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Strategic Perspectives

Inflation, instability drive muted first half for IPOs

By John Filar Atwood

Instability brought on by inflation, rising interest rates, and geopolitical unrest continued to plague the IPO market in the first half of 2023, pushing it to its worst January through June performance since 2016. With 77 deals, the market dropped 35 percent from the 119 IPOs seen in the first six months of 2022, and aggregate proceeds fell to $10.5 billion from last year's $15 billion, a 30 percent decline. The 118 new filings by IPO-hopeful companies represented a 23 percent fall-off from 2022's 153 preliminary registrations as of June 30th.

The numbers are not a complete surprise coming out of a rough 2022 for markets and investors. A key concern was rising inflation, which prompted a coordinated effort by the world's central banks, including the U.S. Federal Reserve, to raise interest rates to try to put the brakes on a possible recession. That strategy has yet to yield significant results, however, and fears of more economic woes still linger.

Those worries, whether based on interest rates, inflation, and/or the war in Ukraine, underlie the current IPO slowdown. The potential for further economic trouble is making investors cautious and putting pressure on IPO company valuations as dealmakers work to avoid over-pricing offerings amid intense scrutiny from investors.

From the standpoint of prospective IPO companies, uncertain economic conditions are keeping them on the sidelines. If they do not need the capital, then going public into strong market headwinds with a probable modest share price and valuation does not make sense. Nowhere is this clearer in the IPO market than with technology stocks.

Tech troubles. The tech sector has long been a driver of the IPO market, but over the past few years solid tech industry IPOs have been hard to come by. Among the reasons is that companies with promising IPO prospects such as Instacart or Reddit are biding their time until the market improves.

In the heady days at the end of the 2021 IPO explosion, both Instacart and Reddit announced that they had confidentially filed preliminary IPO registration statements with the SEC. Fast forward 18 months and neither company has moved on its IPO plans. The same is true of StubHub, which said in January 2022 that it was considering going public through a direct listing but still has not done so.

To put some numbers to the tech sector woes, consider the prepackaged software space (SIC 7372), annually among the busiest industries for IPOs. In the decade prior to 2022, its lowest annual deal count was eight in 2016 with a peak of 50 in 2021. In 2022 there were only two SIC 7372 completed IPOs and there have been five so far in 2023. Similarly, SIC 7370 (Computer Programming & Data Processing Services), which produced 28 new issuers in total from 2019 through 2021, dropped to two IPOs in 2022 and none so far this year.

There is no question that a tech rebound would inject some life into the IPO market, which has some industry observers wondering if the intense interest in generative AI might be the catalyst for an industry IPO turnaround. At the moment, however, the AI space has very few well-established companies that would even consider an IPO, and those businesses are attracting enough private capital to be able to steer clear of the public markets.

While tech IPO numbers were down, the industries that saw the most deals in the first half of the year were blank checks (SIC 6770) with 17, and pharmaceutical preparations (SIC 2834) with nine. It is worth noting that while blank checks accounted for 17 percent of the six-month IPO total, they also were responsible for more than half (19 of 37) of the withdrawn registrations as of June 30th.

Offerings are smaller. There was a dramatic shift toward very small IPOs in the first six months of 2023, with nearly 34 percent (26 IPOs) raising $10 million or less. Add to that the 18 percent that raised between $10 million and $25 million, and you have more than 50 percent of first-half deals at $25 million or below in aggregate proceeds.

By comparison, in the first half of 2022, only 4 percent (5 IPOs) fell within $10 million or less range, and 23.5 percent (28

IPOs) raised between $10 million and $25 million. Over the past decade, 37 percent of the completed IPOs raised between $100 million and $250 million. Only 10.4 percent of new issuers in this year's first half fell within that range.

Even with the surge in smaller deals, new issuers managed to generate a respectable $10.5 billion in aggregate proceeds from January through June. However, more than one-third of that total was accounted for by a single deal—Kenvue's $3.8 billion offering in early May. The provider of consumer health products including Tylenol, Neutrogena, Listerine, and Band-Aid, was the only company to top $1 billion in proceeds in the first half of the year. The next closest offering was Nextracker's $638 million deal on February 8th.

Non-U.S. companies. Despite the reduced number of IPOs overall compared to last year, non-U.S. companies matched their first-half 2022 pace with 37 offerings in the U.S. Whereas in 2022 that was good for a 31 percent market share, non-U.S. companies claimed 48 percent of the IPO market in the first six months of 2023. Nineteen of the non-U.S. new issuers were from China, which is six more deals than the country's entire tally for 2022.

