Greenhill & Co. Australia Pty Limited
Level 34, The Chifley Tower
2 Chifley Square
Sydney NSW 2000
(61) 2 9229 1410
(61) 2 9231 3793 Fax
www.greenhill.com
ABN 89 086 678 346

Greenhill

24 October 2012

Regulatory and Public Policy
ASX Limited
20 Bridge Street
SYDNEY NSW 2000

Attention: Ms Diane Lewis

Via email: regulatorypolicy@asx.com.au

Greenhill Comments on ASX Bookbuild® Initiative

Thank you for the opportunity to comment on the proposed ASX Bookbuild® initiative. Our comments are available to the public.

An assessment of the merits of ASX Bookbuild® requires three things:

1. identification of the standards that should be used to benchmark bookbuilds in Australia;
2. an assessment of whether and how the current process for conducting bookbuilds in Australia might fall short of that benchmark; and
3. an assessment of whether the current or an amended form of ASX Bookbuild® can overcome those deficiencies, and potentially provide other benefits, without increased cost or risk.

In order to do this our comments are structured as follows:

Section 1: Greenhill's Experience in Australian bookbuilds, providing the background to our comments;

Section 2: Assessment of Benchmark for Bookbuilds in Australia, and Shortcomings of Current Practice

Section 3: Assessment of Benefits of and Concerns With ASX Bookbuild®

Section 4: Recommended Adjustments to ASX Bookbuild® to Overcome Concerns

Section 5: Issues on ASX Bookbuild® Requiring Further information; and

Section 6: Responses to the Five Specific Questions in the Consultation Paper.

In summary, we believe the benchmark for bookbuilds and other capital raising initiatives is whether all decisions in bookbuilds are made in the interests of the issuer's current shareholders.

The current process is not fundamentally flawed, but it often leads to decisions being made without due focus on current shareholder interests. This increases the costs and risks of offers and can transfer value from those shareholders to other parties.

ASX Bookbuild® can create greater transparency and thereby help reduce these risks, but a number of ASX Bookbuild®'s initial parameters should be changed to reduce the risk of increased market instability compared to the current process.

Section 1: Greenhill's Experience in Australian Bookbuilds

Greenhill is a leading independent corporate advisor. We began in Australia in 1999 as Caliburn Partnership, and are now one of Australia's largest independent advisors. Our clients include Governments and major companies who regularly seek our advice on equity capital market transactions, including bookbuilds.

Our team members have been advising on bookbuilds in Australia for over 20 years, and have advised on many of Australia's largest and/or most complex bookbuilds and equity offers. The team's experience includes helping design and implement Australia's first bookbuild (the $1.2 billion IPO of GIO), Australia's largest bookbuilds (the Telstra sales), Australia's first announced back-end bookbuild (AMP in 2003), and Australia's first blind-date block-trade bookbuild (BA's Qantas stake).

Our experience covers all types of bookbuilds for shares issues and sales, and all aspects of them. We have advised on:

- bookbuilds for IPOs (such as Westpac's IPO of BT Investment Management),
- bookbuilds for broadly marketed secondary offers (such as the Commonwealth Government's $15 billion Telstra 3 selldown),
- bookbuilds for accelerated placements (such as Lihir Gold's $550 million non-underwritten placement),
- bookbuilds for renounced rights (such as Santos's $3 billion rights offer and Super Retail Group's $334 million rights offer),
- bookbuilds combining placements and sales of renounced rights (such as the AMP IPO and Lihir Gold's underwritten $1.2 billion 2009 placement and rights offer)
- bookbuilds that are volume-only (such as Tischman Speyer's IPO); and
- bookbuilds for block trades (such as BA's $1 billion sale of shares in Qantas).

Our work on bookbuilds includes advising on size and structure, as well as mechanics, costs and benefits. We work with issuers to determine the best means to underwrite, document, market, manage and settle sales of shares through bookbuilds so that shareholders' interest are protected through reduced risks, reduced costs and best quality outcomes. Most importantly, we sit in the bookbuild room with the issuer and its bookrunners at the end of a bookbuild to determine price and allocations.

Greenhill is not a broker. We do not earn commissions through share trading, and we do not seek to profit by trading as principal in shares issued by our clients. Our only focus in bookbuilds is to ensure our issuer clients and their shareholders achieve the best outcomes.

Our depth of experience and independent perspectives are potentially a unique platform for comments on the Consultation Paper.

Section 2: Assessment of Australian Bookbuild Practices and Benchmarks

2.1. The Standard by Which Bookbuilds should be Benchmarked

Greenhill believes the benchmark for all decisions in all capital raisings, including bookbuilds, is whether they will maximise the interests of the issuing (or selling) company's shareholders. This means achieving the best possible outcomes for existing shareholders at the lowest acceptable costs and risks. Specifically, it is the interests of the current shareholders taken as a whole, not solely the interests of the proposed new shareholders.

Our approach was summarised in the Guide that we published in 2010 to help directors of Australian companies understand some of the intricacies of Australian capital raisings, including bookbuilds. The Introduction to that Guide states:

> *"Directors need to act in their shareholders' interests when they issue or buy back equity, but this is more easily said than done. Australian companies now have access to a broad range of capital raising structures, and new ones continue to emerge. These structures can be effective, and their neat acronyms make them seem user-friendly. Most are quite complex, though. Their complexity can cloud a number of issues affecting shareholder value because different balances of cost, risk and reward are created for shareholders. Value can be transferred between groups of shareholders, or even away from shareholders. Directors and companies can be exposed to different risks, and intermediaries can be driven by different rewards….*
>
> *Shareholder interests cannot be safeguarded unless all these issues are clearly understood."*

A copy of this Guide is being sent to you separately. It is Confidential and not for public release.

