Capital Markets in 2030

The future of equity capital markets

pwc

Written by

The Economist INTELLIGENCE UNIT

Foreword

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Welcome to ***Capital Markets in 2030***, a report exploring the changing dynamics in global equity capital markets.

Our initial survey of global executives was conducted in 2011. At that time, strong growth was anticipated in emerging economies and, by association, in their equity markets, to the point that they were expected to become the leading global exchanges for new issues in the medium term. We can now see that the New York, London and Hong Kong exchanges are proving to be significantly more resilient than had been anticipated in 2011, enjoying strong momentum in recent years and now expected to maintain their lead.

Although the growth of emerging market exchanges has been more subdued than anticipated in 2011, Chinese and Indian companies are still expected to dominate future new issues. While further progress in the key emerging market economies will support the growth of their exchanges, the pace of the shift in balance to these exchanges has perhaps moderated.

Technology companies have featured strongly in initial public offering (IPO) activity in recent years. This is set to last, as the sector continues to generate significant demand for equity in public markets, and the competition between exchanges to attract 'unicorns' and 'new economy' companies intensifies, particularly between the US and China (mainland China and Hong Kong).

New York, London and Hong Kong exchanges are proving to be significantly more resilient than had been anticipated in 2011, enjoying strong momentum in recent years and now expected to maintain their lead.

Ross Hunter
IPO Centre Leader

Alongside this, the range of capital raising options has increased significantly in recent years as the established private equity and venture capital pools have grown, and as they are complemented by numerous alternatives.

Ultimately, in our view, the public equity markets remain the natural destination for many companies, and can play a vital role in the healthy functioning of the global economy. The challenge for the exchanges is how they can adapt to the changing landscape, competing but also collaborating with one another, and complementing other financing alternatives to support the provision of capital across the world.

For companies, the choice of credible exchanges for public listings, as well as a range of private funding options, will continue to expand, offering ever more alternatives when they seek to raise capital.

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Executive summary

Global capital markets reached new post–financial crisis highs in 2018. This expansion was largely driven by the US economy. Companies now have to consider a growing range of issues that may affect the shape of future capital market activity, such as an increasing focus by regulators and investors on sustainability and governance, and mounting concerns around deglobalisation, rising populism and greater geopolitical risks.

In 2018, The Economist Intelligence Unit conducted a follow-up to a 2011 survey on behalf of PwC, asking nearly 400 executives at companies from across the globe for their views on the factors that are defining the development of global equity capital markets. This report marks the evolution of these industry leaders' views.

The 2011 report reflected a degree of post–financial crisis optimism, particularly for emerging market (EM) equity markets. Given the growth dynamics at that time, expectations were for EMs — particularly China and India — to increasingly dominate global equity markets in terms of issuance, sources of capital and the influence of their stock exchanges. The latest survey does demonstrate a continued recognition of the growing role of EMs, but also reflects a sometimes radical modification of business leaders' perspectives.

- **Although developed market (DM) exchanges continue to be favoured for listing, their lead over EMs has narrowed significantly since 2011.** The dominance of the New York Stock Exchange (NYSE), the Nasdaq, the London Stock Exchange (LSE) and the Hong Kong Stock Exchange (HKEX) is not as great as before, with Indian exchanges, Shanghai's SSE and Brazil's Bovespa moving up the ranks, in recognition of the growing maturity of EM exchanges. Other exchanges that became more attractive are the Australian Securities Exchange (ASX) and Singapore Exchange (SGX), reflecting the growing importance of the Southeast Asia region.

55%

of respondents feel the most attractive private funding option is private equity.

70%

of respondents agree that most successful companies would still choose to go public at some point in their life cycle.

- **When looking towards 2030, although our respondents still expect companies from China and India to dominate issuance, views regarding the leading exchanges have changed dramatically.** The same four exchanges, NYSE, Nasdaq, LSE and HKEX, are expected to maintain their leading position, reflecting their unmatched levels of resilience and liquidity advantages. In 2011, the medium-term view of the top four exchange destinations was very different — with Shanghai in the top spot, Indian exchanges at number three and Brazil's Bovespa in fourth place.

- **Liquidity remains the top priority (selected as most important by 49% of respondents) when choosing a listing location.** Respondents are increasingly focused on valuations (32%) and concerned about the costs of listing (29%). Meanwhile, stock market ecosystems and the size of the investor base have become relatively less important to participants.

- **Companies' options for raising capital have increased.** Some 76% of respondents believe that companies in both DMs and EMs have more choices of both public and private financing routes.

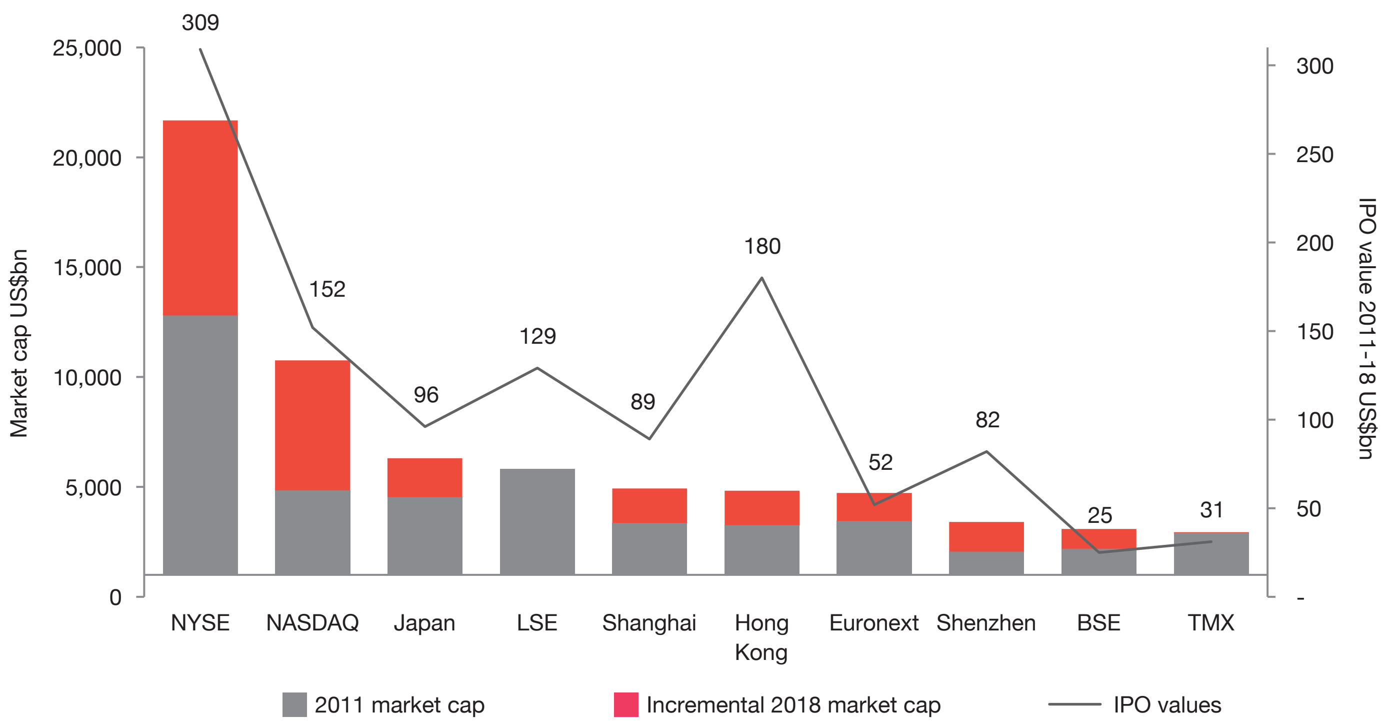
- **Private markets are seen as complementary to public markets, not as rivals.** Seventy percent of respondents feel that the traditional public listing is becoming a less important source of funding. The most attractive private funding option, selected by 55% of respondents, is private equity. Notwithstanding that finding, 70% agree that most successful companies would still choose to go public at some point in their life cycle.

