
NAB kicks off Great Western stock sale

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OUT TO MARKET

Alibaba and the IPO genie

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It is something every West Perth-based exploration geologist, technology nerd or start-up entrepreneur dreams about — making millions from an initial public offering (IPO).

An IPO or share float is the first sale of company shares to the public and it is usually done to raise capital to expand, reduce debt or for working capital.

Large privately owned companies IPO to unlock wealth in an exit strategy for the founders or early private investors.

The Facebook IPO in May 2012 is a great case study of what can go wrong.

The stock fell as soon as it floated with valuations crashing more than 50 per cent over the first couple of months.

It took more than a year for the shares to trade above the $38 listing price, mainly based over concerns about its business model.

Since that early shaky start the stock has soared.

China's biggest e-commerce company, Alibaba set a record for IPOs recently, raising $US25 billion making it officially the biggest in history.

The market capitalisation of the online store is now more than $US220 billion, ranking it bigger than Amazon or Facebook.

The media have featured pictures of hundreds of cheering Chinese investors who became instant millionaires.

Alibaba founder Jack Ma, a former English teacher who had the idea in 1999, is reportedly now China's richest man with a fortune of more than US$15 billion.

IPOs typically close above the offer price on the first day of trading and go for massive runs in share price in a phenomenon known as a "price pop" or "stag".

Twitter, for example, increased by 80.7 per cent to $US47, a day after the float at $US26 per share.

The technical term for this is initial under-pricing.

First-day price pops were unusually high during the dot com bubble, when the typical pop was 65 per cent of the offer price, well above the 7 to 15 per cent range at other times.

Interestingly, Alibaba whose first-day price pop was 38 per cent, hasn't developed any disruptive technology or created any breakthrough new product, it's just brought sellers and buyers together online.

The difference between Alibaba and internet IPOs of the dot-com mania days, when investor psychology allowed companies yet to show a profit to trade at high prices on unrealistic hopes, is that the company generates revenue from its business model.

In fact its internet network model creates $US2.5 billion in annual revenues and about $US2 billion of that is profit.

The reason Alibaba's IPO was so successful was massive pre-IPO hype, the whole China growth story and the fact only 4 per cent of the offer was available for retail investors, and this $US1 billion did not even dent pent-up demand for the internet stock.

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