Transparency, fairness and integrity are referred to in the Consultation Paper, and they are important matters which can materially impact shareholders' interests. They are not, however, the fundamental issue in assessing whether a capital raising is conducted to the appropriate standard.

As discussed in Sections 2.4 and 3, ASX Bookbuild® involves a number of complex processes and comes with its own maze of neat acronyms. We have assessed these processes as best we can to determine if shareholders' interests might be further enhanced if issuers use ASX Bookbuild® rather than the current off-market process in Australia.

2.2. Current Perceptions of Australia's Bookbuilding Process

For some 20 years bookbuilds in Australia have been conducted off-market, usually under the control of one or more global investment banks or brokers who act as the bookrunner(s). These bookbuilds have enabled Australian companies to price and allocate hundreds of billions of dollars of new capital, and they have benefited from the flexibility in offer pricing provided by bookbuilds given the risk of market movements over the potentially lengthy Australian offer periods. There is no reason to believe the prices achieved in these off-market bookbuilds have been substantially less favourable than those that might have been achieved in other sale methods, or that the costs have necessarily been substantially higher.

Given the volumes of capital involved, even small discrepancies in price, allocations or costs can however result in very large transfers of value away from current shareholders. Price-setting and share allocations are highly secretive processes in these off-market bookbuilds, however, and information on them is not shared by bookrunners. Often even the issuer does not know why particular decisions were made. In those circumstances, company directors often cannot confirm that all decisions were made in current shareholders' interests. Our own experience as advisor highlights the many occasions where bookrunner interests and current shareholder interests can and do conflict.

Generic descriptions of bookbuilds can be found in offer documents, but they are usually very general, and emphasise the bookrunner's absolute discretion in many matters, including pricing and allocations. As noted, the bookrunner is almost always one or more of the global investment banks, and there are numerous areas where a bookrunner's commercial interests can be different to current shareholders' interests. Concerns about a bookrunner's potential abuse of these discretions are reinforced as the Australian financial press highlights the alleged or confessed very serious failings of some of these global investment banks in various offshore markets.

Information on specific bookbuilds is almost never provided publicly, and often not even to the directors of the issuer. They and professional investors may receive information on the overall structure and possible pricing of a book while it is open, but not all professional investors receive the same information. Details of specific bidder intentions and individual allocations in any bookbuild are kept highly secret. This information provides a significant commercial advantage in identifying potential buyers and sellers in post-offer trading, so it is jealously guarded by bookrunners.

The general public receives almost no information other than occasional marketing messages which are designed to elicit bids rather than to inform the market. Occasionally the final outcomes of bookbuilds show that these messages were clearly not true, so they are all usually treated with suspicion. The first real information provided to the public is usually the final price, which is necessarily provided after the process has finished. It may be accompanied by general descriptions of the nature of bids and identity of bidders, but this is often dense technical jargon or market-related data that is easily dismissed as "spin".

Rightly, many investors and other market participants (including clearly ASX) are suspicious of this secretive "black box" process. It is neither transparent nor well understood. The controllers of the process are not widely trusted, and shareholders have little reason to believe that they will be treated with fairness or integrity. There also appears to be no accountability for potentially misleading disclosures or other potentially unacceptable conduct.

The naturally raises concerns that minimum standards of corporate behaviour are not being met in Australian bookbuilds.

2.3. *Process Not Perfect - but not Fundamentally Flawed*

The general success of bookbuilds in Australia demonstrates that the current process is not fundamentally flawed. There is no suggestion that it is innately unfair or fundamentally lacks integrity. It is true that it has generated numerous examples of perceived or actual conflicts of interest. Clearly there have been decisions that were not in current shareholder interests, and bookbuild disclosures that may have mislead some investors. In our view, though, these concerns flow from inexpert decisions by issuers and their directors, rather than from fundamental flaws in the current off-market bookbuild process that make it impossible for issuers and their directors to meet the required standards.

In particular, we do not agree with the inference that the lack of absolute transparency means the current process is necessarily flawed or that bookbuilds are not being conducted in shareholders' interests. Bookbuilds are commercial price-setting mechanisms, and shareholder interests usually depend on the issuer achieving an optimal commercial outcome. It would most likely be disadvantageous to issuers and their shareholders (or sellers) if they had to provide full transparency while buyers had complete secrecy for their deliberations. This is a matter on which judgement must always be exercised in order to protect shareholder interests.

The area where Australian bookbuilds are most open to criticism is the concern that crucial decisions – particularly pricing and allocations - appear to be made in the interests of incoming shareholders, and not current shareholders. This is compounded by the concern that incoming shareholders are all clients of the bookrunner, so it is more focused on their interests than the interests of all current shareholders.

It is true that directors turn their minds to these crucial decisions, but they often lack any knowledge of the underlying issues or understanding of how decisions will affect current shareholders' interests. Their examination may well be only cursory because issues are presented by bookrunners as technical or trivial, even though they can cause substantial value-transfers away from shareholders. Indeed, directors often delegate crucial decision-making to intermediaries such as bookrunners because they have greater capital markets experience and an intimate knowledge of the relevant jargon. This is a risk for issuers because the terms of engagement for bookrunners only rarely stipulate the standard that bookrunners must apply in providing advice or making decisions. This means bookrunners only rarely see themselves as being contractually bound to act in shareholders' interests.

Reliance on advice from bookrunners – and even the delegation of authority to them - may have been a lesser concern in the past, but there have been significant changes to the business models of the groups which now usually take this role. These global banks increasingly require clients to accept that the banks have numerous commercial interests that often compete directly with the clients' interests. In effect they assert that their advice is not necessarily provided from a position of trust. Any judgement must necessarily be approached with greater caution when it is based on advice from a party that disclaims any such fiduciary responsibility.