Then and now: Are the markets on trend?

In 2011, survey respondents thought that EM exchanges, most notably China and India, would grow rapidly to rival — if not displace — DM exchanges, particularly London and New York.

The expectation was of high growth in the market capitalisation of companies listed on EM stock exchanges. This was based on overall market bullishness about the rise of EMs and their increasing share of global GDP, coupled with deeper domestic capital capacity and additional opportunities for access by foreign investors. The market capitalisation of companies on Chinese exchanges was forecast to outstrip those on US exchanges by 2030. Evidence suggests that EMs are falling behind on this trend line.

Figure 1: Ten largest exchanges by market capitalisation as at December 2018



Source: World Federation of Exchanges (WFE), exchange data (for LSE only), Dealogic

Note: WFE data includes only domestic market capitalisation

The slower-than-expected growth of EM exchanges is demonstrated when comparing the sizes of the US and Greater China exchanges now and in 2011. The combined US domestic market caps total US$30.4tn; for mainland China and Hong Kong, they total US$10.1tn. In 2011, it was US$15.6tn and US$5.7tn, respectively. US exchanges are now three times the size of their Chinese counterparts, compared with 2.7 times in 2011. The growth of the US market has outstripped expectations, while the growth of China and other EMs has lagged.

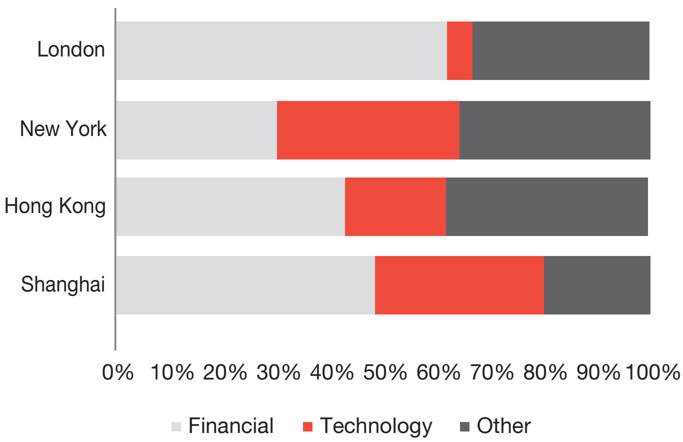
In terms of capital raised, the US, London and Hong Kong remain the pre-eminent international centres; mainland China exchanges also show strong growth.

In addition to representing a significant proportion of the new capital raised, the US market has been the major beneficiary of a dramatic increase in technology-related stock valuations. Largely as a result of that, the US S&P 500 index has doubled since 2007, although prices have come under pressure since late autumn 2018.

Which sectors and where?

Initial public offering (IPO) activity since 2011 has been heavily influenced by the rise of 'new economy' companies. As reflected in Figure 2, technology and financials dominated the listing activity on the leading exchanges in 2016–18. Other notable listings include the IPO of Softbank, which raised US$21.3bn on the Tokyo Stock Exchange in December 2018, the US$5.2bn IPO of Siemens Healthineers and the US$4.4bn IPO of Knorr-Bremse on the Deutsche Börse.

Figure 2: Top IPOs by sector in London, New York, Hong Kong and Shanghai, 2016–18



Source: Dealogic

"The geographical and cultural proximity for mainland investors to invest via the Stock Connect channel should entice companies to list in Hong Kong.

James Fok

Head of Group Strategy
HKEX

Figure 3: Top IPOs in London, New York, Hong Kong and Shanghai in 2016–18

London

Year	IPO	Total amount US$m	Sector
2018	Aston Martin Lagonda Global Holdings plc	1,407	Automotive
	Smithson Investment Trust plc	1,084	Finance
	Vivo Energy plc	819	Oil & Gas
	Avast plc	816	Computers & Electronics
	Nova Ljubljanska Banka	764	Finance
2017	Allied Irish Banks Plc	3,832	Finance
	EN+ Group plc	1,500	Utility & Energy
	J2 Acquisition Ltd	1,210	Finance
	Sherborne Investors (Guernsey) C Ltd	906	Finance
	BioPharma Credit plc	762	Finance
2016	ConvaTec Group plc	1,939	Healthcare
	CYBG plc	566	Finance
	Metro Bank plc	564	Finance
	Countryside Properties plc	506	Real Estate/Property
	Civitas Social Housing plc	436	Real Estate/Property

New York (NYSE and Nasdaq)

Year	IPO	Total amount US$m	Sector
2018	AXA Equitable Holdings Inc	3,157	Insurance
	PagSeguro Digital Ltd	2,606	Computers & Electronics
	iQIYI Inc	2,424	Telecommunications
	Pinduoduo Inc	1,743	Computers & Electronics
	Elanco Animal Health Inc	1736	Healthcare
2017	Snap Inc	3,910	Computers & Electronics
	Altice USA Inc	2,152	Telecommunications
	Invitation Homes Inc	1,771	Real Estate/Property
	Loma Negra CIASA	1,097	Construction/Building
	Silver Run Acquisition Corp II	1,035	Finance
2016	ZTO Express (Cayman) Inc	1,406	Transportation
	LINE Corp	1,322	Computers & Electronics
	Athene Holding Ltd	1,242	Insurance
	MGM Growth Properties LLC	1,208	Real Estate/Property
	US Foods Holding Corp	1,176	Food & Beverage

Hong Kong

Year	IPO	Total amount US$m	Sector
2018	China Tower Corp Ltd	7,491	Telecommunications
	Xiaomi Corp	5,430	Telecommunications
	Meituan Dianping	4,222	Computers & Electronics
	Ping An Healthcare & Technology Co Ltd	1,118	Computers & Electronics
	Jiangxi Bank Co Ltd	1,095	Finance
2017	ZhongAn Online P & C Insurance Co Ltd	1,754	Insurance
	China Literature Ltd	1,227	Computers & Electronics
	Guangzhou Rural Commercial Bank Co Ltd	1,191	Finance
	Zhongyuan Bank Co Ltd	1,190	Finance
	Yixin Group Ltd	867	Computers & Electronics
2016	Postal Savings Bank of China Co Ltd	7,625	Finance
	China Resources Pharmaceutical Group Ltd	1,941	Healthcare
	China Zheshang Bank Co Ltd	1,938	Finance
	BOC Aviation Ltd	1,126	Finance
	China Securities Co Ltd	1,057	Finance

Shanghai

Year	IPO	Total amount US$m	Sector
2018	Foxconn Industrial Internet Co Ltd	4,257	Computers & Electronics
	Hebei Yangyuan ZhiHui Beverage Co Ltd	669	Food & Beverage
	Jiangsu Financial Leasing Co Ltd	636	Finance
	Bank of Changsha Co Ltd	399	Finance
	Bank of Chengdu Co Ltd	385	Finance
2017	Caitong Securities Co Ltd	620	Finance
	Huaneng Lancang River Hydropower Co Ltd	589	Utility & Energy
	Zheshang Securities Co Ltd	409	Finance
	Shandong Publishing & Media Co Ltd	409	Publishing
	Jiangsu Provincial Agricultural Reclamation & Development Co Ltd	351	Agribusiness
2016	Bank of Shanghai Co Ltd	1,599	Finance
	Bank of Jiangsu Co Ltd	1,095	Finance
	Huaan Securities Co Ltd	744	Finance
	Triangle Tyre Co Ltd	661	Automotive
	Bank of Guiyang Co Ltd	640	Finance

Source: Dealogic

In terms of IPO values per exchange, there has been a significant shift back to DMs over the past seven years. The combined value of Shanghai, Shenzhen and Hong Kong IPOs in 2016–18 was US$142.5bn; for NYSE and Nasdaq, it was marginally less, at US$138.6bn. For 2009–11, the three-year period preceding our previous survey, the figures were US$250.1bn and US$128.9bn, respectively.

