

2016 BDO IPO OUTLOOK



ZERO GROWTH FORECAST FOR U.S. IPOs IN 2016

Difficult Year for Tech Unicorns Seeking to Go Public

After three consecutive years of healthy increases in the number of initial public offerings (IPOs) and proceeds raised on U.S. exchanges, the U.S. IPO market came back to earth in 2015, as virtually every statistical category – offerings, proceeds, filings and returns – were down significantly year-over-year.

According to the **2016 BDO IPO Outlook**, BDO USA's annual survey of capital markets executives at leading investment banks, there is no clear consensus on the reason

for the decrease in offerings. When asked to identify the primary reason behind the drop in IPOs, bankers cite – poor IPO performance discouraging other potential offerings (29%), uncertainty surrounding the potential interest rate hike by the Federal Reserve (21%) and the surge in M&A activity causing many IPO candidates to opt for a sale over the risk of an offering (21%). Smaller proportions mention a slowing US economy (16%) and the lack of offerings from traditionally strong technology and energy sectors (11%).

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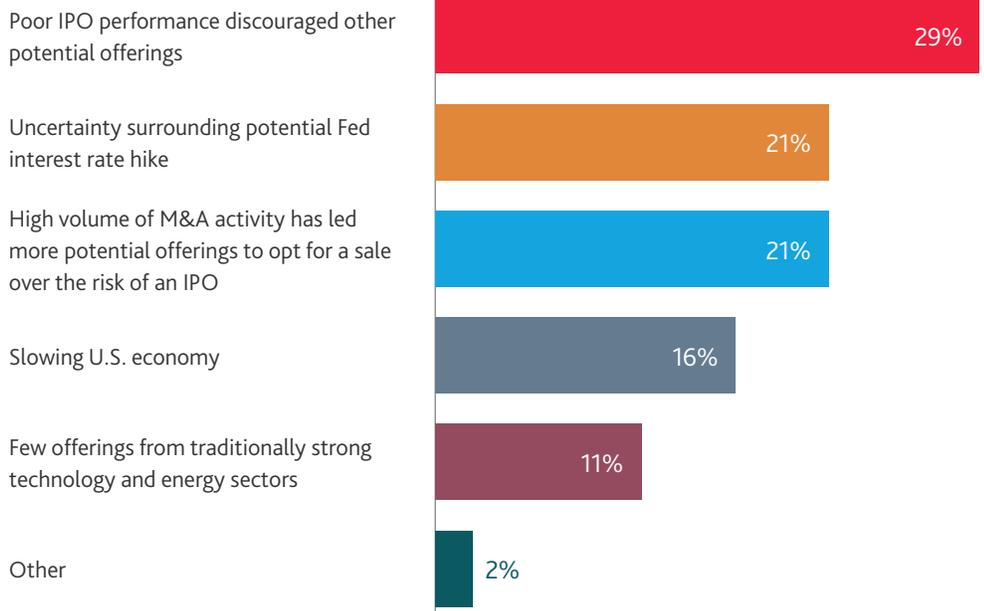
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“Given the robust growth of the U.S. IPO market during 2013 and 2014, the drop in activity in 2015 was to be expected to some extent. While the number of offerings in 2015 is off considerably from the two previous years, it is actually slightly above the average for the previous decade,” said **Ted Vaughan, Partner in the Capital Markets Practice at BDO USA**. “Moving forward, the flat forecast for 2016, a first in the seven years we’ve conducted this survey, is certainly concerning. When one considers that the chief factors the bankers identify for this year’s downturn in offerings are still very much with us as we approach the new year, it is understandable why they are less than optimistic about the outlook for growth in IPO activity in 2016.”

Looking forward, I-bankers are forecasting similar results in 2016. Thirty-seven percent of the capital markets community predict an increase in U.S. IPOs in the coming year, although only 4 percent believe it will be a substantial jump, while an almost identical proportion (36%) forecast activity as flat compared with 2015. Just over a quarter (27%) expect a decrease in offerings on domestic exchanges. Overall, bankers predict the number of U.S. IPOs in 2016 will be about the same as 2015 (+.15%). However, they anticipate these offerings will average \$219 million in size, which projects to \$37 billion in total IPO proceeds on U.S. exchanges, an increase of 23 percent from 2015.