We note in passing that the Australian Government, for example, has always been aware of this issue and specifically retained ultimate decision-making authority in all its bookbuild sales, rather than allowing a bookrunner to control decisions. The Government has also retained an independent advisor to ensure that it had the required insights when making its own decisions about protecting taxpayer interests.

2.4. Managing the Risk

The risk of conflicted or poor decision making within the current process can be managed relatively easily.

In our view issuers and their directors must simply confirm that they are responsible for all decisions and disclosures in bookbuilds. This would involve ASX requiring issuers to confirm that all decisions in the sizing, structuring, marketing, pricing and allocations in bookbuilds were made in shareholders' interests, or to explain why this was not done. This would be part of the information required before trading in the new securities could commence. Directors would be expected to have the technical knowledge and market understanding to provide this confirmation, including the ability to assess potentially conflicted advice from any party involved in the process, but could do this through the use of a sub-committee with members having the requisite experience and knowledge, and/or the appointment of specialist advisors.

In addition, any disclosure on the progress of bookbuilds should be recognised as a statement made by the directors in relation to the offer or sale of securities, and required to meet the standards otherwise applicable to such statements.

These simple and easily manageable steps would in our view immediately improve the market's confidence in bookbuilds. Directors would be much more likely to test decisions or any disclosure in advance, and much less likely to rely on potentially conflicted advice. The market would have greater comfort that all decisions in bookbuilds (even those taken in strict confidence) were being properly considered and made in the best interests of existing shareholders.

ASX should require this confirmation regardless of the type of bookbuild used. There should be no regulatory arbitrage between the current process and any new process.

Section 3: Potential for ASX Bookbuild® to Add Value in Bookbuilds

3.1. Potential value-Add of ASX Bookbuild®

We believe ASX Bookbuild® can make a significant contribution to improving the outcomes of Australian bookbuilds. It takes a number of important steps towards ensuring fairness and integrity in bookbuilds, and towards ensuring issuers recognise and endorse the parameters of a bookbuild. Some of the specific benefits it brings include:

- **Providing greater transparency**: by identifying the parameters that need to be evaluated in a bookbuild, ASX Bookbuild® draws attention to the skills and functions involved in bookbuilding. This means directors will focus on the skills they need to apply in protecting shareholder interests, and on whether their board does or does not have them. It will also assist the directors identify whether agents are supplying skills that are directly relevant to the process;
- **Broadening the pool of potential investors in bookbuilds**: by enabling clients of all brokers to bid in bookbuilds, ASX Bookbuild® should increase total demand for any offer. Under the current system bidders rarely bother bidding if they are not a client (or even a favoured client) of the bookrunner or member of the selling syndicate. Investors are usually concerned that their bid will not be accepted at all if the bookrunner has no capacity to settle with them, or that their allocation will be immaterial because they are not a priority client of the bookrunner;

- **Providing a framework where issuers must consider in advance the key pricing and allocations issues**: ASX Bookbuild® requires issuers to consider in advance the granular technical issues that will affect the outcome of a bookbuild. This creates a better opportunity for directors to reflect carefully on how these decisions may affect current shareholders' interests. Many directors have an awareness of the potential for various issues to impact value, but they are often raised by the bookrunner just before a looming deadline, so directors have little or no time to test whether the bookrunner's proposed solution is really in shareholders' interests In these circumstances advance consideration can only benefit existing shareholders; and
- **Providing a mechanism to recognise the importance of current shareholders in any issue**: Most Australian offer structures now allow directors to cater specifically for the interests of current shareholders, and this focus is continuing. The emergence of accelerated tradeable renounceable rights issues with back-end bookbuilds is a further step in maximising the level to which current shareholder interests are protected. ASX Bookbuild® has the capacity to ensure special classes of bidders are rewarded or protected, and this could include current shareholders. We note however that this mechanism requires further work, and this is one of our recommended adjustments to ASX Bookbuild®.

In order to minimise risks to shareholders, and to maximise its potential to add value to issuers, we recommend a number of adjustments to the parameters of ASX Bookbuild® set out in the Consultation Paper. These recommendations are set out in Section 4 of this Submission. In Section 5 we list several considerations which may lead to recommendations for additional adjustments once further information is available. Most recommendations can be addressed by changes to the parameters of ASX Bookbuild®. As noted above, one important recommendation is to add a parameter to include current shareholders as a priority group under ASX Bookbuild® (see Section 4.1).

3.2. Impact of ASX Bookbuild® without Adjustments

As set out in Sections 3.3 and 3.4 below, we are concerned that issuers using ASX Bookbuild® may cause less stable markets for their shareholders (compared to the position under the current off-market process) both before and after an issue in the absence of adjustments to its parameters.

In addition, we note that ASX Bookbuild® is only a technology platform, and a technology platform alone cannot ensure shareholder interests are safeguarded. It can provide an integrated logistical solution, and it can set out a checklist of parameters that must be considered in order for bookbuilds to be effective and fair, but it cannot make qualitative assessments of relevant factors. Even if ASX Bookbuild® is adjusted as recommended, issuers will still need to remain involved and focussed on shareholder interests.

Users of ASX Bookbuild® should therefore also be required to issue a statement of the nature described in Section 2.4 confirming that all decisions on bookbuild matters were taken by directors after due consideration and made in the best interests of existing shareholders.

3.3. Market Stability Ahead of an Issue For Users of ASX Bookbuild®

ASX Bookbuild®'s current inability to allow allocations to be adjusted in response to "negative" market behaviour may encourage a greater level of such activity for its users than for issuers using the current off-market process. This is likely to lead to less stable markets for users of ASX Bookbuild® if it is thought that they may raise capital at any time.

