

## **15<sup>th</sup> China International Finance Forum, Shanghai 15 and 16 December 2018**

### **Session 6: Overseas Stock Listing Summit**

Alex Erskine, Managing Director and Founder, Erskinomics Consulting Pty Limited, and former Chief Economist, Australian Securities and Investments Commission 2007-2013.

#### **Overseas financing and stock listing**

##### SLIDE 1

Thank you for the invitation to address this Overseas Stock Listing Summit, an important part of the 15<sup>th</sup> China International Finance Forum. I am delighted to be here, but I must read a disclaimer: What I say today are my views. I am not speaking on behalf of my former employers such as the Australian Securities and Investments Commission (ASIC) or Citibank. Nor am I giving general or specific advice – please pay for your own from a professional adviser.

I will talk about many aspects of overseas financing and stock listing. First, the opportunity. Second, the path of investment and financing. And third, listing in Australia.

##### SLIDE 2 Topic 1 The Opportunity

The opportunity is so obvious. Overseas financing through stock listing raises new equity capital, enabling the company to reduce leverage and take out some insurance against all that can go wrong in the future, either abroad or at home.

If a company has a strategic plan that requires cross-border growth, wants improvements in the way investors view the company and seeks a wider group of investors to support the company, overseas financing and stock listing should be considered.

##### SLIDE 3

There are two ways a company domiciled in say China can list shares on an overseas exchange such as the Australian Securities Exchange. If they are not already listed in China, or elsewhere, they can apply to list new shares in an Initial Public Offering (IPO). These would then be called N-share companies in China. The other way – if they are already listed in China – is to cross-list the same shares in Australia. We will look again at the mechanisms later in a more detail.

##### SLIDE 4

Chinese companies have taken to issuing equity in foreign markets with enthusiasm. The table shows share issuance for the 25 years from 1990 until 2014 for issuers from 25 emerging market countries. It is from a very recent World Bank working paper. Of the 17,682 issuers, 3,445 are from China and 14,237 from 24 other emerging markets. It shows high annual issuance and issue size for Chinese companies in both domestic and foreign markets – and, compared to other issuers, especially in foreign markets. The cross-border issues have mainly been on US and European stock markets.

##### SLIDE 5

## CHECK AGAINST DELIVERY

If common sense were all that matters, I would think that cross-border listing is an area of finance that seems almost certain to grow in future. Most financial development is already excessive – too much debt, but not enough equity. Surely more cross-border listings are needed?

There are advantages and disadvantages of cross-border listing. A few years ago, the focus was much more on the column of advantages. But now the practical advantages and disadvantages – the pros and the cons – of an overseas listing seem to be more equal than before. Now the academic studies are more mixed, more uncertain about whether the benefits exceed the costs.

### SLIDE 6 Topic 2 The path of investment and financing

Faced with these uncertainties and more difficult conditions, companies have to be both strategic and opportunistic if they want to get the benefits of an overseas listing. The path of investment and financing has to be first about the company – because it will need a story to persuade the investors to buy – second about choosing the right stock market on which to list (the market that has the right balance of size, turnover, investors and regulations) and third about deciding quickly to issue when the conditions are favourable.

### SLIDE 7

You would think the outlook for cross-border listings would be – and should be – excellent. I present two examples to show the actual performance has not been good – it has not lived up to the promise.

First, cross-border equity raisings are still a most minor part of overseas financing and financial flows. Most overseas financing involves banks, sovereigns and portfolio investors, not corporates, not FDI, and not cross-border equity raising. See BIS Working Papers No 760 Gross Capital Flows by Banks, Corporates and Sovereigns 2018.

And second, the title of the World Bank's latest Global Financial Development Report is Bankers without Borders. Equities again play a minor role in cross-border funds flows that the report tracks. I think it is going to be a long time before there will have been enough cross-border listing and associated equity flows to have a future Global Financial Development Report titled Stock Brokers without Borders.

### SLIDE 8

The modest upsurge for Chinese companies listing – at least in Australia – seems to have already come to an end. I think around 50 – 70 Chinese companies in all have listed at some time, but not all are listed now. In the last two years there have been hardly any new listings of Chinese companies, some have de-listed and several applications have been rejected. The issue appears to be compliance with disclosure and other requirements.

Chinese companies seeking to list in future will also have to contend with sceptical investors – returns on the Chinese equities listed during the last decade have been comparatively poor.

### SLIDE 9 The downward spiral

But it seems all cross-border listing and financing – not just in Australia – is becoming even more difficult. I have put 4 factors on the screen.

