Corporate Debt, Turnaround & Restructuring

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SOUTH AFRICA

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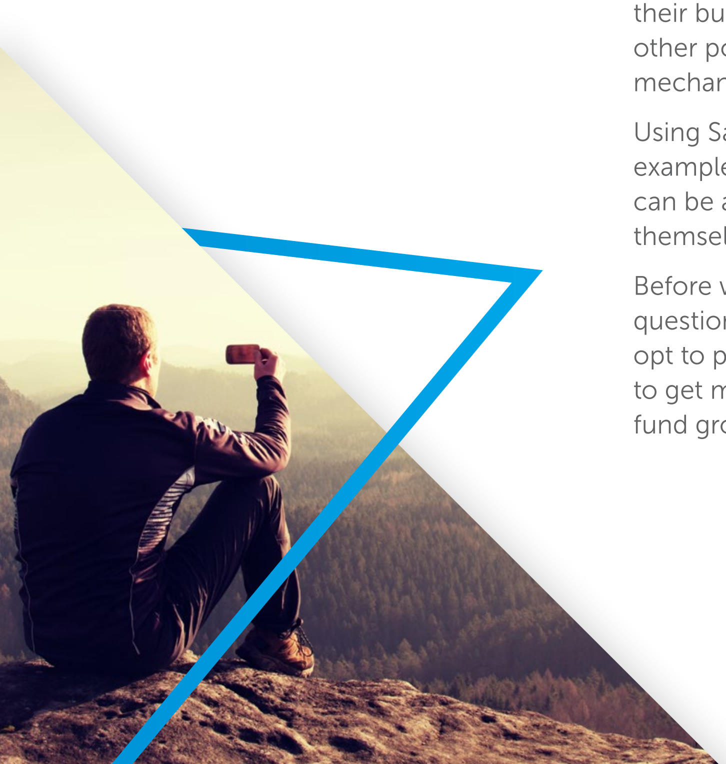
Trading floor to boardroom door: The strategic power of delisting



South African stock markets are experiencing lower levels of liquidity, particularly in small- and medium-cap companies, due to a trend by institutional and other significant investors towards investment in larger, more liquid companies, driven in part by a growth in exchange traded funds, whose index spread mitigates risk for investors. Ultimately small- to medium-cap listed companies are perhaps becoming less relevant in the investor universe and are finding it more difficult to attract and raise equity capital through the public markets.

It is in this context that listed companies will be required to consider their capital strategy to ensure a viable future for their business and value for their stakeholders. Amongst other potential strategies, delisting may be a useful mechanism to contribute to a strategic turnaround.

Using Sasfin's recent proposed delisting as a prime example, we unpack how exiting the listed environment can be a savvy move for companies looking to reinvent themselves and set the stage for future success.

Before we tackle the concept of delisting, let's ask the question: why list in the first place? Companies generally opt to publicly list on one or more stock exchanges to get more ready access to equity capital in order to fund growth.

However, in the South African market in recent years, listed companies have generally found it increasingly challenging to raise equity capital for a number of reasons, such as economic uncertainty and reduced investor confidence. In addition, equity capital is also more expensive than loan capital. For example, interest payments on debt are tax-deductible, which can lower the effective cost of debt. Equity dividends, however, are paid from after-tax profits, making equity more expensive for companies from a tax perspective.

With that being the case, if a company cannot raise equity in the market, or raising equity comes at a high price, companies may ask themselves: why remain listed?

Part of the value trade-off of being listed is the additional costs embedded in maintaining a listing on a securities exchange, such as the cost of listing, advisory and non-executive directors' fees, etc. Listed entities must also factor in the wasted opportunity cost of compliance – management will be required to spend a considerable amount of time away from running the company's business to adhere to a demanding regulatory and reporting environment. The regulatory overlay imposed by the securities exchange also creates an additional compliance layer which may impede the company's ability to nimbly pursue transactions and other opportunities. In addition, the company may wish to rather direct its administrative spending towards investments.

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In light of these costs, delisting may for some companies free-up much needed capital and resources as well as enable companies to respond to market conditions or pursue opportunities with less regulatory compliance burdens. For those companies, the benefits of delisting may outweigh the net benefits of being listed.

From a foreign investment point of view, the source of offshore capital will often determine an investor's view of delisting. While institutional money, such as unit trusts and pension funds, may want to exit (or be required to exit in terms of its investment mandate) when a company goes private, sources coming from private equity, development financiers and traders may want to jump at taking companies private.

Sasfin's rationale for its proposed delisting included furthering its strategic action in an unlisted environment, eliminating ongoing costs associated with being listed, and supporting the growth of Sasfin Wealth with material commitments by Sasfin Holdings' two largest shareholders and the management of Sasfin Wealth.

It comes as no surprise that Sasfin has said that delisting is an optimal strategy as it currently has a limited free float. As an unlisted company, Sasfin will be able to execute on its strategic reset, which will include further strategic actions.

An entity looking to adapt to changing market conditions, escape a rigid regulatory environment and reduce the high costs of being listed ought to at least consider a delisting as part of its business turnaround strategy, because it can be value constructive.

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BBBEE STATUS: LEVEL ONE CONTRIBUTOR
Our BBBEE verification is one of several components of our transformation strategy and we continue to seek ways of improving it in a meaningful manner.

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