IPO activity on U.S. exchanges has fallen considerably in 2015. What one factor do you feel has had the greatest impact on this decrease?



Source: 2016 BDO IPO OUTLOOK

SOURCES & ATTRIBUTES OF 2016 IPOs

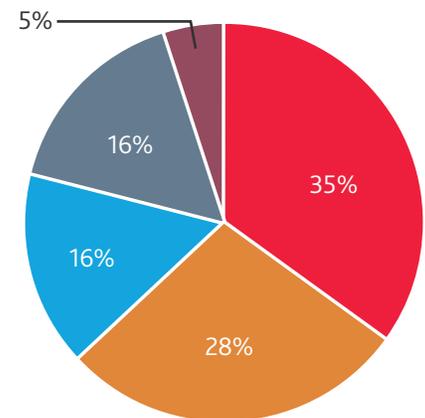
Private equity (47%) is the most often mentioned source of IPOs for the coming year. Spinoffs and divestitures (26%), venture capital portfolios (18%) and owner managed privately-held businesses (9%) are the other sources identified by bankers.

When asked what offering attribute will be most valued by the investment community in 2016, more than one-third (35%) of bankers cite long-term growth potential and over one-quarter (28%) identify businesses with innovative products or offerings. Stable cash flow (16%), profitability (16%) and low debt (5%) are cited by smaller proportions of participants.

In 2016, the investment banking community is predicting an average offering size of \$219 million for U.S. IPOs. They are also forecasting one-day returns of 12 percent and overall returns of 2 percent for the average IPO. Each of these figures is in line with this year's disappointing performance, reinforcing the capital markets community's subdued expectations as we enter 2016.

What one attribute of potential offerings will be most valued by the investment community in 2016?

- Long-term growth potential
- Innovative business
- Stable cash flow
- Profitability
- Low debt



Source: 2016 BDO IPO OUTLOOK

“U.S. IPO proceeds are down by more than 60 percent from 2014, the largest drop of any of the statistical categories. Absent mega-offerings, such as an Alibaba or Facebook, it will be difficult for IPO proceeds to reach the heights achieved in 2014, as the overwhelming majority of U.S. offerings in 2015 have been by companies with less than \$1 billion in annual revenue,” said **Chris Smith, Partner in the Capital Markets Practice at BDO USA**. “This trend is an outgrowth of the Jumpstart Our Business Startups (JOBS) Act, enacted in 2012 to make it easier for firms with less than \$1 billion in annual revenue to tap the public markets by reducing costs and regulatory burdens. Moving forward the health of the U.S. IPO market will be more tightly linked to the number of offerings versus total proceeds raised.”



INDUSTRIES

For three consecutive years, the healthcare industry has been the bellwether of the U.S. IPO market. In 2015, the healthcare sector spawned three times the number of offerings from any other industry. In 2016, close to two-thirds (62%) of those in the investment banking community are predicting a further increase in offerings from the healthcare industry and lesser majorities are forecasting an increase in IPOs in technology (59%) and biotech (57%). No other industry is predicted to achieve an increase in IPOs by a majority of the survey participants. (see full chart on the right).

Proportions of Capital Markets Executives expecting IPO activity to increase, remain stable or decrease in specific industries.

INDUSTRY	INCREASE	FLAT	DECREASE
Healthcare	62%	26%	12%
Technology	59%	33%	8%
Biotech	57%	29%	14%
Financial	31%	42%	27%
Real Estate	31%	33%	36%
Energy / Natural Resources	30%	22%	48%
Media / Telecom	29%	42%	29%
Consumer / Retail	18%	40%	42%
Industrial / Manufacturing	17%	52%	31%

