

**A REVIEW OF THE IPO ACTIVITY ON THE ROMANIAN CAPITAL MARKET.  
COMPARATIVE ANALYSIS WITH THE INTERNATIONAL CAPITAL MARKET**

Laura Raisa MILOȘ\*

**Abstract**

*The process of transition deterred for the Romanian economy the creation and development of an adequate economical infrastructure and of the institutions and mechanisms that regard the transactions with financial instruments. Through the main functions of the capital market, the one of financing the economy is one of the most important. It is an alternative to financing through the banking system, though it is slightly little used in Romania by the nonfinancial companies. In this paper the author tries to analyse the benefits of issuing equity on the capital market as a mean for financing a company's deficit and in the same time, tries to emphasize the current state of the Romanian capital market in comparison with the other European capital markets, as far as concerns the attractiveness of capital market, measured as the volume and structure of IPO's on the market.*

**Key words :** capital market, IPO, financing decision

**JEL classification :** G20

**1. Introduction**

The Romanian financial system is recognized to be over-dependent on banks in financial intermediation and underdeveloped capital markets. This is the main reason why, currently, the number of companies that choose to finance their activities through the capital market is not very large.

Strenuous efforts have been made though in Romania in order to establish efficient and stable financial systems, in particular to reconstruct the banking sector and develop capital markets. Given its size, growth potential and its role in financing other sectors of the economy, the financial sector has a direct and decisive impact on the aggregate competitiveness of modern economies. Efficient and liquid risk capital stock markets play a large role as a source of financing for high-growth companies. Financing through capital market can provide the company not only the needed financial resources, but also other benefits, important for a financing decision making. Through these benefits we can count:

- **Access to a large community of investors** (financial companies, nonfinancial companies, individual investors, public sector). All these investors are used to investing in

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\* Laura Raisa MILOȘ (iovulaura@yahoo.com) is Assistant at Eftimie Murgu University, Reșița, Faculty of Economics and Administrative Studies, and Phd Candidate at West University of Timișoara, Faculty of Economics and Business Administration, in the field FINANCE. Her research interests include: capital markets, financial management, econometrics, credit institutions. His teaching interests include: capital markets, econometrics, credit institutions.

the projects of the companies and the assumption of risks. Once that the company manages to be listed on the capital market, it also widens its alternatives of financing.

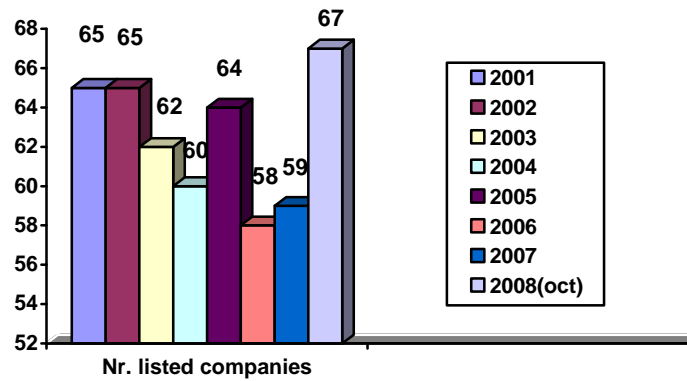
- ***Financing the growth of the company*** – financing through issuing equity can provide a certain flexibility, a lower financial risk and a proper financial leverage. A company that chooses to issue equity is not necessarily losing its decisional power. Financing through capital markets attracts especially companies that need to develop high volume of investments.
- ***Increased liquidity*** – capital market allows the quick transformation in liquidity of the invested capital. The shares of a publicly owned company are more liquid than the ones of a closed company.
- ***Notoriety, increased visibility among the business partners and of the current and potential customers through free publicity*** – a company that goes public guarantees the solvability, transparency and the prestige of the company. In this way, it proves that it can realize profits and allocate dividends, that is a competitive and stable company. This perception leads to a further development of the business relationship, and adds confidence among customers, suppliers and other stakeholders. On the other hand, the marketing effect of an IPO is well-known. There are numerous examples of international IPOs made just as a mean of advertising for the company.
- ***Establishing a market-value of the company*** –the shares of a company benefit from an objective evaluation, they have a significantly larger value than the ones of a closed company. The capital market identifies systematically the growth opportunities and making profit opportunities. The continuous evaluation of expectations regarding a certain company can be explained by the strong variation in the prices of the quoted shares.

