MEASURING IPO SUCCESS IN NAIROBI STOCK EXCHANGE (NSE)

With Kenya Initial Public Offering (IPO) market beginning to show signs of recovery, with Nairobi Stock Exchange (NSE) warming up for both KENGEN (Kenya Electricity Generating Company) and Equity Bank IPOs it's important to remind ourselves of how to measure IPO success as investors. The double-digit first day jump in share price celebrated as the measure of success for an IPO must be re-examined and replaced by metrics that include longer-term vision. As IPO market recovers one common indicator of success that many IPO watchers continue to apply is the increase in share price on the first day of trading. Some considered a two-digit increase to be the measure of IPO success. Others drew a benchmark from so called daily doublers or IPOs that doubled their share price on day one. True an argument can be made that some measure of underpricing is appropriate compensation for first-round investors who face levels of risk that they would not face for secondary offerings. But even then from the perspective of issuing shareholders, an excessively first-day jump should be viewed as a measure of mispricing and failure of an IPO rather than as a measure of its success.

How should IPO success be measured? While there are obviously large differences in the number and types of activities involved in the intricacies of IPO situations the practical way to measure an IPO's success that eschews the goal of a huge first day leap in share price is viewed more in valuable metric because it takes unto account a company's longer-term competitiveness and the degree to which both new and existing shareholders are fairly compensated.

The IPOs success can be measured from two angles. First is market competitiveness, which involves relative company value equal to or higher than industry peers. Within 30 days of the IPO the company's market capitalization should be at or above the level of its industry peers. For companies in banking and financial services for example relative company value may be measured as market-to-book value of equity. For industrial companies multiples such as market value of equity over earnings, entity value over EBITDA or cash flow may be more appropriate. This relative value expresses a company's competitiveness in the capital markets. Investors can thus use it as guide to better understanding a company's continuing ability to attract funding. Second is the market pricing which should be less than 20 percent change between offering price and 30-day post-IPO market capitalization. Only an offering price that reflects the market value of the assets sold ensures that both new and issuing shareholders are fairly compensated. Market value should be measured 30 days after an IPO to allow the market time to fairly evaluate the assets on offer. IPOs measured are supposed to be both competitive in terms of relative value with industry peers and offered at a fair market price.

It's important to note that there are several reasons which might prompt a company to make a decision to issue an IPO.Companies might issue stock to finance investment opportunities, yet this in itself does not justify Initial Public Offering (IPO) since bank loans or private equity placements could equally well fill a need for funds. Morever investments by firms does decline after IPO thus decision to go public is likely driven by other reasons. It's equally important for investors to understand that investing at the pre-IPO stage can involve significant risk for investors. Pre-IPO investing involves buying a stake in a company before the company makes its initial public offering of securities.

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