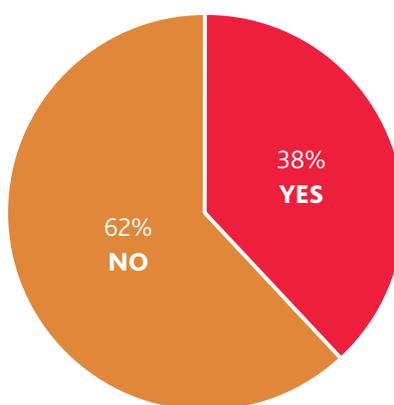
TECH TAKES AN IPO HOLIDAY

In recent years, many businesses, especially technology companies, have put off their IPOs due to the widespread availability of private financing at extremely attractive valuations. Currently there are more than 100 private companies valued by VC firms at \$1 billion or more. When asked about the valuations of these "tech unicorns", close to two-thirds (62%) of investment bankers do not believe these valuations will be supported in the public markets.

Due to these inflated valuations and the pricing pressures brought about by this year's poor IPO performance, a majority (60%) of capital markets executives anticipate the tech sector will remain a marginal player in the 2016 IPO market. Moreover, close to half (47%) of bankers believe a correction in the valuations of highly visible, pre-IPO tech companies may cause investors to lose confidence and lead them to avoid the risk of new offerings to the public markets.

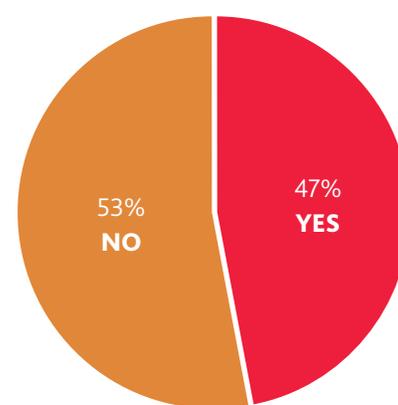
Close to three-quarters (73%) of the capital markets community believe private company marketplaces, such as Nasdaq Private Market and Second Market, can serve as an effective tool to correct inflated valuations prior to an IPO coming to market.

Currently there are more than 100 private companies valued by VC firms at \$1 billion or more. In general, do you believe these valuations would be supported in today's public markets?



Source: 2016 BDO IPO OUTLOOK

Do you believe a correction in pre-IPO tech companies will have a chain reaction causing investors to avoid the risk of new offerings?



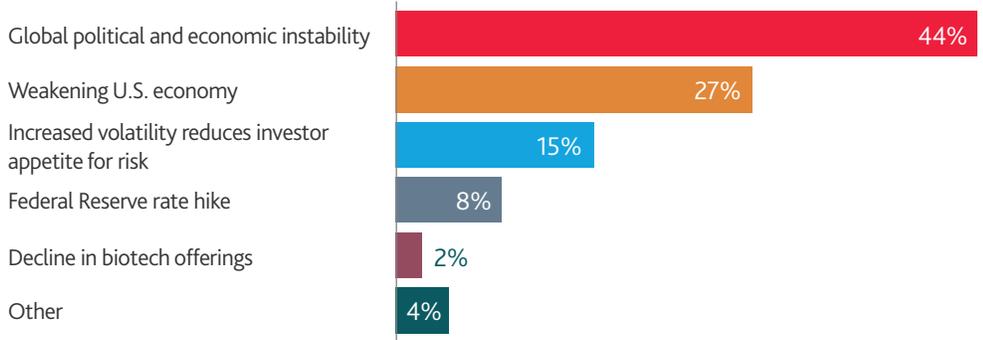
Source: 2016 BDO IPO OUTLOOK

"Given the reduced demand for highly anticipated public offerings by Square and other technology companies, private investors, who have previously valued tech startups at \$1 billion or more, are likely to avoid new deals unless these businesses are willing to raise money at lower values. The combination of potentially lower valuations and lower capital availability for late-stage private rounds should encourage some companies to move toward the IPO process, but many others will still turn to a private sale," said **Lee Duran, Partner in the Capital Markets Practice of BDO USA**. "U.S. companies are now dropping initial public offerings and selling themselves at the highest rate in years as M&A activity has surged. The technology sector has been one of the chief drivers of U.S. M&A activity in 2015. Given the uncertainty of the current IPO market, company owners are increasingly likely to find an attractive offer from a potential acquirer more appealing than the inherent risk of an IPO."