A simple example to consider is a potential short-seller. If a company is thought to need capital, and is a user of ASX Bookbuild®, funds could short-sell the company's shares (thereby exacerbating the company's predicament) ahead of an issue, knowing the company's own processes will help them cover their short in the offer, and probably at a discount to the disturbed market price. A raft of like-minded funds could even jeopardise the potential for a successful raising, which would clearly be contrary to shareholders' interests.

The Recommendation we make in Section 4 as a whole are intended to address this risk.

3.4. Market Stability After an Issue For Users of ASX Bookbuild®

ASX Bookbuild® requires all potential bidders, including traditional price takers such as retail investors or index funds, and those simply wanting to maintain a proportionate holding, to specify prices for their bids. They cannot lodge clearing price or strike-price bids, as they usually do in off-market bookbuilds. Their alternative is not to participate.

If they participate, these traditional "price-takers" are likely to bid high in order to be allocated stock. They will most likely lodge and maintain their bids without any close checking of the minute-by-minute pricing data on ASX Bookbuild® because they will assume others have done sufficient work to ensure the final bookbuild price reflects the likely market price. In other words, they will assume the bookbuild price is driven by detailed market analysis, not gaming or wishful thinking.

The current design of ASX Bookbuild® does not enable issuers to differentiate between bids whose pricing might be driven by gaming or wishful thinking, and those driven by detailed professional analysis. Detailed analysis is not perfect, and professional investors may not necessarily be better long-term investors than those applying less rigour to valuations, but it is strongly arguable that these bidders are better able to assess likely share prices than those who do no analysis. That means their bids are probably more meaningful in assessing demand inflection points. ASX Bookbuild®'s inability to differentiate between these bidder groups in allocations and pricing creates a greater risk that ASX Bookbuild® will over-price offers and have a greater level of post-offer underperformance compared to an offer under the current off-market process.

This concern is particularly relevant in IPOs, where there is no prior market guidance, and where retail investors will almost certainly bid (as they do now) at the upper-end of any indicative price range provided at the time of the offer.

The risk of a weaker market is also increased under ASX Bookbuild® because ASX Bookbuild® does not currently allow issuers to have regard to a bidder's history of market behaviour (such as normal invest size or holding period) in making allocations. This creates a greater potential for allocations to immediate sellers ('flippers") than under the current off-market process. It is a truism that any bidder – even a major long-only fund – might be an immediate seller of any volume of shares allocated to it even in the most carefully considered process. However, shareholder interests are not being protected if an issuer insulates itself from having to consider whether a bidder is likely to sell, hold or add to a particular allocation.

ASX Bookbuild®'s proposed Divestment Cap is a further risk to post-offer market stability. The cap is additional to existing statutory restrictions and limits in a company's constitution, so it can only lead to more selling. This is a further potentially material disadvantage compared to the current off-market alternative. Other concerns with this proposed feature are set out in Section 4.10.

As noted, Section 4 contains a number of recommendations designed to address these concerns.

Section 4: Recommended Adjustments to ASX Bookbuild®

4.1. Recognise Shareholders as a Separate Priority Category

Directors are required to act in the interests of their own shareholders, and this can be better done if they are recognised separately in bookbuilds. The current “priority” pool is inadequate because shareholder allocations could be seriously diluted through allocations to others who are deemed “priority”, such as sub-underwriters. It also fails to reflect the broader focus on shareholders that is evident in most other new issue processes in Australia.

RECOMMENDATION: Include “Current Shareholders” as an additional priority group. Subject to meeting bid size and price criteria, these bidders would be assured of receiving their proportionate allocation of the shares offered in the bookbuild. This would be an additional benefit: like any other bidder, shareholders would remain able to receive priority for price leadership, “priority’ classification or any other classification.

4.2. Allow Strike-price and Volume Bids

The volume of demand as well as the quality of price discovery information provided by ASX Bookbuild® will be enhanced if bidders can lodge price-insensitive bids. These could be bids for a total value or number of shares at the final price.

We believe this facility would increase total demand by allowing bidders to show their interest is volume, not price-sensitivity. This differentiation will also provide higher quality information to the issuer for use in the analysis of the final book of demand.

Allocations to these bidders may be proportionately less than for price-specific bids given the reduced level of information provided, but their volume contribution is important in any bookbuild, and they should be facilitated.

RECOMMENDATION: Allow “Strike-Price” or “Final-Price” bids, or bids for a set value or volume of shares. These bids would not be eligible for allocations based on price leadership, and may receive a smaller proportional allocation than price-specific bidders.

4.3. Allow Retail Investors to Bid Outside the Bookbuild

Price discovery is not assisted by forcing retail investors to lodge bids only though brokers and only at specific prices. We recommend that in IPOs in particular a portion of the total offer be set aside for retail investors, who would be required to subscribe off-market and to provide funds for all shares assuming the offer is priced at the top of the indicative bookbuild price range. Applications may be capped in size. The data on the offer displayed by ASX would show the coverage of the book assuming either the fixed allocation to the retail tranche, or potentially the coverage ratio (see Section 4.5) assuming different proportions of the offer might be allocated to these off-market retail subscribers. The indicative maximum and minimum proportions might be specified in the offer document.

In our view, total demand from non-professional investors will increase if they are not expected to assess prices like professional investors in order to bid. In addition, many retail investors prefer not to be forced to use a broker in order to deal with a company of which that they are (or intend to be) a shareholder. There is also a level of concern about investors being forced to fully fund a broker in advance of a bid, and to maintain credit risk exposure to that broker for some time.

The proposal to allow the market a minimum of just 10 minutes to respond to changes to the bookbuild parameters is relevant here. That proposal seems reasonable for professional investors, but is unreasonable for all others, including most retail investors who cannot be expected to check market announcements within such a timeframe. This function therefore points to the need to allow non-professional investors to bid for issues outside the ASX Bookbuild® market-based process. If this were not possible, it is arguable that the minimum acceptable timeframe would need to be potentially as long as one business day to respond to such changes.