Stock markets provide high-growth, innovative companies with a means of raising large amounts of long-term capital by selling company shares to outside investors. In addition, in the non-financial sector, small and medium sized entities can access a wider availability of more innovative and lower cost finance to fuel their growth, while larger companies profit from an overall reduction in the cost of capital and a wider range of financial products.

It is said that the company is "floated" on the stock market through an initial public offering (IPO). An IPO offers many companies the best way of financing their continued growth. However, it is true that an IPO involves for the entrepreneur some loss of control over the company, proportional to the amount of equity that is sold to outside investors. Although, the new funds generated through a capital increase are normally used for further investments or to reduce the company's liabilities.

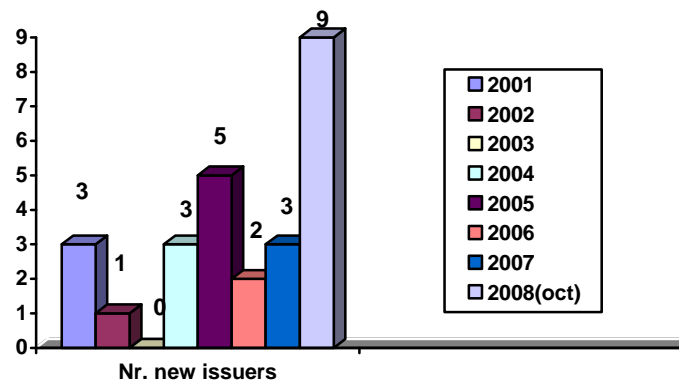
## **2. Current situation of IPOs on Romanian capital market**

It is clear that, as far as concerns the Romanian capital market, it has registered a positive trend regarding the issued equities. But this visible growth is unfortunately, more due to the increase in the value of the quoted shares than of the number of new listed issuers. The companies listed on the capital market don't differ too much from the ones existent at the beginning, and with the mass privatization process. Figure 1 shows the small variation in the number of the listed companies and in the number of new issuers on BVB in the period 2001- october 2008.



Source of dates: [Dates computed from www.bvb.ro]

Fig. 1. Dynamics of listed companies on BVB in the period 2001-2008(oct.)

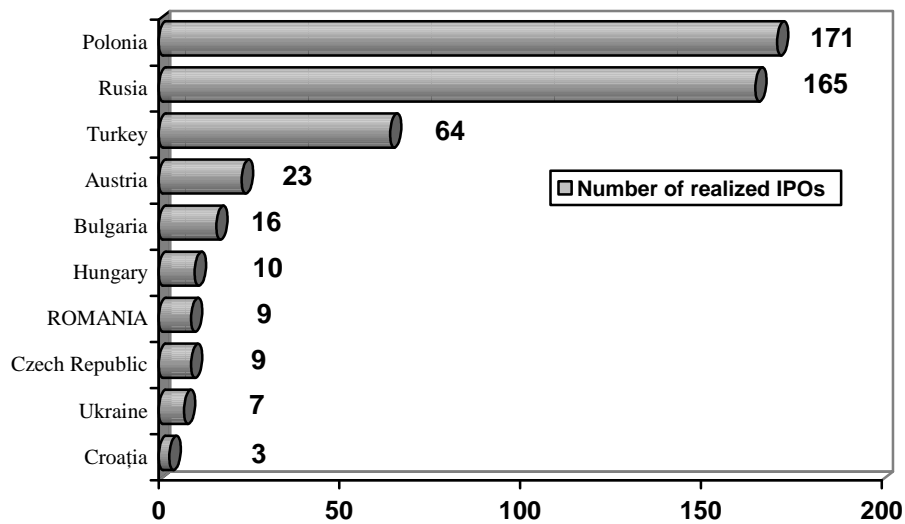


Source: [Dates computed from www.bvb.ro]

Fig. 2. Dynamics of new issuers on BVB in the period 2001-2008(oct.)

The number of IPOs realized in the last period show the relative low position of Romanian capital market in the ranking of the Central and Eastern European countries. We can easily notice from the figure below that in the period 2003-2007, Poland ranks one with a total number of 171 IPOs, followed by Russia, with 165 IPOs and Turkey, with 64 IPOs.