IPO THREATS

When asked to comment upon the greatest threat to a healthy U.S. IPO market in 2016, close to half (44%) of I-bankers cite global political and economic instability. More than a quarter (27%) specifically identify a weakening US economy. Smaller minorities focused on reduced investor appetite for risk (15%), a Federal Reserve rate hike (8%) and a major decline in biotech offerings (2%).

What do you consider to be the greatest threat to a healthy U.S. IPO market in 2016?



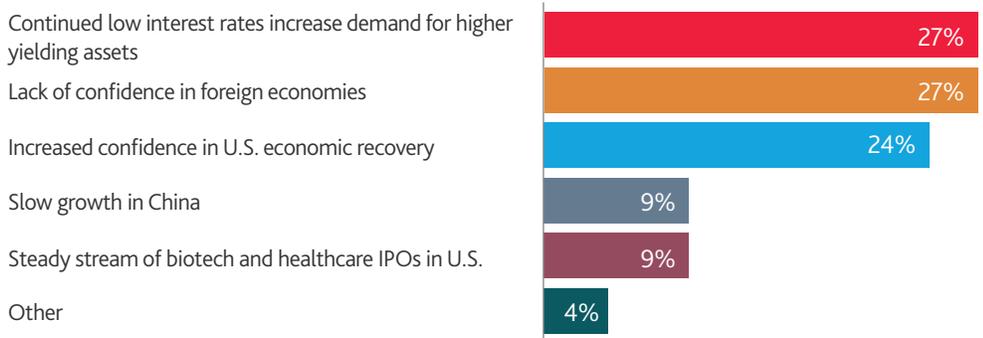
Source: 2016 BDO IPO OUTLOOK

GLOBAL IPOs

The U.S. led all countries in IPO proceeds in 2015, generating 17 percent of total global proceeds. When asked to identify the chief factor driving this trend, the capital markets community is divided among three main areas - continued low interest rates increasing demand for higher yielding assets (27%), a lack of confidence in foreign economies (27%) and increased investor confidence in the U.S. economic recovery (24%). Slow growth in China (9%) and a steady stream of biotech and healthcare IPOs in the US (9%) are other factors mentioned by smaller proportions of the bankers.

Moving forward, 42 percent of I-bankers believe U.S. exchanges will increase their share of global IPO proceeds during the coming year, although only 5 percent describe the increase as substantial. An identical percentage (42%) predict the U.S. cut of the global pie will remain about the same as 2015. Just sixteen percent anticipate the U.S. share will decline in 2016.

What one factor do you believe had the greatest impact on the U.S. exchanges maintaining their leadership in total global IPO proceeds in 2014?



Source: 2016 BDO IPO OUTLOOK

More than one-third (38%) of capital markets executives believe the number of foreign-based IPOs on U.S. exchanges will increase in the coming year, though only 4 percent describe the increase as substantial. A similar percentage (35%) expect the number of foreign-based offerings to remain about the same as 2015 and more than one-quarter (27%) predict a decrease in foreign-based offerings. A majority of the bankers (59%) identify Asia as the geographic location most likely to spawn foreign-based

IPOs on U.S. exchanges in 2016. Europe (19%) and Latin America (11%) are other regions cited by sizable proportions of bankers.

In terms of which foreign exchanges will be most popular for IPOs in 2016, Hong Kong (21%), London (19%) and Shanghai (18%) were the exchanges most frequently mentioned by bankers.



ABOUT THE SURVEY

These findings are from *The 2016 BDO IPO Outlook* survey, a national telephone survey conducted by Market Measurement, Inc. on behalf of the Capital Markets Practice of BDO USA. Executive interviewers spoke directly to 100 capital markets executives at leading investment banks regarding the market for initial public offerings in the United States in the coming year. The survey, which took place in late November and early December of 2015, was conducted within a scientifically-developed, pure random sample of the nation's leading investment banks.

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