## CHECK AGAINST DELIVERY

First, we are entering a phase of the economic and finance cycle when interest rates have been increasing. Equity markets have been shaken and are still shaking. If you had thought of raising debt or equity capital in the low-interest rate era but didn't, now it will cost you more.

Second, we are also going through a period of re-regulation, with increased focus on taxes and transparency and disclosure. This complicates any cross-border business, including listing and maintaining those listings.

Third and fourth, there is a re-thinking about the 70-year trend towards increased globalisation and economic and financial integration. Not only is the UK seeking to negotiate its withdrawal from the European Union; but also the US and China are engaged in a trade war.

Of these, it is my fear of a full-scale trade war that has me on the edge of my seat ... look at the chart on the right of the slide. To me, it is the most terrifying graph in economics. It shows month-by-month how world trade spiralled downwards when the US and Europe engaged in a trade war in the 1930s. The trade war exacerbated the Great Depression, which only ended with the Second World War. I thought we had learned from that, but obviously not.

I could mention more gloom. Some say globalisation and finance are at the crossroads – we will have to wait and see.

### SLIDE 10 Topic 3 Listing in Australia

So now to the third and final topic. Listing in Australia

I emphasise that I am not giving an official view, just my own interpretation. The Australian Stock Exchange and the Australian Securities and Investments Commission both look forward to more foreign companies listing in Australia. But they do want higher-quality companies than some of the ones that previously listed. The requirements facing issuers have been raised, tightened up.

### SLIDE 11

Australia's stock market is not the very largest, but it is still large, on some measures the 14<sup>th</sup> by market capitalisation. It has several attractive features.

The market capitalisation of the ASX is just under A\$2 billion. There are over 2000 domestic companies listed, and 137 foreign-origin companies. China is the origin of the largest number of the foreign companies that are listed.

What is perhaps most attractive about Australia is that the benefit of several decades of sound macroeconomic policy – low inflation, budget balance and a floating exchange rate – as well as sound prudential regulation and pursuit of market integrity. These conditions have led to more than 25 years of sustained economic growth and also have allowed a very large pension fund sector to develop (what Australians call superannuation) as a result of government compulsion. The superannuation pool of funds is by now quite large, at A\$2.5 trillion, and is set to rise for several decades yet.

### SLIDE 12

Not only have the superannuation funds grown very rapidly, perhaps the most attractive aspect for an issuer is that the pool of superannuation funds are invested substantially in equities. This is a logical

## CHECK AGAINST DELIVERY

consequence of Australia's pension schemes mainly being Defined Contribution funds, rather than Defined Benefit funds.

### SLIDE 13

The rules for the listing of Foreign Incorporated Companies are readily available from the Australian Securities Exchange (ASX). They include an option, to apply:

- under a so-called profits rule, or
- under a so-called **assets test**.

The assets test is more suitable for companies that do not have a sufficient track record as a viable business.

No matter which test is chosen, the applicant must achieve a **minimum "free float"** of 20% or more of its shares, and a **"spread test"** of at least 300 non-affiliated security holders with shares worth A\$2,000 (or more).

There is a different set of requirements for larger more established companies, under the Foreign Exempt Listing rules, *if* they are listed on an acceptable exchange (e.g. Hong Kong – I haven't seen a company being exempted as a result of its listing in Shanghai).

No matter which route you or your clients wish to take, do get your own professional specific advice. There are Australians in Shanghai or Beijing who may be able to help.

### SLIDE 14

Of course, in achieving your listing and maintaining that listing thereafter, there are – and will always be – significant on-going market integrity obligations, especially around continuous disclosure. These obligations are spelled out in the Listing Rules and Guidance Notes of the exchange, the ASX, and in the laws and guidance provided by the Australian Securities and Investments Commission, ASIC.

I have highlighted an ASIC report RG521 Further Review of Emerging Market Issuers, published in April 2017. It in turn built on many concerns about the impact of emerging market issuers on Australia's market integrity (see RG368 Emerging Market Issuers August 2013). ASIC is bound to persist with its focus on market integrity.

Australia does want foreign companies to list. The quest for rising standards applies to all issuers, foreign and domestic. If I were a potential Chinese issuer seeking listing on ASX, I would want to be the best issuer I could be.

### SLIDE 15

So it may be the right time to start planning a cross-border listing in Australia. Do think of starting now. By the time you are ready, the world may have got over its present challenges and conditions for issuing may be more favourable.

Thank you. I wish you the best in these very interesting times.