In Romania, the IPOs developed in the period 2003-2007, were the ones of companies like SSIF Broker Cluj (2004), Flamingo, Vrancart and Apa Staretului (2005), Transelectrica, Alumil Rom Industry and CCC Blue Telecom (2006) and only one IPO, that of Transgaz in 2007. From these few IPOs, two of them even failed because of the small percent of subscription.



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ce: [Dates computed from www.kmarket.ro]

**Fig. 3. Dynamics of IPOs in the period 2003-2007 at the level of Central and Eastern Europe**

The lack of IPO activity in Romania, in my opinion, is due to the fact that Romanian companies find rather difficult the possibility of financing their activity and investment projects through the capital market. This is the consequence of their reluctance about the future of the capital market or of the fact that the pre-requisites for being listed are not comfortable for these companies (25 % of their shares publicly distributed, the necessity of transparence and audit of their last three financial statements, the fees charged by BVB and the financial intermediary etc). Not at least, the long period of time since the moment of taking the decision of financing through the capital market and the moment of obtaining the necessary funds is an important factor when deciding to launch an IPO.

Of course, the current international context was not in the favour of Romanian capital market as well. For the year 2008, there were, for the first time in the capital market history, more than 20 IPOs announced. Of these, until October 2008, there were realized only five (STK Emergent, Contor Group, Teraplast, Casa de Bucovina and Pomponio), from which one failed. Because of the critic situation that Romanian capital market is facing recently, there will probably lack other IPOs until the end of this year.

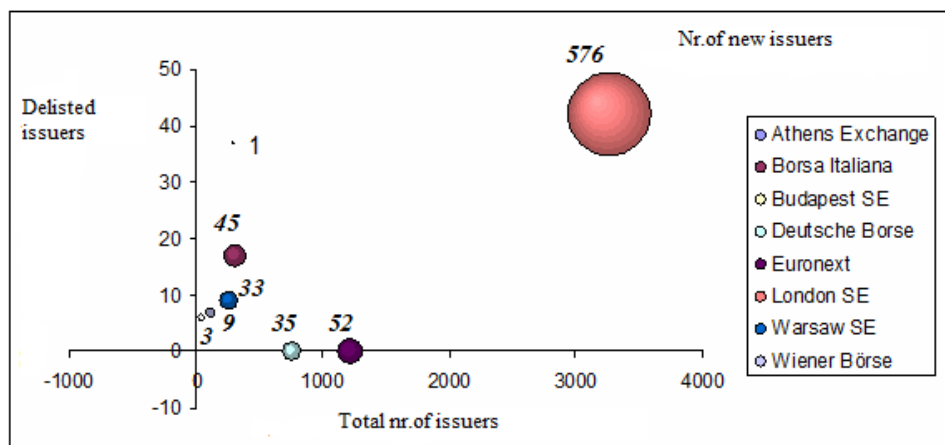
One possible solution for developing the capital market and refreshing it in this respect would be the listing of several utility companies with strategic importance for the national economy. That would make investors more confident in the local capital market and the percent of IPOs of medium and small companies would maybe increase as well. The most suitable example for this consideration would be the IPO launched by Transgaz, finalized in 2007, that has attracted more than 24 times the initial offer of the company. This demonstrates the significant demand for IPOs issued by these kind of companies. This is the main reason why listing at least 5 % of the shares of some companies like Hidroelectri-

ca, Nuclearelectrica, Romgaz, Romtelecom, Tarom airline and Bucharest's international „Henri Coandă” Airport would bring future development to the local capital market.

### 3. Recent evolution of IPOs on international capital markets

Unlike the Romanian companies, for the European companies the capital market represents a good opportunity to finance themselves, which can be proved by the increased number of issuers from the capital markets, and by the large volumes of IPOs launched by these companies. The role of capital market in their economy can be seen as a really important one, and the value of issuing of these companies is increasing every day.

The number of issuers from the developed capital markets not only that overcomes in a high proportion the number of issuers from the Romanian capital market, but it also includes both national and international companies. On the first position, as it might be expected, outlines the London Stock Exchange, capital market that has cumulated 3256 issuers in the year 2006 (2913 domestic issuers and 343 foreign issuers). In the same time, it ranks first having in consideration the IPOs issued on the market, with a number of 576 companies (544 domestic issuers and 32 foreign issuers). The following places are taken by: Euronext, Borsa Italiana, Wiener Börse and Warsaw Stock Exchange (Figure 4).