RECOMMENDATION: Allow a portion of an offer to be allocated to retail investors, where those investors bid for those share separately. Investors should be made aware of the indicative coverage ratios assuming different allocations to retail.

The relevant offer document would need to specify the procedures to be implemented if bookbuild parameters were changed materially. These investors must also have a reasonable opportunity (measured by their own standards) to amend or withdraw their bid in these circumstances.

4.4. Enable Rewarding or Discouraging of Investors based on Non-Bid Issues

In the same way that some investors may warrant “priority’ treatment for their ability to protect shareholder interests (such as by facilitating the certainty of an underwritten offer), others may act or have acted in ways that damage shareholders, and should not be rewarded by participation in an offer. As set out elsewhere, examples of such bidders include short sellers, competitor corporations, corporate raiders and those known to lack the capacity or intention to maintain any allocation.

Pre-agreed formulae may appear more transparent than decisions in off-market bookbuilds, and this transparency may be equated to fairness, but they create the risk that issuers will not have the flexibility to avoid being gamed in ways that are contrary to shareholder interests. Directors need to have the capacity to avoid this. ASX Bookbuild® should therefore include the flexibility to allow directors to reduce allocations (potentially to nil) where appropriate, as well as the current capacity to reward “good” (or “priority”) bidders. ASX Bookbuild®’s current inflexibility in this regard is a material disadvantage for issuers and their shareholders compared to an off-market bookbuild, notwithstanding the purported “fairness” (although this is presumably fairness to potential investors rather than current shareholders).

The degree to which an allocation to any specific bidder should be reduced will always be questions of judgement, but directors must have the capacity to make these judgements and protect shareholders. It is unlikely an immaterial change to an allocation would affect shareholder interests, so the capacity may only apply to material changes to potentially material (in size) allocations.

The fact that market activity that is not in shareholder interests can be penalised or prevented may itself be a safeguard against such activity, including short selling ahead of an offer and flipping.

Potential corporate raiders and competitors should also be assessed by directors. These parties have the right to become shareholders at any time by buying on market, but shareholders would normally expect to benefit from the increased share price resulting from their buying. It seems contrary to shareholders' interests to allocate stock to these investors in a bookbuild when their bidding and allocations (or their exclusion) may well not be price-sensitive.

RECOMMENDATION: Enable an issuer to reduce (potentially to nil) the allocation to a bidder in a bookbuild under any allocation algorithm if that allocation (or the potential for such an allocation) is reasonably believed by the directors to be contrary to shareholders' interests.

4.5. Show Indicative Coverage Ratio at Base of Offer Price Range, not Indicative Price

It is proposed that ASX Bookbuild® show a live indicative bookbuild price to brokers (see paragraph 2.4 of the Consultation Paper) and therefore the market. This price is a function of bids lodged and the Excess Cover Percentage (ECP). The ECP is not disclosed, though, and can be varied at any time. We understand the ECP would be varied by an issuer to solve for an appropriate price.

This creates a real concern that the information conveyed by the latest "live" price may be confusing if not misleading. Changes in the "live bookbuild price" price may not reflect changes in bid pricing or bid volumes at all, but instead be due solely to a temporary revision of the ECP. In practice the "live price" could rise (indicating potentially greater bidder demand), when bids were being cancelled.

The ECP could also be easily gamed by bidders. They could lodge and then withdraw a series of bids and assess the price changes. Total demand at the price would quickly be known.

To avoid the use of potentially misleading or arbitrary data, and to provide more reliable information to the market, we recommend ASX Bookbuild® instead show a coverage ratio at the base of the issuer's indicative price range. Issuers could also choose to show the ratio at higher prices. This largely reflects current practice, and provides flexibility to issuers to raise, lower, widen or narrow their price range (and to show the relevant coverage ratio) in order for the issuer to signal potential final pricing. The most important consideration to bidders is always whether and at which price a book is covered, so they will have this fundamental data. Clearly they must then make their own assessment of the price they will bid in order to be allocated shares, but the strength of demand at the base price is a strong guide.

This coverage ratio should be shown in broader terms rather than as a highly specific number. This avoids the risk of gaming or back-solving, and still provides the data investors would expect to have. The ratio could simply be “Below (say) 125%” until the offer is covered by more than this at the base price, and then perhaps “Between (say) 110% and 150%”.

We believe transparency in bookbuilds will be better if disclosure is based on fundamentals, rather than on a variable that can be unilaterally changed in secret at any time, like the ECP. Issuers have the flexibility to amend their price range and to show coverage ratios based on the updated price range, so bidders can still be motivated to bid aggressively at appropriate prices. The publication of a broad range for coverage rather than a specific price also provides a buffer to deal with the fact that bids may be duplicated in the book (see Section 5.4) or allocations may be withheld (see Section 4.4).

RECOMMENDATION: Show an indicative coverage ratio at the base price for an offer and such other price points in the range as the issuer wishes, and do not show any calculation associated with the arbitrarily assessed ECP.

New coverage ratios will be published if an issuer adjusts the price range

4.6. Increase Data on Bidders Available to Issuers when Determining the Bookbuild Price and Allocations

Bidding data used to establish a bookbuild price under ASX Bookbuild® will be anonymous, except for the bids from “priority” bidders. It appears that no other bidders can be identified until allocations to them are in the settlement phase. This means issuers and bookrunners have considerably less information available to them than under the current off-market process. This creates a number of material concerns:

- Shareholder interests are not being protected as well if an issuer insulates itself from being able to assess whether bidders at different price points may have conducted greater or lesser levels of analysis. This is similar to the concern set out in Section 3.4 where issuers may set the size of allocations without being aware of a bidders’ potential investment horizons,

- Limiting the identified investors to “priority” investors means directors may have reduced understanding of broader market thinking because of the smaller number of parties involved, and increases the risk that these few investors can guide directors to a more favourable outcome by gaming their bids; and

- Even if there are numerous “priority” bidders, the information obtained by assessing their pricing may be of limited value because they are likely to be a similar-minded group which discussed the same information with the same bookrunner prior to their decision to sub-underwrite (if applicable).