Hong Kong IPO proceeds significantly outweighed Shanghai and Shenzhen combined IPO funds raised in 2018, although for the 2016–18 period, mainland China exchanges marginally led the way. This makes it clear that Chinese companies are increasingly finding access to sufficient sources of capital on the mainland. As noted by James Fok, Head of Group Strategy at the HKEX, however, the Hong Kong route offers additional advantages to company founders in terms of ease of sell-down and political de-risking. He also says that “the geographical and cultural proximity for mainland investors to invest via the Stock Connect channel should entice companies to list in Hong Kong.”

The new technology wave and its impact on global capital markets

Looking to 2030, PwC anticipates that technology will remain the most important sector.

Historically, the US market has been a more attractive environment for technology companies, with better valuations and a more knowledgeable investor base, attracting the lion’s share of Chinese technology IPOs, including Alibaba’s record-breaking US$25bn IPO in 2014. Increasing efforts by leading financial centres to win over such companies will continue to intensify competition between the New York and China (mainland China and Hong Kong) exchanges in particular. Listings of companies such as Xiaomi and Meituan in Hong Kong in 2018 are evidence of this.

A number of recent market and regulatory developments can be expected to help attract more IPOs to Hong Kong and mainland Chinese exchanges, away from the US market:

- The amendment by HKEX of IPO rules in April 2018 to allow dual-class shares for listing companies gives certain shareholders, such as company founders, voting power beyond the proportion of their equity holding. This is popular with ‘new economy’ companies and was previously available only in the US.

- Changes to the HKEX listing rules to relax the three-year profitability requirements for biotech companies paved the way for more of these firms to list in Hong Kong rather than the long-established US market.

- Mainland China is now allowing global technology companies easier access to domestic investors. Authorities have endorsed the Chinese depositary receipts scheme, which will allow Chinese investors to hold a form of shares in firms listed abroad. This scheme is currently available only to the largest companies.

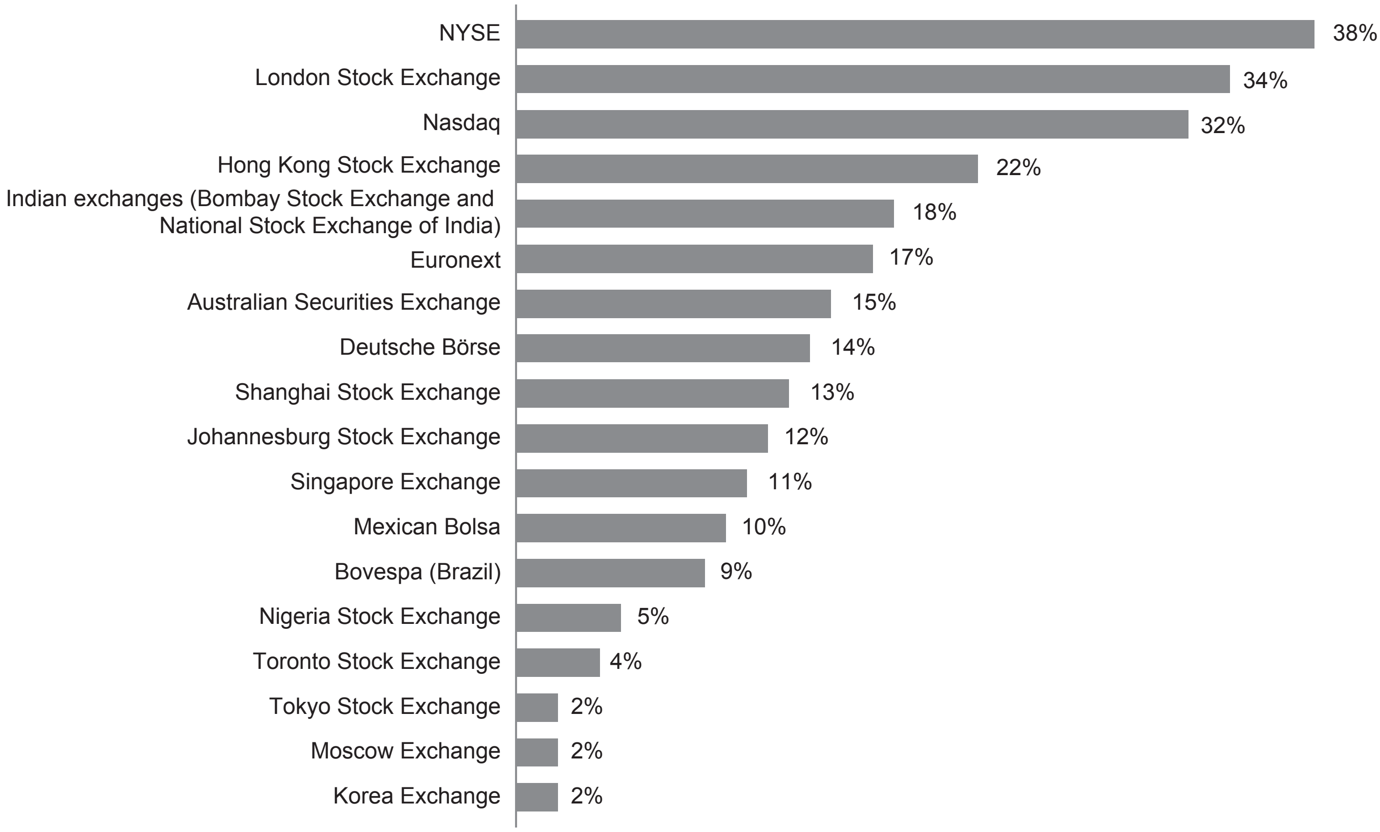
- The Shanghai exchange is moving to a registration process prior to listing, similar to Hong Kong and the US, which is expected to reduce the current lengthy wait for new issuers. Notably, in January 2019 the exchange unveiled trading rules for its much anticipated Technology Innovation Board. It will now allow unprofitable tech firms, including pre-revenue biotech startups, as well as the companies with a dual-class shareholding structure, to list on the new board, giving the Shanghai bourse greater freedom to attract promising technology startups away from New York and Hong Kong.

If local regulatory constraints are alleviated, domestic markets might prove more attractive for fast-growing Chinese companies, given how well Chinese investors understand these companies and the potential depth of their home market.

Which markets attract foreign issuers?

When survey respondents were asked which exchanges they think issuers consider beyond their home exchange when planning an IPO now, DM exchanges continued to dominate, although the proportion favouring EM exchanges has increased significantly since 2011 (see Figure 4).

Figure 4: Which of the following exchanges do you think issuers consider (beyond their home exchange) now when planning an IPO?



Source: The Economist Intelligence Unit

The biggest gains were for Indian exchanges, with 18% selecting those now versus 5% in 2011; Shanghai increased from 4% to 13%; and Brazil's Bovespa was selected by 9% today versus 5% in 2011. Other exchanges that became more attractive were Australian Securities Exchange (ASX) (from 5% to 15%) and Singapore Exchange (SGX) (from 6% to 11%). This change in view since 2011 reflects the strong performance of the Indian market, particularly in 2017 and 2018, and the growing importance of ASX and SGX as regional hubs for Southeast Asia.

Although Greater China remains the primary Asian market, India has seen significant increases in IPO activity after a period of market downturn. India may also benefit from concerns by Asian equity investors over the US's and China's growing trade rift, as India is less involved in regional supply chains than other major Asian countries such as China and South Korea.

Is the Indian market starting to fulfil its potential?

In 2017–18, 335 IPOs raised US$17.4bn, much more than in the prior five years. This is due to several factors. Political stability under Narendra Modi's government and a positive economic outlook resulted in a number of large Indian IPOs coming to market in recent years, most notably in the insurance sector. Positive changes to the Indian capital market regulations further contributed to IPO momentum.

India is expected to continue generating healthy levels of IPO activity as a result of its positive economic outlook and deepening domestic liquidity. The uncertainty surrounding this year's general elections, along with wider geopolitical factors, however, have the potential to dampen investors' appetites for Indian stocks.