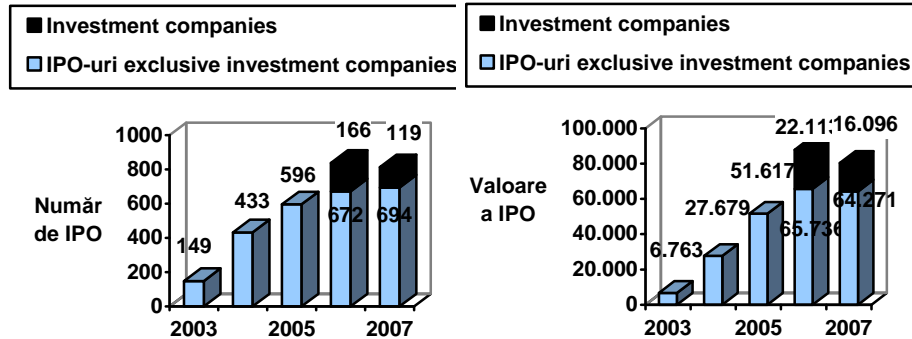
Source of dates: [World Federation of Exchanges, 2007]

Fig.4. Ranking of main European capital markets in 2007

As far as concerns the evolution of IPO at the level of European capital markets, we can notice that the volume of IPOs has remained significant, despite the problems that have appeared on international markets on the second half of the year 2007. Comparatively, the number of IPOs realized in 2007 was slightly reduced than the one registered in 2006, respectively a volume of 813 IPOs in 2007, against 838 IPOs in 2006 and a slightly reduced net value obtained by the issuers, with 9 % lower than the one registered in 2006, decreasing from 87.849 million Euro in 2006 at 80.367 million Euro in 2007.

An interesting evolution was registered by Warsaw Stock Exchange, that has managed, through its performance, to locate right next to most developed capital markets like LSE or

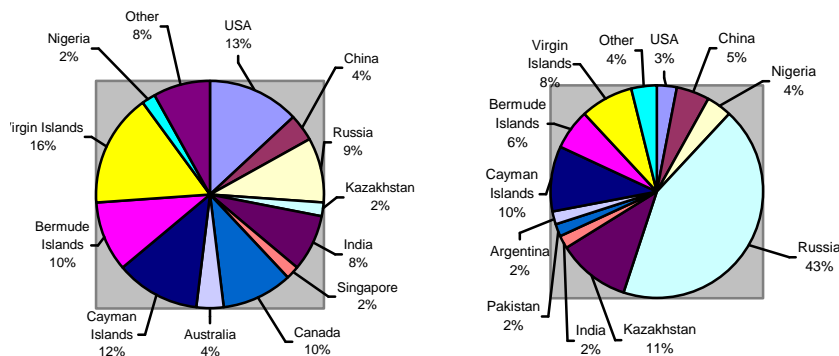
Euronext. In 2007, it has realized more than 80 IPOs, a volume slightly more reduced than LSE, with a total number of 99 IPOs (Figure 5).



Source of dates: [PWC, 2007]

**Fig. 5. Evolution of IPO on the European international markets, in the period 2003-2007 (millions Euro)**

Not only domestic companies decide to finance their deficits by reaching to their local capital market. Lately, it has been noticed the increasing volume of international IPOs, of non-European companies on European capital markets. These IPOs attract significant resources, especially those from Russia or Kazakhstan. An example in this respect could be offered by the VTB Bank, that has cumulated a value of 4.274 million Euro and has been declared the biggest IPO of the year 2007 in Europe. The origin of these important IPOs, can be noticed in the figure below:



Source of dates: [PWC, 2007]

**Fig.6. The origin of the international IPOs realized in 2007 on European capital markets (by number and by value, %)**

#### 4. Conclusions

As revealed in the previous analysis, the number of listed companies on the Romanian capital market has remained almost constant over the considered period of time (2001-2008), with a slight increase in the number of IPOs realized by these companies. A significant refreshment in what concerns the attractiveness of capital market for the investors, willing to finance as well local companies could be the listing of several utility companies with strategic importance for the national economy. Until then, the European capital markets seem to gain a certain advantage regarding the function of financing the economy. Not only developed economies, but also economies belonging to Central and Eastern European countries have known a significant growth of the IPOs launched by their domestic companies. This fact should not leave Romanian capital market without reaction. With the passing of time and learning from other companies experience, the Romanian companies will become more aware of the benefits of financing through the capital market and of the positive effects of launching an IPO.