Malaysia was second behind China with four new issuers through June 30th, equaling its 2022 total. Canada matched Singapore with three IPOs, and Bermuda and Israel produced two each. Ireland and Taiwan, neither of which was home to a U.S. IPO company in 2022, produced one new issuer apiece. Notably absent at the 2023 mid-year mark is the U.K., which is active in U.S. markets nearly every year, including its four IPOs in 2022 and 15 in 2021.

Law firm rankings. Through the end of June, 108 law firms participated in some form of IPO representation - as either issuer's or underwriters' counsel - seven fewer firms than in the same period last year. Latham and Watkins and Ogier lead the rankings by number of IPOs with 11 representations each, although the aggregate offer amount for Latham's deals is significantly higher than Ogier's. Maples and Calder is third with nine IPOs by virtue of the offer amount tie-breaker with Ellenoff Grossman and Sichenzia Ross which also worked on nine deals in the first half of 2023. Maples and Calder has finished atop the year-end rankings in each of the past two years with 28 and 217 completed offerings, respectively.

Conyers Dill found itself in sixth place at the mid-year mark. The firm, which finished 48th in the 2022 rankings by number of IPOs, had eight representations in this year's first half. Hunter Taubman also had eight, but its aggregate offer amount was $468 million behind Conyers.

If Conyers Dill can hold onto its top-ten placement for the rest of the year, it will represent a significant improvement over its 48th place finish in 2022. The same can be said of Jingtian Gongcheng and Ortoli Rosenstadt, which found themselves in the 8th and 9th positions in the rankings at June's close. Ortoli was up from a 26th place finish last year, while Jingtian did not record any IPO representations in 2022. Both firms had seven representations as of June 30th, but Jingtian's raised slightly more money.

Kirkland & Ellis claimed the final spot in 2023's mid-year top ten rankings by number of IPOs. The firm, which finished in 12th place in 2022, closed the first half with six representations, only one short of its 2022 total.

The top ten ranking by number of offerings is notable because a few of 2022's top firms did not make the list. Loeb and Loeb was just outside the top ten in 11th place with six representations, The firm was tied for first place last year with 28 IPOs. Davis Polk & Wardwell currently ranks 18th after finishing fourth in 2022.

Ranked by total offering amount, Davis Polk claimed the top spot despite only having worked on only three IPOs in the first half of the year. The firm's deals raised $4.7 billion, led by Kenvue's $3.8 billion offering. Davis Polk served as underwriters' counsel for that IPO. Kenvue's issuer's counsel, Cravath Swaine, found itself in second place by aggregate offer amount even though the Kenvue deal was its only representation from January through June.

Latham found itself in third place thanks to its work on 11 offerings that raised an aggregate of $2.26 billion. The only other firm whose first-half representations netted more than $1 billion was Kirkland & Ellis at $1.09 billion. That was good enough for 4th place as of June 30th, narrowly ahead of Simpson Thacher's $981 million.

Lead manager rankings. In the first half of 2023, JPMorgan and Boustead claimed more IPO business than any other lead managers. With eight IPOs, JPMorgan is on pace to easily exceed its 2022 total of nine IPOs, while Boustead matched its tally from last year. Of note is that while work on blank check offerings has significantly supported the business of lead managers over the past two years, neither JPMorgan nor Boustead counted an SIC 6770 IPO among its completed representations in the first six months of 2023.

In the mid-year rankings, JPMorgan and Boustead were only one representation ahead of the next closest investment banks, Bank of America and EF Hutton. EF Hutton was the top IPO lead manager in 2022 with 27 IPOs, so it has some work to do in the second half of 2023 if it wants to approach that total this year. Bank of America tallied nine representations last year and could easily improve on its 2023 performance.

Lined up right behind EF Hutton in the rankings are Goldman Sachs and Barclays, each with six IPOs as of June 30th. Using the aggregate proceeds tie-breaker, Goldman Sachs is comfortably ahead of Barclays with \$5.2 billion to Barclays' \$1.8 billion.

Barclays climbed into the top ten from a 23rd place finish in 2022. Other banks that improved their standing so far in 2023 include Jefferies and Benchmark which made the top ten after finishing last year in 13th and 17th place, respectively. Each of Jefferies, Benchmark and Citigroup worked on five deals in the first half of the year. Citigroup earned the number seven spot in the rankings with IPOs that raised \$1.8 billion.

Three of the top ten lead managers (JP Morgan, Bank of America, and Goldman Sachs) surpassed the \$5 billion mark in aggregate proceeds, with JP Morgan leading the way with more than \$6 billion. Each bank served as co-lead on Kenvue's \$3.8 billion offering. At 2022's midpoint, no investment bank had reached \$5 billion in total proceeds, with Goldman's \$3.3 billion leading all banks.