"The long-term prospects are very strong," says Vikram Limaye, Managing Director and CEO of the National Stock Exchange of India, "with good demographics, increasing living standards and strong GDP growth." He points out, "Over the past couple of quarters, macroeconomic indicators have weakened, but underlying earnings growth has strengthened," which has allowed the Indian economy to stay resilient against the global economy headwinds.

The converse has applied to the DM exchanges, with significant decreases. Some 38% would consider NYSE for a non-domestic listing now versus 74% in 2011. Similarly, London has fallen from 72% to 34%. Tokyo is now referenced by only 2% of respondents, down from 12% in 2011.

This clearly represents increasing recognition that EM exchanges are growing and maturing to meet the needs of a wider population of issuers and investors. "Twenty-five-plus years ago, there were really only five options: London, New York, Tokyo, Frankfurt and Hong Kong, for large international listings," says David Erickson, senior fellow in finance at the Wharton School at the University of Pennsylvania. "That's clearly changed and, with the rise of technology and reduction on restrictions, if the access to capital is available locally, companies more often look to list locally. It's simpler."

Looking to 2030

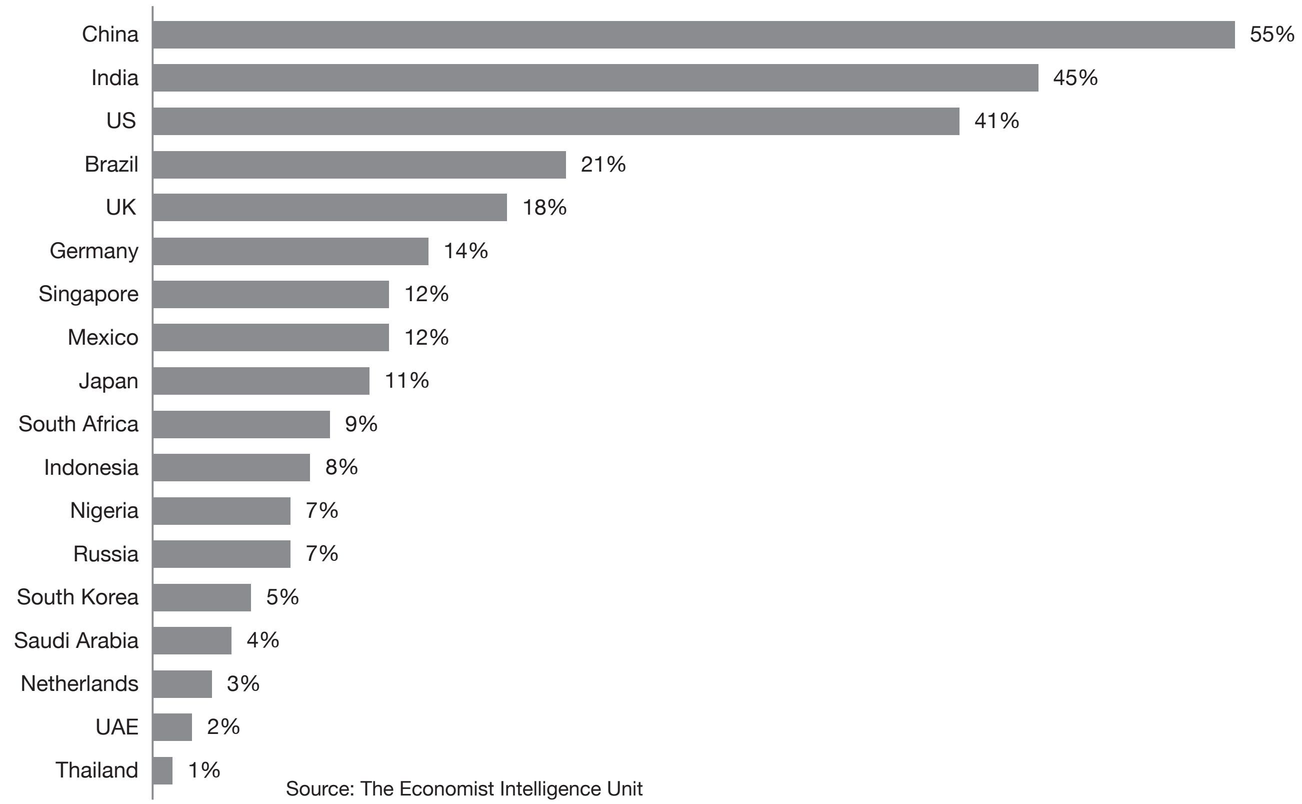
In 2011, as global markets were recovering from the 2008–09 financial crisis, globalisation was still viewed positively by both governments and their populations, and, despite concerns with respect to European and US growth, risks in emerging and developing economies were seen as less severe. Now, however, with populism and nationalism on the rise around the world, many of the fundamentals of globalisation are being challenged.

As the US looks to exit or modify trade and other international agreements and Europe focuses on its own internal tensions and managing the effects of Brexit, there may be more scope for EM economies to increase their economic and political influence on the global stage. Notably, China has been extending its influence through the Belt and Road Initiative.

In the context of capital markets, domestic growth prospects and their stage of maturity will underpin the relative advancement of EM exchanges.

Which countries will lead capital raising in 2030?

Figure 5: From which countries will most issuers originate in 2030?