On the other hand, the increasing integration of the European countries into the international capital market reinforces the importance of removing the structural problems that Romanian capital market is facing nowadays. Further reforms and measures should be taken in order to achieve a fully functioning and efficient capital market, capable of attracting all-sized companies in financing their financial deficits. Therefore, the development of Romanian capital market should continue, in order to convince the local companies to seek financing on the domestic market and not on larger or more liquid markets.

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- \*\*\* World Federation of Exchanges, *Statistics*, at <http://www.world-exchanges.org/WFE/home.asp?action=document&menu=10> accessed on 9<sup>th</sup> of March
- \*\*\* <http://www.kmarket.ro>, accessed on 9<sup>th</sup> of March
- \*\*\* <http://www.bvb.ro> , accessed on 9<sup>th</sup> of March

**Appendix 1****Total number of issuers on European capital markets**

Capital market	Number of issuers					
	2005			2006		
	Total	Domestic	Foreign	Total	Domestic	Foreign
Athens Exchange	<b>304</b>	302	2	<b>290</b>	288	2
Borsa Italiana	<b>282</b>	275	7	<b>311</b>	284	27
Budapest SE	<b>44</b>	44	0	<b>41</b>	41	0
Deutsche Börse	<b>764</b>	648	116	<b>760</b>	656	104
Euronext	<b>1259</b>	966	293	<b>1210</b>	954	256
London SE	<b>3091</b>	2757	334	<b>3256</b>	2913	343
Warsaw SE	<b>241</b>	234	7	<b>265</b>	253	12
Wiener Börse	<b>111</b>	92	19	<b>113</b>	96	17

Source: [World Federation of Exchanges]

**Appendix 2****Number of new listed companies on European capital markets**

Piața de capital	Number of new listed companies					
	2005			2006		
	Total	Domestic	Foreign	Total	Domestic	Foreign
Athens Exchange	<b>5</b>	5	0	<b>1</b>	1	0
Borsa Italiana	<b>19</b>	19	0	<b>45</b>	24	21
Budapest SE	<b>1</b>	1	0	<b>3</b>	3	0
Deutsche Börse	<b>15</b>	15	0	<b>35</b>	31	4
Euronext	<b>34</b>	32	2	<b>52</b>	40	12
London SE	<b>626</b>	605	21	<b>576</b>	544	32
Warsaw SE	<b>35</b>	33	2	<b>33</b>	27	6
Wiener Börse	<b>7</b>	6	1	<b>9</b>	8	1

Source: [World Federation of Exchanges]

**Appendix 3****Ranking of European capital markets (both regulated and over-the-counter), according to the volume of IPOs issued**

	Number of IPOs	Offered value (mill.Euro)
<i>ORGANIZED EXCHANGES</i>		
London SE	99	27.641
WSE	80	1.980
NYSE Euronext	40	7.563
Oslo Bors & Axess	37	1.993
OMX	35	2.301



Borsa Italiana	29	3.943
Deutsche Börse	28	6.734
BME	12	10.084
SWX	10	1.975
Wiener Börse	6	1.427
Athens Stock Exchange	3	479
ISE	1	1.495
Luxemburg	/	/
<i>OVER-THE-COUNTER</i>		
London (AIM)	220	9.537
London (PSM)	5	1.909
OMX (First North)	50	837
NYSE Euronext (Marche libre)	48	24
NYSE Euronext (AlterNext)	39	445
Deutsche Börse (Entry Standard)	34	250
WSE (NewConnect)	24	41
Luxemburg (EuroMTF)	13	1.295
ISE(IEX)	9	183

Source: [PWC, 2007]

#### Appendix 4

##### Ranking of the most important 5 international IPOs developed on international capital markets

Societate	Obtained value (mill.Euro)	Organized exchange	Field of activity	Origin country of the issuer
VTB Bank	4,724	London	Banking	Russia
Eurasian Natural Resources Company	1,888	London	Mining	Kazakhstan
InnoLux Display Corporation	931	London	Technology	Taiwan
Magnitogorsk Iron & Steel Works	748	London	Base resources	Russia
PIK Group	690	London	Real estate	Russia

Source: [PWC, 2007]