Directors will naturally seek to assess the views of the broadest range of investors prior to setting a bookbuild price. Narrowing the subset of investors whose pricing views can be identified appears to undermine ASX Bookbuild®’s objectives of increasing the role of all market participants in bookbuilds, and of reducing the risk that bookrunners or issuers selectively favour specific groups in the process.

We therefore recommend that ASX Bookbuild® provide that a function whereby all bidders can choose to make their identity known when bidding, so they can choose to ensure the directors are better informed. In addition, directors could require a bidder to disclose its identity in certain circumstances. Issuers would have the capacity to stipulate their own level for disclosure (eg a minimum percentage of the offer, or a minimum dollar value, any bid that, when added to its current holding, would exceed a specified percentage of the company). These bids could still be considered if the bidder’s identity were not disclosed, but directors would have the right to reduce the allocation to either the disclosure threshold, or such lower number as they believed appropriate.

RECOMMENDATION: Adjust the bidding process so that bidders can disclose their own identity prior to the bookbuild closing, and so that issuers can require disclosure of the identity of any bidder seeking an allocation above a stated threshold. A party lodging multiple bids at the same price but in sizes below the disclosure threshold would be deemed to be manipulating or misleading the market.

4.7. Improve Functionality for IPOs

ASX Bookbuild® is currently intended for use only for IPOs and placements. We do not believe its current form would meet issuer requirements in an IPO. This is because its functionality does not allow it to ensure the ASX-required shareholder spread is achieved. This could be addressed by providing for minimum number and sizes of allocations, or more likely by allowing retail investors to subscribe for share off-line (see Section 4.3).

RECOMMENDATION: Increase ASX Bookbuild® functionality to ensure issuers in IPO are not potentially prevented from achieving the required spread of shareholders.

4.8. Provide Functionality to Cover all types of Bookbuilds

As set out in Section 1 and in the Appendix, there are at least seven different types of bookbuilds in Australia for share issues and sales, and a similar process is used for hybrid offers, as well as reverse tenders in some buy-backs. ASX Bookbuild® is currently targeting just placements and IPOs. As set out in Section 4.7, it appears to pose risks for IPOs, and its relevance in placements may be limited because many placements in Australia are made at a fixed price (ie without a bookbuild) so that investors can respond more quickly.

ASX Bookbuild® would be more likely to be accepted by the market over time if it were applicable in all potential forms of bookbuilds. It risks becoming a marginalised product if it is not relevant to the market from the outset, and in our view the current limitations mean it is unlikely to have this real relevance to the market.

We therefore recommend that its functionality be increased prior to launch to enable it to be used in the broadest possible range of circumstances.

Question 5 on page 13 of the Consultation Paper asks if ASX Bookbuild® could be enhanced to facilitate bookbuilds of renounced rights. In our view this is the main form of bookbuild that the program is currently ideally suited to, as it requires only that the price be set at the highest price with a coverage ratio of 100% or more.

RECOMMENDATION: ASX Bookbuild® should have sufficient functionality included from launch to enable it to be used in all forms of bookbuilds. The adjustments to achieve this do not appear major, and clearly some functions of ASX Bookbuild® will not be applicable in all forms of bookbuilds.

4.9. Enable Data Flows Outside Limited ASX Hours

ASX Bookbuild® appears to have limited timing flexibility compared to current broker-operated bookbuilding systems. ASX Bookbuild® only provides data while ASX is trading (ie between 10am and 4pm on maximum 5 days a week). Even if this is expanded to reflect the hours when ASX is open, not just trading, these times would fail to reflect the round-the-clock nature of Australian equity offers, in which investors in Europe, Asia and the US can provide and obtain relevant information in their own time zones. Functionality should therefore be provided though other websites (eg the issuer's, or its bookrunner's) around the clock, subject to appropriate protocols.

Reducing the hours in which a bookbuild can be conducted is highly likely to reduce rather than enhance demand, which appears contrary to ASX Bookbuild®'s aims. It may also limit that ASX Bookbuild®'s relevance to companies that have substantial levels of offshore shareholders because it is not well-suited to protecting their shareholders' interests.

RECOMMENDATION: ASX Bookbuild® should be available whenever ASX is open. In addition, some of the functionality should be available through the issuer's own website, or through its agents, at times when ASX is closed so that bids can be lodged and resultant ratios (see Section 4.5) determined at any time of the day, even when ASX is closed.

4.10. Remove Divestment Cap

We do not believe that ASX Bookbuild®'s proposed divestment cap is necessary or attractive. The risk of a post-offer overhang compounds rather than remedies the risks to shareholders created by ASX Bookbuild®'s inability to allow any real-time subjectivity in allocations. The solution is to allow more flexibility in allocations as set out in Section 4.6, rather than risk destabilising the post-offer market.

A bookbuild divestment cap raises many other concerns. We assume it would be an ongoing ownership restriction on specific investors, because the cap could otherwise immediately be overcome if the bidder sold and bought back the same number of shares on market (so minimal rice risk). It is unclear if issuers' constitutions will allow this unilateral imposition. We are also concerned about the position of directors when they set a price knowing that they may potentially require a bidder to divest a substantial number of shares, particularly if there is a risk that that "divestment demand" proves to be material in their setting of the final bookbuild price. Clearly there may be confusion in the company's information about bidder support and coverage ratios if it is based on this "divestment" demand.

RECOMMENDATION: Remove the Divestment Cap. Issuers should be able to identify bidders in advance of material allocations of shares so they are not in a position where they might allocate shares and simultaneously require their divestment.