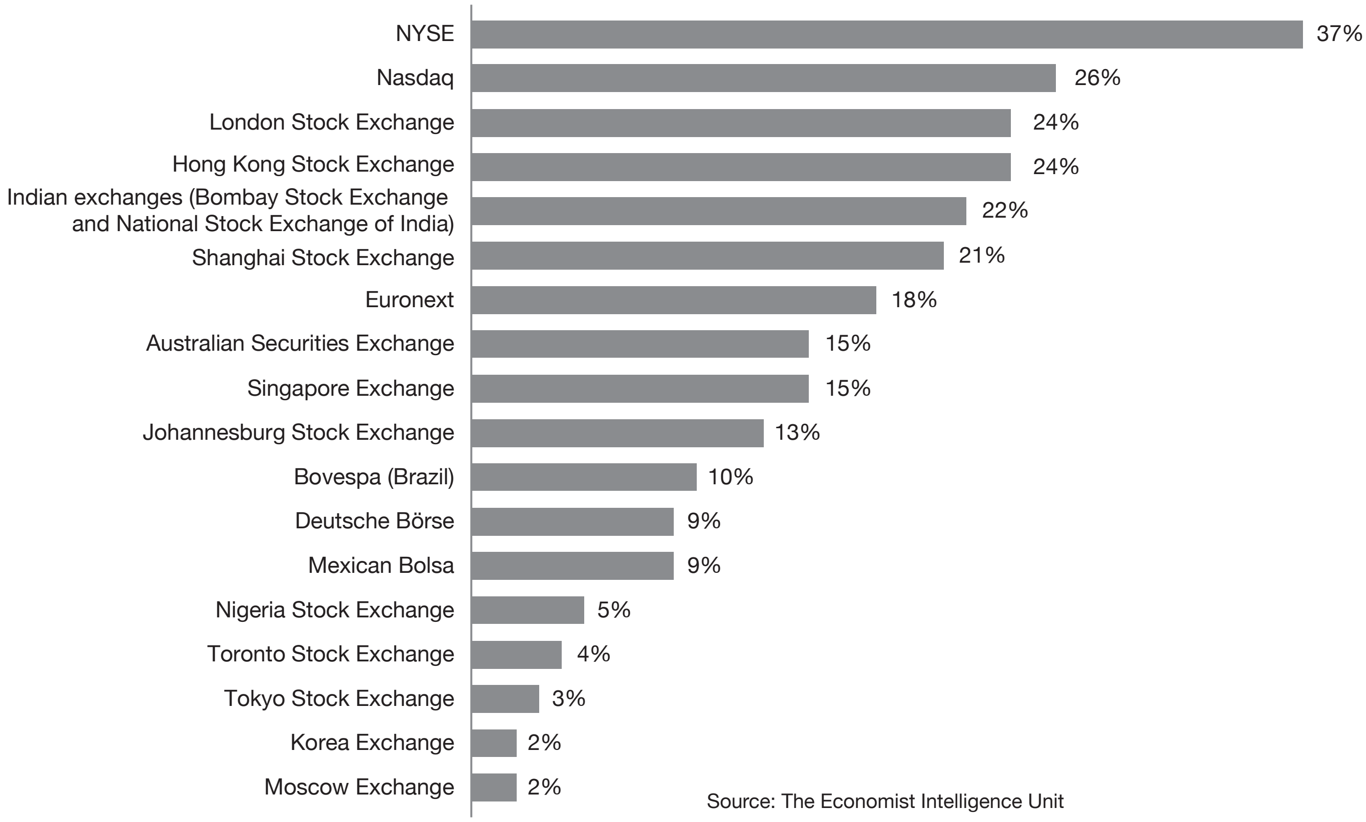


Source: The Economist Intelligence Unit

Our survey confirms the growing importance of EMs in terms of countries expected to dominate issuance by 2030 (see Figure 5). In 2011 we noted, "Companies from the East are expected to dominate the IPO pipeline by 2025. China was predicted by around 80% of respondents to be the home of most new issuers by 2025. India came second in terms of issuers, but third in terms of capital." Today, China and India continue to lead, although their expected importance has diminished substantially, which may be attributable to greater recognition of political realities and constraints in those two key markets, as well as, possibly, increased investor interest in the broader region. As noted by the HKEX's Mr Fok, "we need to look at the development of the economies around Asia. There are significant opportunities for companies in the Southeast Asian time zone; as a block, Southeast Asia is a large growth market."

This relative diminution of China and India becomes more pronounced when it comes to respondents' views on which exchanges will be considered by companies beyond a local listing by 2030 (see Figure 6).

Figure 6: Which of the following exchanges do you think issuers will consider (beyond their home exchange) in 2030 when planning an IPO?



Source: The Economist Intelligence Unit

There has been a significant reordering in how respondents think about future cross-border issuance. In 2011, respondents predicted that the Shanghai market would be the leading exchange globally by 2025, and India and Brazil would follow in third and fourth places. Our current survey places these markets in sixth, fifth and 11th place, respectively.

New York maintains its lead, and the Nasdaq has increased in popularity from 18% to 26%, perhaps as a reflection of technology sector dominance. Shanghai's popularity, on the other hand, has fallen from 55% to 21%, and India has also become less attractive despite its strong levels of activity over the past couple of years. London remains a top IPO destination despite the uncertainty that surrounds Brexit; investors do not think that IPOs will dramatically shift to Euronext or the Deutsche Börse.

Still heading East?

In 2011, respondents believed that not only would there be a rapid increase in the relative scale of the EM exchanges through local listings, but such exchanges would be increasingly attractive as listing destinations for non-domestic companies because of their investor base and local market opportunities. This has not happened, however, and now only about a third of respondents think that there would be a substantial shift in DM companies looking to EM exchanges for their IPOs in 2030.

Mr Erickson believes that the reasons DM companies are pulling back from pursuing EM listings are relatively mundane: "European companies such as Prada and L'Occitane in the past have listed primarily on the Hong Kong market for strategic reasons in order to raise their profile in the region, as Asia was their largest growth market. That's much less the case these days, and companies make the decision more on where they are based and can be included in local indices and where the best valuation is to be had." Equally, the establishment of trading mechanisms such as the Shanghai–London Stock Connect provides an opportunity to raise companies' profile in China and throughout Asia without the commitment and cost of a full listing.

Although cross-border IPOs can be expected to play a more limited role in the growth of EM exchanges, other forms of access to these markets are being actively developed.


The long march

Certain events and interventions may have slowed China's market growth. As noted by Mr Erickson, restrictions on IPOs in the Chinese mainland markets designed to control volatility in 2015, as well as large Chinese companies such as Alibaba choosing to list in the US, "potentially explain why the capitalisation gap between Chinese and US markets has widened." This, in turn, could be colouring expectations.

The speed of change in China has been slower than expected, as Hong Kong–based investment banking expert and author of *IPO: A Global Guide* Philippe Espinasse notes. "Many announcements are made on a regular basis by the regulators, but many initiatives also fail to see the light of day, or get shelved for one reason or another," he says. "To all intents and purposes, and except for a small quantum of institutions and the limited Connect schemes, the mainland's markets still remain closed to international investors and, I believe, will continue to be so for a number of years."

Nevertheless, China's fundamentals are supportive. As Mr Erickson says, "There's a lot of individual wealth: a population of 1.4bn people, and ten years ago they couldn't even buy an equity mutual fund, as they didn't yet exist in China. With 300m domestic retail accounts investing in Chinese stocks, the pot of retail money is huge." And, although international institutional money may have been deterred by the volatility and the lack of regulatory progress, the phased inclusion of A-shares in MSCI indices and the recent launching of the Shanghai–London Stock Connect indicate a Chinese market that is increasingly open.

Craig Coben, Global Head of Equity Capital Markets, Bank of America Merrill Lynch, believes it's too early to tell. He thinks that the Shanghai Connect may see significantly more capital flows between Shanghai and London, but that this is a long-term, not short-term, project.

300m

of domestic retail accounts invest in Chinese stocks.

What drives the choice of exchange?

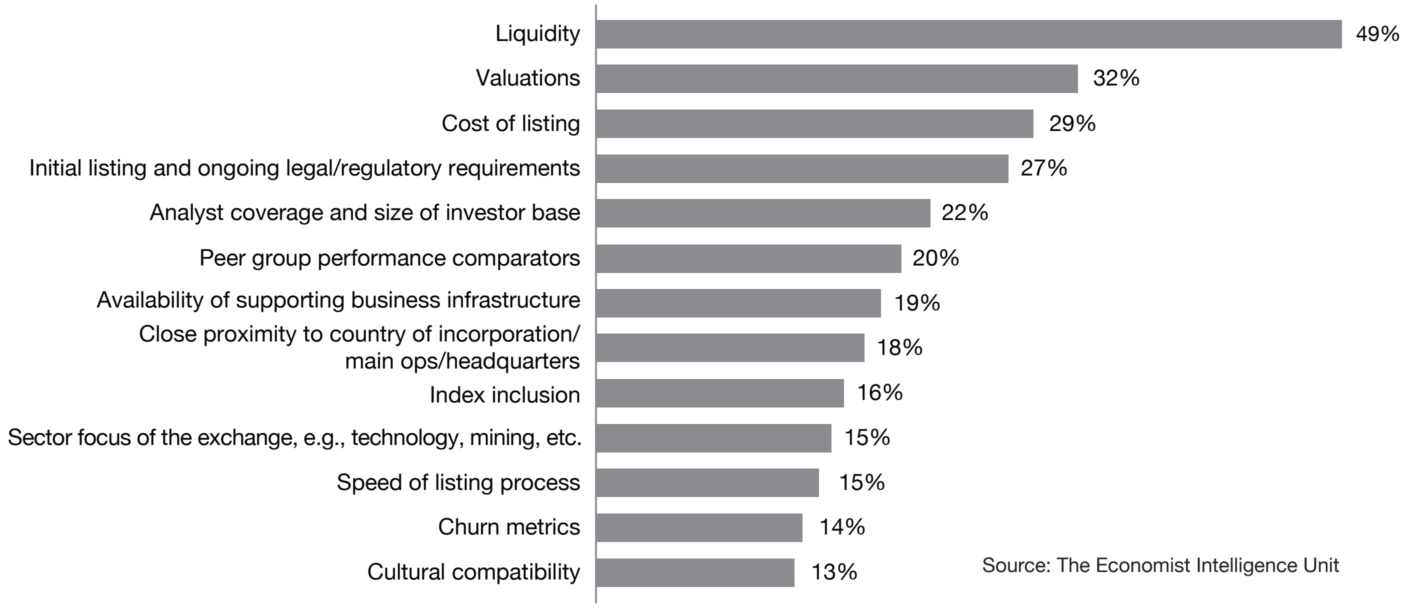
What do companies look for when choosing an exchange? What deters them? Figures 7 and 8 list some factors.

