Innovators drove the markets – what drives them now?

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Capital markets bankers have spent much of the last five decades dreaming up products to help clients and themselves make money, but is process, which has largely taken a back seat, now becoming the battleground?

…..Even Eric Dobkin, the Goldman Sachs veteran known as 'the father of the IPO', agrees that the way in which equity offerings are done today is much as it became after he and his generation had set about transforming equity capital markets execution in the 1980s. Have outcomes got better? There is little evidence of that……After about 40 years of international equity offerings, deals still get pulled at the last minute or else trade appallingly after being mispriced. Practice has not made perfect, which suggests that either it is impossible to improve outcomes or it is possible but the answer has not yet been found or the incentives for bankers to do so are entirely missing…….

<u>One firm trying to fix at least some of these issues with a rare example of process innovation in equity capital markets is STJ Advisors, which celebrated its 10th anniversary in 2018</u>. STJ argues that it is uniquely positioned as a non-competitor to the banks that manage equity offerings and that it is able to collect data from those banks that usually would not be prepared to share it with others.

By collating that data and then mapping and analyzing it in multiple ways, the firm can divide the target account base between the banks in the syndicate with precision, with the aim of making the marketing effort considerably more widely spread and efficient than might be the case if banks were left to their own devices.


John St John, STJ Advisors

This is partly because of external factors. "Commissions are down 95% in 20 years, so there has been a huge contraction in the number of accounts that banks cover," [founder John] St John says.

There also came to be a greater reliance on the participation of hedge funds as they emerged in the 1990s, although the performance of deals once more than about 25% has been allocated to hedge funds suffers rather predictably.

The concentration effect, whereby deals are now controlled by a small number of firms that focus almost exclusively on a small number of accounts, is what St John thinks hurts deal performance.

His aim – bringing the effort back into distribution so that every firm working on a deal is motivated to sell to a select group of accounts where it claims to have its best relationships – echoes Dean's complaint about how the market has shifted.

And, after doing about 120 IPOs at his firm, St John reckons he has the statistics to back up his claim. He defines an IPO failure as being it not pricing when scheduled after the announcement of an intention to float – unless the Vix [the Cboe's volatility index] is above 28.

Curiously, no European IPO has ever priced when the Vix is above 28. On that basis, he says failure rates on IPOs in Europe are getting worse, rising from about 20% of deals about five years ago to 40% in the last quarter of 2018.

Pricing performance on STJ offerings looks more controlled, which St John puts down to the more stable foundation provided by the broader account base of long-term investors who understand the equity story.

The first-day performance of his deals in the last five years has ranged from plus 10% to minus 10%. The market as a whole ranges from approximately plus 50% to minus 50%.

ECM bankers still like to complain about St John's methods, even 10 years on, given the workload that it involves and the control that it removes from them. Off the record, however, some give him more recognition than they are prepared to do in public.

"What he is doing is unique – he's well ahead of the mob," says one. "His database is unparalleled in terms of what accounts are doing, what they have participated in the past and where the relationships between individuals are."