed company's position in the industry, its outlook and prospects, and business and growth strategies.

One must also take into consideration the utilisation of proceeds from the IPO. This indicates whether the money raised will be put to the best use possible — whether it is substantially to repay loan or for expansion purposes.

Warren Buffet speaks about "the moat" that a company can have. This refers to an advantage or a protection (hence the "moat") that a company has that cannot be easily replicated by another company. This moat attracts a premium pricing from the market.

So, if an IPO company has such a moat, then it makes sense to invest in that company and price-earnings valuations may become secondary.

'Green shoe' option

One must also be aware if the IPO is subject to a "green shoe" option.

On Jan 11, 2008, the Securities Commission introduced an over-allotment option and price stabilisation mechanism to enhance the efficiency and competitiveness of the fundraising process for IPOs in line with international best practices.

The "green shoe" mechanism allows the issuer to over-allot securities in excess of the number of shares constituting the original offer size to ensure that the demand for shares in an IPO can be met in an efficient manner and that price volatility during the period immediately after listing can be minimised.

The mechanism can be used for any IPO where the total value of shares offered is not less than RM150 million.

It can commence on the date of listing of the issuer and continue to be carried out during the first 30 days of trading from the IPO date.

So, with a "green shoe" option, for the first 30 days, the share price will hover around the IPO price.

This is something of an insurance policy for successful IPO subscribers, a kind of "get out of jail free" opportunity.

So, if there is no overwhelming premium during the first 30 days of listing, the subscriber may wish to exit the company at about the IPO share price.

Again, one must hasten to add that such an exit approach is a short-term view approach that is especially suited for a "stag".

A "stag" is someone who buys shares in a company that are sold to the public with the intention of selling them immediately for profit.

Given the vagaries of investing in an IPO and the apparent subjectivity on how the market prices an IPO share on listing, some have sworn never to subscribe to an IPO but to consider investing after the share is listed — unless there is a strong overwhelming and persuasive "moat".

The writer is chief executive officer of Minority Shareholders Watch Group