Going Public in China

The Shanghai stockmarket opened in December 1990. Since then, more than 1600 Chinese companies, including many state-owned businesses, have listed on either the Shanghai or Shenzhen exchanges. In the boom year of 2007, there were 124 initial public offerings on the Shanghai exchange. These raised a total of $65 billion, nearly double the proceeds from offshore IPOs by Chinese companies.

Until 2000 China operated a quota system in which the regulator stipulated the total number of shares that could be issued each year and approved each individual application. Once the quota was filled no further issues could be made. The regulator also required firms to price new issues by multiplying earnings per share by a multiplier which was always fixed far below prevailing market P/E ratios. Not surprisingly, therefore, new issues proved very popular and provided very high initial returns (see Figure 15.3). The record initial return during these early years was a mouth-watering 38,000%. These restrictions on the IPO market have been progressively relaxed, and China has moved toward a more market-driven pricing process.

Although the bookbuilding method is used in China, the majority of IPOs are sold by a public offer. In this case the company states the price at which it wishes to sell stock and invites applications from investors. If, as often happens, there is an excess of applications, investors are chosen by lottery. In case there are not enough applications, the company generally arranges standby underwriting, whereby a group of institutions receive a fee for agreeing to buy any unsold shares.