4.11. Restructure Mode of Managing Sub-Underwriter Involvement

We are not convinced that the potential for "priority bids" necessarily "upholds the underwriting mechanism' as set out in paragraph 2.6 of the Consultation Paper. ASX

Bookbuild® appears to require sub-underwriters to lodge bids at the underwritten price when the book opens in order to take risk from an underwriter, although it is unclear why this cannot be an off-market contractual obligation.

Other questions which arise are:

- Do bidders lose priority if a bid that is lodged at the beginning of the bookbuild is amended in any way?
- How does a general sub-underwriter (rather than firm-in-relief sub-underwriter) bid? Any bid will increase its risk because it would receive a 100% allocation (assuming there is a shortfall) and then still be liable for a percentage of the shortfall.
- Will priority bids by sub-underwriters mislead the market by implying those bidders want to buy shares at the bid price, when in practice they are buying at a lower price because of the sub-underwriting fees being paid to them. The concerns from the Just Group IPO in 2004 are relevant

RECOMMENDATION: Issuers should confirm if an offer is fully or partially underwritten. Priority bids entered by an underwriter or sub-underwriter should be clearly identified and must be on a firm-in-relief basis in order to provide market clarity on pricing and demand levels.

4.12. Provide Flexibility to Ensure All Decisions are in Shareholders' Best Interests

ASX Bookbuild® is a technology platform, and cannot make qualitative assessments of any matters. Directors must make these decisions. It will be important for users of ASX Bookbuild® to recognise that its process may provide more transparency and potentially less risk of unfairness in pricing and allocations, but this alone does not safeguard shareholder interests. There is also a risk that bidders use the restrictions that an issuer places on itself in the bookbuild to design a bidding strategy that produces outcomes that are not in shareholder interests, regardless of the issuer's good intentions at the time.

Directors must retain and be willing to exercise the capacity to prevent unwelcome outcomes (such as by not making allocations). Clearly this must always be in shareholders' interests, and within their legal powers. One consideration would be to allow variations from any of the published parameters if the issuer obtained an independent opinion (potentially akin to opinions from Nomads in the UK) that the variation was in the interests of shareholders. The opinion could come from any competent adviser (including groups that may otherwise act as bookrunners) provided they were not involved in the offer

RECOMMENDATION: ASX Bookbuild® should permit issuers to adjust outcomes produced by pre-established parameters (even those disclosed to the public) if they have the legal capacity, believe the adjustment is in shareholders' interests, and have an independent opinion supporting these positions.

Section 5: Issues Requiring Further Information

The Consultation paper does not provide information on a number of matters that will affect ASX Bookbuild®'s value, or the market's willingness to use it. They include:

5.1. Costs

The total costs for using ASX Bookbuild® are unclear, as is the allocation of those costs. Costs could have a material impact on user uptake as issuers will assess these costs against the costs and benefits of using other processes for bookbuilds.

In addition, it is unclear if there are restrictions on how issuers could allocate costs to users of the facility. There would be a concern if costs could be allocated in ways that created financial disincentives that limited the willingness of other brokers to encourage their clients to bid in a bookbuild. This would jeopardise ASX Bookbuild®'s ability to increase the potential pool of bidders, and therefore potential total demand, for an issue.

The Consultation Paper also notes that non-brokers may be appointed as lead managers or corporate advisors for issues being conducted using ASX Bookbuild® (paragraph 3.2). The Consultation Paper does not indicate whether these parties, or indeed any parties, will be charged fees by ASX Bookbuild® in order to access the data in the ASX Bookbuild®. These hidden additional costs would inevitably be passed to the issuer, so the costs of ASX Bookbuild® will not be clear until they are clarified.

5.2. Trading Halts

The Consultation Paper indicates that issuers will use ASX Bookbuild® during trading halts. It is not clear whether trading halts will automatically be granted for the conduct of any offer where the issuer/seller uses ASX Bookbuild®, or whether the offer must first meet other parameters.

The paper should specify any parameters that might limit the circumstances when issuers could use ASX Bookbuild®, and whether they are different to the factors applying in the consideration by ASX of a non-user's request for a trading halt. Information on the exact circumstances allowing trading halt requests to be granted may in fact be welcomed by the market regardless of considerations around ASX Bookbuild®.

It would of course be of concern if ASX's decision to grant a trading halt for an issue or sale were impacted by the potential for it to receive fees through an issuer's use of ASX Bookbuild®.

5.3. Settlement Risk Underwriting

ASX Bookbuild® has the benefit of expanding the pool of bidders beyond the bookrunner's clients, but it appears to increase the risks to issuers that funds may not be provided at settlement. This is a material consideration for issuers, even if remote.

Issuers manage this risk under the current off-market process by agreeing settlement underwriting with their bookrunners. They therefore have the benefit of a level of insurance against this risk with a counterparty whose credit risk they can establish for themselves. Bookrunners in turn manage this risk by assessing the credit risk of their own client bidders.

The process under ASX Bookbuild® is different because potential bidders may have no relationship with the bookrunner. Brokers would be responsible for the bids they enter on behalf of their clients, but this means that issuers must accept each broker's assessment of the credit risk of its own clients, as well as the risk that each broker itself may delay or default on settlement. This is a material change in an issuer's risk profile, and means an issuer may have no cost-effective way to protect against any delayed or failed settlements. We understand the NGF would not cover this risk.

The considerations involved in settlement risk need to be clarified so this risk can be costed and managed, including potentially through underwriting.

5.4. Need to "Scrub" the Book

Bookbuilds frequently involve numerous brokers talking with numerous levels of the same investors. This can lead to numerous bids being lodged on behalf of the same investor because no broker wants the investor to miss out, and they are uncertain if bids have already been lodged.