Priorities have moved slightly since 2011. Liquidity remains a constant and dominant factor and respondents are increasingly focused on valuations, the costs of listing and peer group performance. As the world has become more digitally connected, the stock market ecosystem (including analyst coverage) and size of investor base are now, however, considered less important.

Valuations were the second most important factor for respondents. Nikhil Rathi, Chief Executive of the London Stock Exchange, however, doesn't see this as a defining factor. "Any company at IPO time will be worried about valuations. They worry about whether they will be valued too low and, conversely, investors will always worry that they pay too much. I don't think we're seeing a particular shift in the market because of where participants believe we are in the cycle. Good companies in attractive sectors will always be able to attract long-term capital."

> Investors are looking for three things: sustainable growth above the level of GDP; strong cash generation; and robust margins, resilient in the face of competition.
>
> **Craig Coben**
>
> Global Head of Equity Capital Markets
> Bank of America Merrill Lynch

Figure 7: What are the most important factors when choosing a stock exchange/market for an IPO?



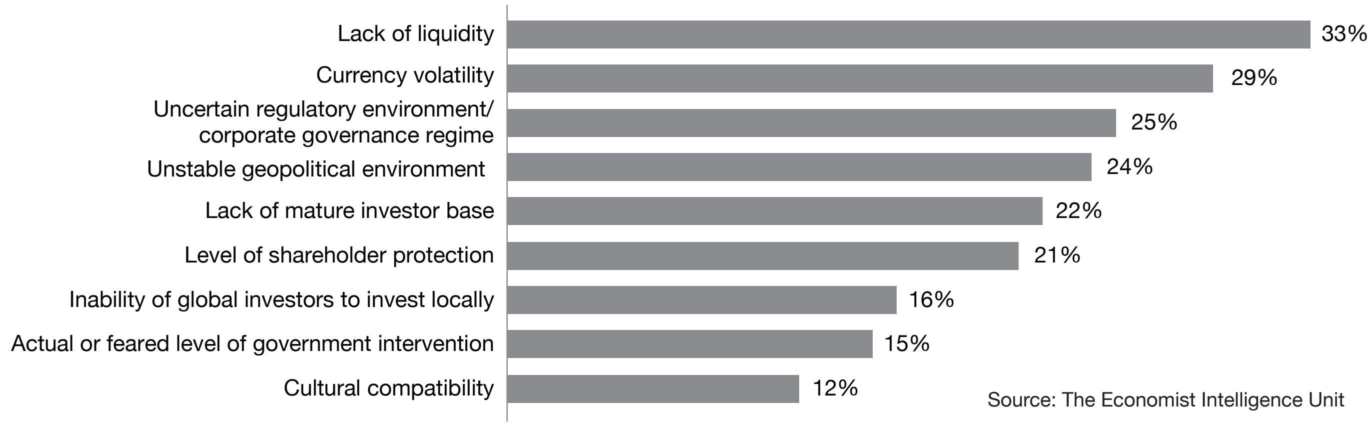
Source: The Economist Intelligence Unit

What is holding back EM exchanges?

The world has changed considerably for survey respondents since 2011. Back then, respondents were most worried by an uncertain regulatory environment (cited by 56%) and political uncertainty (33%). Now the biggest deterrents are lack of liquidity (33%) and currency volatility (29%). An uncertain regulatory environment/corporate governance regime is cited by only 25%. What is clear is that liquidity remains the main factor for issuers deciding on where to list (see Figure 8).

33% of our respondents are worried by lack of liquidity.

Figure 8: What are the main concerns with listing on an emerging market stock exchange?



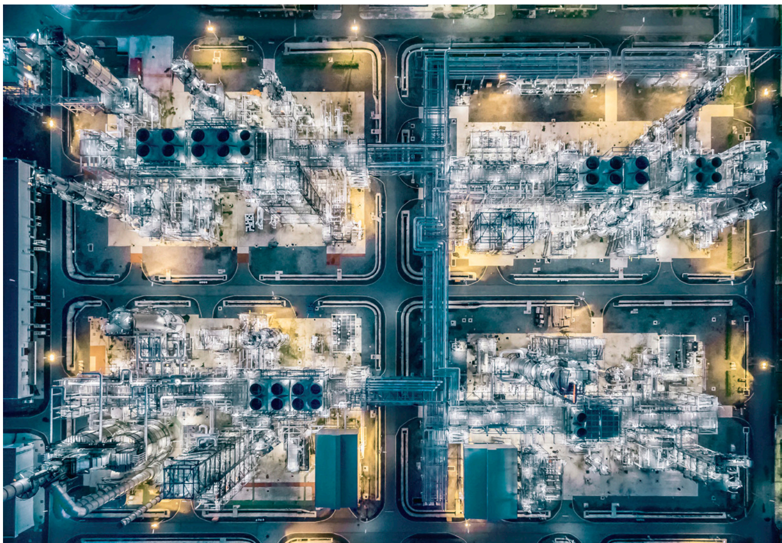
Source: The Economist Intelligence Unit

Corporate governance tightens up

When it comes to concerns about corporate governance, EMs are increasingly paying attention. Vikram Limaye, Managing Director and CEO of the National Stock Exchange of India, says that strengthening governance has been a focus area for Indian regulators and government, citing the recent Kotak Committee report's recommendations, which "are being implemented as we speak." He says there is an increasing awareness that corporate governance lapses "will not be taken lightly," but concedes "we still have a long way to go."

More generally, says Mr Espinasse, governance in the more established EMs, such as Hong Kong, Singapore, Malaysia, South Korea and Taiwan, "is actually pretty much on par with that in major markets in the US or Europe nowadays." The main difference is that investors in EM cannot initiate class action lawsuits, unlike in the US, "so the 'bite' and consequences of poor governance for issuers in emerging markets are not as significant," although he says "this is slowly changing."

Mr Coben places such concerns in the context of the broader market environment. He says, "Emerging markets have sold off, driven by rising US rates and a rising dollar. There seems no reason to believe that governance has declined in emerging markets — quite the reverse, if anything — but concerns over EM governance become amplified when the overall EM thesis comes under pressure in environments such as this."



Geopolitical risk remains a drag

For Hassan El-Khatib, Managing Director of Equity at the European Bank for Reconstruction and Development, “Geopolitical concerns are definitely top of the list.” The growth of nationalism in many countries in Eastern Europe is an example, “and we are trying to warn governments of the dangers of this,” he says. “Poland has the opportunity to be a regional hub that could capture the ten to 12 countries around it with the appropriate framework, but you need a regulatory and legal system that is conducive to this.”

Although geopolitical risks are endemic, risk perception differs between EMs and DMs; market participants expect a rougher ride in the former when turbulence hits. “Investors are looking for IPOs made of bricks, not straw, so when the big bad wolf comes knocking — be it in the form of trade wars, volatility or whatever — the investment can withstand it,” says Mr Coben. The view is that, considering historical experience, DM exchanges are more resilient.

There are a number of geopolitical risks that may, at least in the short term, override the positive developments and fundamentals, with disproportionate effects on emerging economies. One key risk in The Economist Intelligence Unit’s view is the US–China trade war morphing into a global trade war. Another key risk is cyberattacks. These could transcend borders and cripple large parts of global supply chains, disrupting global trade.

Mr Rathi at the LSE takes a relatively sanguine approach to geopolitical risk. “Markets are accustomed to evaluating all sorts of risk, whether geopolitical, financial or — increasingly — climate. Investors are very good at pricing in these risks,” he says. While global trade challenges may affect such matters as equity performance and profitability, London had more than 110 IPOs and new listings in 2018. Mr Rathi believes “investors continue to see through geopolitical complexity to company fundamentals.”

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Markets are accustomed to evaluating all sorts of risk, whether geopolitical, financial or — increasingly — climate. Investors are very good at pricing in these risks.

