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WHY DO COMPANIES GO PUBLIC (IPO)?

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Abstract

This work is devoted to the study of the reasons for the company's IPO. Based on the bibliographic analysis, several reasons for the company's IPO were listed and the answer to the question "Why is going public so important" was received.

Keywords: initial public offering, going public, issuance of shares, prestige, and reputation of the company

An initial public offering (IPO) is an important step in the development of a company. With the help of this tool, the company not only acquires the status of a public company, but also receives many benefits and advantages. Among them, one can highlight access to the capital of a wide range of investors, obtain an assessment of the company's market value, and increase its capitalization, improving the image, prestige, and reputation of the company. The term fully reflects the essence of the event:

– "initial" indicates that the company's shares are entering the stock market for the first time.

– "public" means that they are made available to an unlimited number of bidders.

In fact, after an IPO, a private (closed) company, whose capital was previously made up solely of contributions from the founders/owners, becomes public. Primary placement can be carried out by both newly created firms and those that are well known for a long time. The only requirement they have in common when conducting an IPO is that the issuer's shares have never been publicly offered before.

Primary placement, as a rule, has several purposes:

– Raising funds on favorable terms. Share capital - gratuitous receipts, it can be used by the company for any purpose (in some cases they are stipulated in issuance documents). In addition, the transformation of a company into a public company, as a rule, greatly simplifies access to credit resources and reduces costs.

– Fair assessment of the company's value, and capitalization maximization. The price of shares on the market, as a rule, tends to be fair, which reflects the efficiency of the issuer, and its financial and production indicators. Naturally, with an increase in the price of an asset, both the total value of the company and the absolute expression of the share of each shareholder (co-owner) increase.

– Increasing transparency, recognition, and growth of rating indicators. With the growing demand for securities from investors, the popularity of the company is growing. In addition, publicity implies regular checks with the publication of results and the disclosure of information.

Entering an IPO includes a number of mandatory activities:

1. Decision-making. At this point, a complete analysis of the activities and structure of the company is carried out, and the possible benefits and risks of the public offering are calculated.
2. A list of participants (underwriters, bookrunners) is determined, an exchange floor is selected, a memorandum is drawn up and published, and an advertising campaign for investors (roadshow) is carried out.
3. The starting price of the asset is determined, the basis for which is the collection of applications from investors.
4. Start of trading.

An IPO is an important step in the development of a company. The company is pushed to issue not only by the natural growth of the organization itself, but also by other important reasons.

Gaining access to capital from a wide range of investors is one of the most frequently cited reasons for companies to go public. Due to the fact that the issue of shares does not create a debt burden, the company does not need to return the funds raised or pay interest on them. In addition, the company can use the attracted capital for further expansion and those goals that the management sees and sets for itself, taking into account the interests of investors and shareholders who have allocated their funds for the implementation of this strategy. Also, a new source of financing helps the company reduce the amount of debt on previously attracted bank loans and thereby reduce financial leverage.

Raising funds enables the company to finance long-term investment projects, which increases the company's capitalization, and leads to an increase in its value on the stock market, increasing liquidity and attractiveness for investors.

The next important reason is to improve the image, prestige, and reputation of the company. Obtaining the status of a public company makes it easier to establish relationships with counterparties. The ability to establish commercial relations is especially important for those companies that seek to enter Western markets and whose reputation plays an important role for Western partners.

CEOs of companies often cite the desire to enhance the company's image and reputation as a motivating factor when entering an IPO.

Marchisio and Ravasi conducted a survey among the leaders of Italian companies that had recently gone public. The third and fourth most popular reasons for IPOs were to improve the image and reputation of companies, as well as to increase their attractiveness to investors. Rydqvist and Hogholm analyzed prospectuses and found that in 67% of cases the desire to improve the company's reputation was the reason for entering the IPO.

The issuance of its own shares in an IPO enables a company to obtain an instrument to pay for takeovers of other companies. Often large companies grow through acquisitions of competitors and smaller companies - an approach that is common among technology companies in the US, for example. Google and Facebook buy startups every year to launch new projects and support existing ones. When buying, one of the forms of payment is not only cash, but also shares of the parent company. In addition, through the issuance of shares, a company can attract and retain talented employees by offering them an Issuer Stock Option in the form of a bonus, which can be monetized after a certain number of years in the company. This method is especially relevant for growing companies and those companies that are not able to pay high wages to employees at the moment. However, in the event that the company does not develop or the share price does not increase, then the option will not have value for the employee.

Another reason for the company's IPO may be the desire of shareholders to diversify their portfolios. Diversification can be achieved by directly selling the shares of the IPO company or by using the capital raised in the IPO to buy shares in other companies.

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