Globally, some time is spent when books close to "scrub" them, or de-duplicate bids. This necessarily takes a little time and can only reduce the preliminary total demand number. We are concerned that the current system does not appear to allow flexibility to undertake this housekeeping. The price shown as the "indicative bookbuild price" may well be different after this process, so the market may well have been misinformed as the book was closing. As set out in Section 4.5, we recommend against disclosing an indicative price based on the ECP. Instead, broad coverage ratios should be shown. There remains a risk that the broad coverage ratio range may change from one band to another because of de-duplication, but the risk of misleading investors is materially reduced.

For certainty, we note that we do not believe the 10 minute adjustment to the random timer is adequate to address this concern.

5.5. Conditions for Early Offer Closing

It is unclear if an offer can be closed early even if particular parameters have not been met. The potential need to cancel, rather than have an early close to, an offer may be a disincentive for issuers to use ASX Bookbuild®.

It is also unclear how this function will work in conjunction with the sensible preference for many major investors to bid at the last minute. This behaviour is rational: if they bid early their demand can be used to catalyse other, higher bidders, leading to them potentially having to pay a higher price for the same shares than if they had bid later.

5.6. Price Leadership

The concept of price leadership under ASX Bookbuild® may warrant further thought as it may be gamed. It appears possible to lodge bids just prior to the time an offer is expected to close that are very marginally (say 0.5 cents) above the indicative price (assuming this information is disclosed). These bids would likely be price insensitive, and the bidder may choose to cancel them if it sees that it has caused a price increase rather than gained a potentially larger allocation at the lower price. The binary parameters for price leadership may therefore need further elaboration.

Section 6: Responses to Questions in the Consultation Paper

Our responses to the five specific questions in the Consultation Paper are:

6.1 *Are there any operational matters that should be taken into account for the purposes of ASX Bookbuild®?*

A number of issues require adjustment or consideration, as set out in Sections 4 and 5. We make no comment on the proposed changes to ASX Procedures.

6.2 *Are there any operational reasons why you would not be able to use ASX Bookbuild®?*

If amendments to ASX Bookbuild® improve its ability to protect shareholders we expect clients could use it.

6.3 *In relation to the random timer discussed in paragraphs 3.17 and 3.18, do you think it is appropriate for there to be a period of 10 minutes added to the random timer in circumstances where TLM has changed a public bookbuild parameter?*

As noted, this would be adequate provided non-professional investors could access offers by other means as well, and the relevant offer document set out the circumstances in which they might be able to withdraw or amend their bids. In the absence of this we do not think the time is adequate for all investors.

6.4 *Are you aware of any internal costs that you or your organisation would incur in using ASX Bookbuild®?*

We are not aware of any costs unless ASX seeks to charge additional costs an issuer's advisors in order for them to access ASX Bookbuild® data.

6.5 *Can you suggest any future improvements or enhancements to ASX Bookbuild® (e.g. allowing ASX Bookbuild® to be used for a bookbuild of renounced rights in a rights issue?*

In our view this is the main form of bookbuild for which ASX Bookbuild® is currently ideally suited. It requires only that the price be set at the maximum price where the coverage ratio is 1.0x or more.

Thank you for the opportunity to provide these comments. If you have any questions please contact Rowan Johnston at Greenhill on 02 9229 1441 or at rowan.johnston@greenhill.com. We would be pleased to add further information at any time.

Yours sincerely

Jamie Garis
Managing Director

Rowan Johnston
Principal

Greenhill

Bookrunner Focus in Different Types of Australian Bookbuilds

Type of Bookbuild Raising	Issuer's Targeted Outcomes from Bookbuild	ASX Bookbuild® Functionality
IPO	PRICE - usually a margin below likely first day's trading price SPREAD – need to meet ASX requirements for shareholder depth SHAREHOLDER BASE – usually a balance of local and offshore institutional investors, local retail investors and "priority" investors	PRICE -managed reactively by changes to ECP SPREAD – cannot be managed SHAREHOLDER BASE – limited capacity to manage through Priority Bidder designations
Broadly marketed Secondary offer	PRICE – target is market or higher SHAREHOLDER BASE – potential to accept lower price in order to ensure more stable post-sale register, along with focus on not rewarding those who potentially disrupt market in lengthy offer period	PRICE -managed reactively by changes potentially to ECP SHAREHOLDER BASE – limited capacity to manage through Priority Bidder designations
Accelerated Secondary Offer	PRICE – target is market or higher SHAREHOLDER BASE – potential to accept lower price in order to ensure more stable post-sale register	PRICE - managed by setting ECP potentially to 100% SHAREHOLDER BASE – limited capacity to manage through Priority Bidder designations
Placement	PRICE – target is market or higher SHAREHOLDER BASE – protect shareholders by allocating to current holders (at least proportionately) and likely longer-term holders	PRICE -managed reactively by changes to ECP SHAREHOLDER BASE – limited capacity to manage through Priority Bidder designations
Rights Issue (RI) Shortfall	PRICE- as high as possible because shares being sold on behalf of others SHAREHOLDER BASE – not material given price focus (but subject to statutory considerations)	PRICE -managed by setting ECP at 100% SHAREHOLDER BASE – limited capacity to manage through Priority Bidder designations
Combined placement and RI Shortfall	PRICE – balance benefit of being at market (ie stable) for placement, and as high as possible for shortfall sale SHAREHOLDER BASE – protect shareholders by allocating to current and other likely longer-term holders	PRICE -managed reactively by changes to ECP SHAREHOLDER BASE – limited capacity to manage through Priority Bidder designations
Volume Only	PRICE – fixed SHAREHOLDER BASE - protect shareholders by allocating to current and other likely longer-term holders	SHAREHOLDER BASE – limited capacity to manage through Priority Bidder designations