Nikhil Rathi

CEO, London Stock Exchange

DM advantages

When asked about whether stock markets in DMs have advantages that will be difficult for EM exchanges to overcome in the near future, respondents’ view has changed: in 2011, only 18% of respondents felt this to be the case, whereas today nearly 53% agree.

This links back to the overarching focus on liquidity. Most EM exchanges still don’t have the liquidity to rival their DM counterparts. Larger companies in many EMs need to be able to tap into deep pools of capital not yet available in their home markets. “Turkey is a good example,” Mr El-Khatib says. “There are some fantastic Turkish companies, many of which are exporting the majority of their output, despite the turmoil. Indeed, the lira’s weakness helps them. But the country’s overall situation does not, and they are often looking to list in a market with more liquidity and stability, and fewer drawbacks,” he explains.

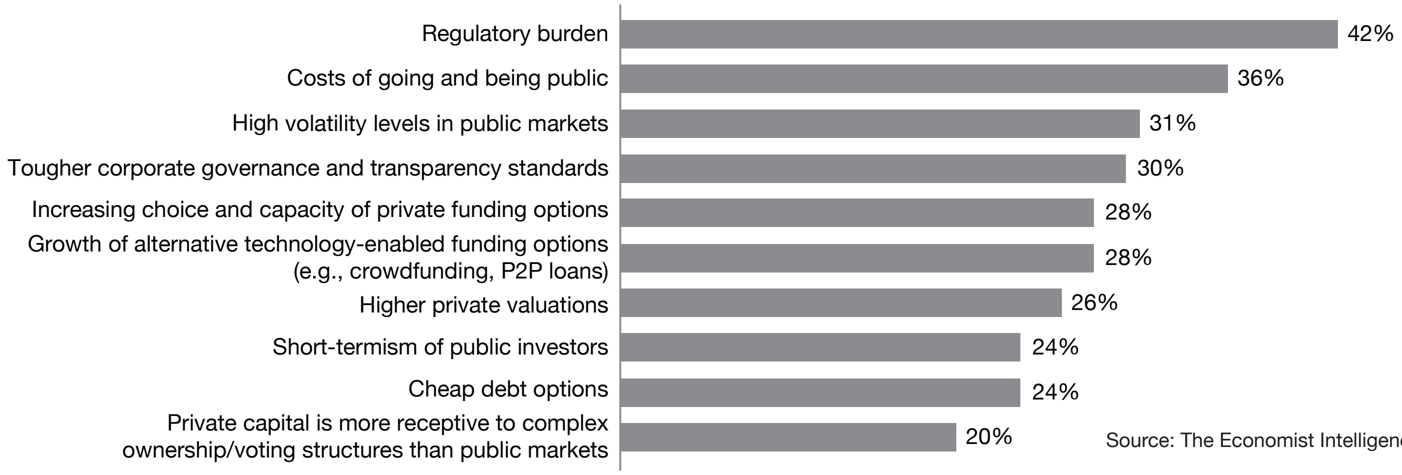
Certain DM exchanges have very specific advantages. As noted by Mr Erickson, “The US represents the largest pool of growth investors, so is still the strongest pull for tech companies, Alibaba being an example.” Mr Espinasse agrees that although a domestic listing will be the rule for most, the exception is technology companies, “a number of which will often consider listing in the US, with a view to achieving higher valuations as a result of US investors’ familiarity with the industry.” He also singles out resources companies, which “often tend to list in London, Toronto or Sydney, essentially for the same reasons.”

The US’s domination may, however, be challenged. According to Mr Limaye, a decade ago Indian tech companies would have naturally listed offshore, whereas now they are actively considering a domestic listing, supported by the strong growth of the domestic asset management industry.

Nevertheless, it looks like DM exchanges’ reputation for stability in the face of adversity has been upheld. As noted by the LSE’s Mr Rathi, “Over the recent period, we have seen significant geopolitical events, such as the Brexit vote and the US presidential election. Throughout this period, liquidity and activity have been strong, and investors have been able to get in and out of stocks at prices acceptable to them.”

Are public equity markets under threat?

Figure 9: What may cause public equity markets to decline in popularity?



Source: The Economist Intelligence Unit

Consistent with the finding that the cost of listing is now seen as a more important factor when deciding on the listing destination, the cost of going and being public has also become a more pressing concern, with 36% of respondents citing it as a cause for public equity markets to decline in popularity (see Figure 9).

"The cost of regulation is a factor, no question," says Mr Erickson; however, this "gets bundled up with the other issues when a company decides whether to list or not."

Mr Espinasse thinks that the cost should be a minor consideration when choosing a listing venue on the part of an issuer. He says, "Listing is never a cheap exercise, but more important in my view is the aftermarket share price performance and liquidity benefits that can be derived from such listing." Mr Coben also finds the negative effects of cost of regulation "a bit overstated." He says that he has never heard of anyone saying that they are not listed because of this. For him, the standards of disclosure are probably more important.

Listing costs are substantially similar in Asia and Europe. In the US, underwriting fees tend to be significantly higher — in some cases, double the percentage of proceeds one would pay in London or Hong Kong. The US aftermarket costs of compliance and governance also tend to be higher. Mr Espinasse considers this to be logical because, he says, "an issuer statistically stands a higher chance of getting sued there than in other jurisdictions."

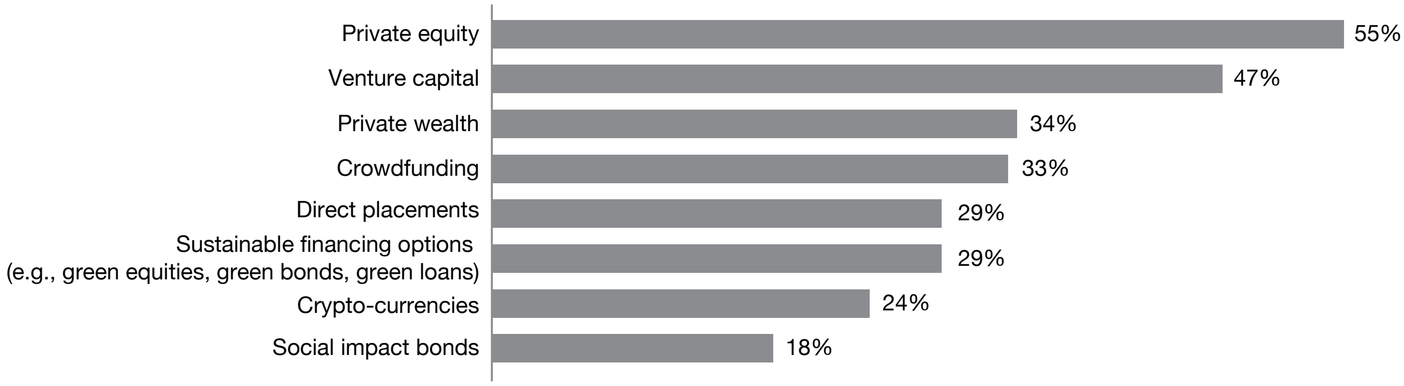
The LSE's Mr Rathi says that although there is a cost of changing regulation, this doesn't mean costs over the long term will rise. He cites the Shanghai–London Stock Connect, which should make it easier for companies and investors on both sides to raise capital and invest. "Likewise, technology is making documentation easier and faster," he says.

Mr Erickson argues that the unwieldy nature of the whole listing process is much more of an issue. He says, "In the US, it hasn't fundamentally changed from where it was when I started in the industry 25-plus years ago." Capital raising remains overly complicated and is therefore driving companies towards "more efficient" private capital markets, which have "effectively disintermediated the IPO market."

Regulators need to strike a balance between protecting investor confidence and stimulating market developments.

Private markets: To rival or to complement?

Figure 10: Which private financing options do you think are the most attractive?



Source: The Economist Intelligence Unit

Since 2011, emerging concepts and funding alternatives have started changing the face of the global financial markets. Over 75% of our respondents see that companies in both DMs and EMs now have more choices of both public and private financing routes.

