IPO market is back

Sentiment expected to remain positive in short term, but valuations may prove dampener in long run

Leong Chan Teik

SHARERS of China company Hengxin Technology, which makes cables for the telecommunications industry, rocketed 14 per cent last week on their debut on the Singapore Exchange.

Some, hotel group Banyan Tree will offer its shares to the public. The separation of companies is between seven and 12 times earnings and earnings per share.

Both factors are important. In terms of profits generated. Share price to earnings ratio, the better value the share price since the start of the year.

Mr Tan, president of the Securities Investors Association of Singapore (Sias), says: "Investors should be careful if the IPO fever continues. It may be time to take profits."

But pricing is also key. "Most IPOs are still underpriced at between seven and 10 times earnings," he says. "The better value the share price in terms of profits generated."

"Investors should be careful if the stocks are rushed up subsequently to exceed the market average of 15 times earnings," he adds.

Mr Tan of Philipfi re reckons that as market enthusiasm over IPOs continues to develop, companies aspiring to list their shares will demand higher valuations, which in turn will exceed market averages.

"Already, it is happening. He notes the best performing Chinese companies that were listed last year - China Shipping Spreader, China Oil Chem Fibre and Longcheer - sold their IPO shares at between five and eight times earnings per share."

This year, companies with similar sales and profits - such as Gabus Bio-Chem Technology, China Milk, Sun Gas and Indian Chemical group - sold their shares at between seven and 12 times earnings per share, he says.

If the IPO fever spreads, something else happens: a rapid succession of companies will launch IPOs.

Investments will not have the time or resources to quickly differentiate between good-quality IPOs and the lesser ones. "In 2000, many technology-related stocks performed badly because they could not be differentiated by investors due to too many IPOs," says Mr Tan.

Mr Terence Wong, chief investment analyst at Sal Retail Research, agrees that the IPO fever will cool down eventually, and suggests that investors sell any IPO shares which are no longer bargains.

"The valuations of many recent IPOs have run ahead of business fundamentals. It may be time to take profits," he says.

Investors should take such factors as the price-earnings (PE) ratio, which is the ratio between the share price and the profit, the value of a company's assets per share, and price-sales ratio, which is likely to increase, except that it looks at revenue instead of profits.

Impact of foreign listings

On MAY 5, a milestone was reached with the listing of the 100th Chinese company, plastics firm Midshott, Holdings, on the Singapore Exchange (SGX). SGX aims to attract more foreign companies, especially from China, to list in Singapore.

"More IPOs are good for Singapore retail investors if the companies are of good quality. They enable investors to profit from booming businesses in foreign places, and diversify their investments."

"Quantum leaps in their revenue and earnings are not uncommon," says Mr Wong of Sun Research.

IPOs enrich the variety of stocks that Singapore retail investors can invest in. Consider Pahh, a China company which makes explo-sives for use in hydro-electric con-struction and oil exploration.

Its shares have shot up from the IPO price of $2.60 cents last month to 91 cents on Thursday.

Investing in IPOs, however, is as troublesome to rail with.

Mr Wong describes the basic challenge: "IPO investors should have a good grasp of the business as well as valuations of their investments."

He adds: "Do not ever buy even if the company possesses solid fundamentals."

But to begin with, it is a challenge for Singaporeans to gain a good understanding of foreign businesses such as those that make textile fibres, soybean products and agricultural equipment.

"Many businesses can be difficult to understand unless one pays regular visits to China or gets constant updates from management," says Mr Tan.

To complicate matters, it is never crystal clear how a business' solid fundamentals may last.

What is obvious is that companies tend to launch IPOs during the good years. And typically, an IPO is one big job as the company in question calls on potential big investors and organizes press conferences to put the best possible spin on its prospects and latest rosy earnings, says observers. Post-IPO, the business and stock performance can range from exhilarating to depressing.

Consider two IPOs from last year: The shares of Yatai Technologies, an Israeli maker of products that pro-