Private equity (PE) and venture capital (VC) have grown substantially in the past decade as more accessible and scalable PE markets have developed in a period of relatively cheap debt. More than half of our survey respondents cite PE as an attractive option (see Figure 10).

PE remains largely a DM phenomenon, with the two largest markets being the US and Europe.

Javier Martinez-Piqueras, Global Head of Equity Capital Markets at UBS, sees PE as having “refocused on its core ‘venture capital’ mission and abandoned the pre-2008 LBO excesses,” making the role of local expertise increasingly important. He says, “I would therefore not be surprised if we see an increasing decentralisation and specialisation of PE firms, and EM economies are probably positioned to benefit disproportionately from this trend, given their lower starting point.”

Over

75%

of our respondents see that companies in both DM and EM now have more choices of both public and private financing routes.

“There’s a huge gap between the level of PE penetration in our region compared with Western Europe and the US,” says Mr El-Khatib. He says that PE works in a fashion complementary to public markets and is proving to be a major source of listing as the PE houses exit, giving the examples of Hungarian road transport firm Waberer’s, the Profi supermarket chain in Romania and the recent IPO of Play, Poland’s second-largest mobile operator.

PE is seen as a complement to public equity, rather than simply as a rival, in India as well. “PE companies have been investing large amounts of capital over the past several years, and many are now looking for exits,” says Mr Limaye. PE firms in India tend to have minority holdings of about 20 to 30%, on average. “This is expected to result in a large number of IPO exits over the next few years,” he adds.

Some see inherent advantages in PE, however, that give it an edge over public markets. “Companies don’t need to go public so much these days to raise capital,” says Mr Erickson, citing the US$1.7tn of dry powder that the PE industry can draw on. China’s Ant Financial is an example of a company that has been rumoured to be going public for the past year and that has raised US$14bn from PE investors.

“Talking to partners at VC and PE firms — why would they IPO a company if they can sell for a similar price to another PE firm or corporate buyer?” asks Mr Erickson. He says, “They don’t have to worry about not maximising price in the IPO and the lockup restrictions they will have on potential sales. And they don’t have to worry about the quarterly reporting and other regulatory issues.”

Although 50% of respondents believe a public listing is becoming a less important source of funding globally, about 70% of survey respondents think it would be advantageous for successful companies to go public at some point in their life cycle. This is in line with Mr Fok's observation that the availability of capital in private markets means companies are listing at later stages, are larger and more sophisticated, and so will choose one of the leading exchanges.

Ultimately, therefore, rather than simply being seen as rivals to public equity markets, companies increasingly consider private markets to be complementary sources of capital that they can tap into when appropriate, drawing on the ever-growing universe of private financing options.

It's clear that what has changed in recent years is the stage at which companies seek to list, being financed for longer by private markets. As the growth of private capital continues, its influence on the level and timing of public company listings will also increase across the globe, according to the cycles of fundraising and exits.

"There is a blurring of boundaries in how companies raise capital: crowdfunding, private equity and sovereign wealth funds," according to Mr Rathi. As he says, "A company can initially capitalise through crowdfunding and then go on to list on a public market. The latter gives it the advantages of regulatory protection, transparency and a global equity base, which spreads the equity risk."

Public markets of tomorrow

In PwC's view, thriving public markets play a vital role in the health of economies, in both the DM and EM world.

In addition to the natural evolution of domestic capital markets in developing economies, reflecting deeper capacity, better infrastructure and underlying GDP trends, the future growth of public equity markets, in our view, will be affected by a range of other factors, including the following:

- **PE:** as the scale of PE continues to grow, public markets will provide an important exit route for owners, on both domestic and leading international exchanges.
- **Technology**: the technology sector will continue generating significant levels of activity in public markets, intensifying competition between exchanges — both international and domestic — to attract the 'unicorns' and other prize issuers.

- **Privatisations**: it is apparent that public markets provide a well-established avenue for privatisations. As developing economies continue to open up, more privatisations can be anticipated via an initial public offering route across the globe — particularly in Central Asia, Central and Eastern Europe, the Middle East, Southeast Asia, and parts of Africa.

- **International entrepreneurs**: as EM economies mature, entrepreneurs will continue seeking exits to raise capital for business expansion, as well as, at times, hedging political risks through a listing on an international exchange.

- **Deals**: as EMs and their exchanges become more sophisticated, more equity capital market transactions will arise as a result of public companies' mergers and acquisitions and divestments.

Conclusion

If market participants proved too exuberant over EM prospects in 2011, they are perhaps too pessimistic now. Equity markets are late cycle, and EMs have experienced significant volatility and outflows. Risk and governance concerns will naturally be more prominent in such conditions, playing to the perceived strengths of DM — established legal framework, tried and tested structures, and deep liquidity.

On the other hand, according to Mr Coben from Bank of America Merrill Lynch, markets are now looking for growth, and "as macro growth remains moderate, investors will pay a premium for companies that can deliver higher growth." This represents a significant opportunity for EM issuers with the right profile.

Despite the more subdued view on EM, respondents still expect China and India to dominate future issuance. Over time, this should support the growth of their exchanges and narrowing of the gap with the leading financial centres. Business leaders' anticipation of strong issuance and available capital from China and India is a common theme running through both our surveys, and we expect to see a long-term growing influence of the key emerging economies. The shift to EMs will continue, but it will be less seismic, more progressive, more realistic and grounded in developments since 2011.

What is clear is that the choice of credible exchanges for public listings, as well as the range of private funding routes, will continue to grow, offering ever more alternatives to companies when they seek to raise capital.

About this report

Capital markets in 2030: The future of equity capital markets is a PwC report, written by The Economist Intelligence Unit.

In July 2018, The Economist Intelligence Unit (EIU), on behalf of PwC, surveyed 370 equity capital market participants to determine their views on the future of capital markets. Respondents were drawn from around the world; 52% came from developed markets and 48% from emerging markets.

Survey respondents included C-suite executives (51%) and senior executives and managers (49%). They represented a wide range of sectors: financial services (21%); information technology (10%); manufacturing (7%); energy (7%); telecommunications (6%); healthcare (6%); consumer services (6%); consumer goods (6%); retail (6%); industrial (5%); metals and mining (5%); travel and transport (4%); utilities (4%); materials (2%); and other (4%).

In addition, The EIU conducted a series of in-depth interviews from August through December 2018 with eight stock market and finance experts from around the world. PwC would like to thank all the interviewees and executives taking part in the research in kindly giving their valuable time and insights.

The EIU bears sole responsibility for the content of this paper except where otherwise indicated. The findings and views expressed in the paper do not necessarily reflect the views of the sponsor.

In-depth interviews:

- Craig Coben,
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- Hassan El-Khatib,
  Managing Director of Equity at the European Bank for Reconstruction and Development (EBRD)
- David Erickson,
  Senior fellow in finance at the Wharton School at the University of Pennsylvania
- Philippe Espinasse,
  Investment banking expert and author of
  IPO: A Global Guide
- James Fok,
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  Hong Kong Stock Exchange (HKEX)
- Vikram Limaye,
  Managing Director and CEO of the National Stock Exchange of India
- Javier Martinez-Piqueras,
  Global Head of Equity Capital Markets,
  UBS
- Nikhil Rathi,
  Chief Executive of the London Stock Exchange

About the IPO Centre

Our IPO Centre was created to make it easier for you to understand what you need to know and to do to complete an IPO.

We bring together our knowledge of local and international capital markets to help you evaluate the pros and cons of an IPO, navigate the listing process and prepare your business for life as a public company, regardless of the market you choose to list on.

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PwC Capital Markets

We have a team of nearly 500 professionals deployed in over 30 key global capital markets. With our in-depth knowledge of the execution process and the rules and regulations governing the world's leading capital markets, we can help clients navigate every phase of the complex IPO process.

Our network of capital market specialists across the world provides a broad range of services to companies and investment banks in connection with the capital market transactions, including:

- preparation for becoming a public company
- selecting the right market and advisory team
- advising on regulatory, reporting and governance matters
- undertaking financial and business due diligence investigations
- assisting with project management of the IPO process.

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