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Global Offering of Shares Listed on the Korea Exchange

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International Investors Take Note

Dong Chul Kim of Paul Hastings Charts the Rise of International Offerings by Korean Issuers

In the fourth quarter of 2014, two large initial public offerings (IPOs) of Samsung Group affiliates, Samsung SDS and Cheil Industries, drew the attention of the international investment community. The IPOs raised approximately $1.1 billion and $1.4 billion respectively, making them the two largest IPOs in Korea in 2014. These IPOs were well received not only among Korean investors but among international investors and were heavily oversubscribed. This article provides background information on how Korean IPOs are sold to international investors.

Following POSCO

Starting from POSCO's first-ever listing on the New York Stock Exchange as a Korean company in 1994, several blue-chip corporate issuers and financial institutions followed suit, listing their American depositary receipts (generally known as ADRs and which facilitate payment of dividends and trading in the U.S.) on the New York Stock Exchange in the late 1990s and early 2000s. These issuers included Korea Telecom, SK Telecom, Korea Electric Power Corporation, LG Display, KB Financial Group, Woori Financial Group and Shinhan Financial Group. Meanwhile, a few start-up companies in the technology sector sought listings on the NASDAQ, which generally offered the most favourable valuation to tech companies. For example, Thrunet listed its shares on NASDAQ in 1999 during the internet bubble (although it was later delisted) while companies like G-market, Gravity and Pixelplus listed on NASDAQ in the mid-2000s. Since the mid-2000s, however, listings in the U.S. became less popular among Korean issuers (like other non-U.S. issuers), due in part to the tightened corporate governance standards and certification requirements under the Sarbanes-Oxley Act. Instead, Korean companies seeking to raise money from foreign investors sought other listing venues such as London or Singapore. For example, STX Pan Ocean listed its shares on the Singapore Exchange in 2005 and Lotte Shopping listed its shares on the London Stock Exchange and the Korea Exchange simultaneously in 2006, which raised $3.7 billion.

Amendment to Listing Rules

In 2007, the amendment of the listing rules in Korea that permitted Korean companies listing on the Korea Exchange to offer their shares to foreign investors in the IPO process brought about a significant change in Korean companies' equity financings from foreign investors. Since then, most of the large IPOs in Korea, such as the IPOs of Samsung Life, the largest ever by a Korean issuer, Samsung Card, Mando, Hi-mart and CJ HelloVision, featured an overseas tranche which was offered to institutional investors in the US and other foreign countries. The growth of the Korea Exchange in size and the recognition of it as a reliable market among foreign institutional investors also contributed to this trend.

The following table shows a list of IPOs listed on the Korea Exchange which included an international tranche:

	Issuer	Industry	Year	Size ($ million)	Int'l Offering Format
1	Samsung Card	Credit card	2007	530	144A/Reg S
2	STX PanOcean	Shipping	2007	545	144A/Reg S
3	Tong Yang Life Insurance	Life insurance	2009	315	144A/Reg S
4	Jinro	Beverage	2009	545	Reg S only
5	SK C&C	IT services	2009	500	144A/Reg S
6	Korea Life Insurance	Life insurance	2010	1,650	144A/Reg S
7	Samsung Life Insurance	Life insurance	2010	4,525	144A/Reg S
8	Mando	Auto parts	2010	460	144A/Reg S
9	Hyundai HCN	Cable TV	2010	80	144A/Reg S
10	Hi-Mart	Retail	2011	390	144A/Reg S
11	CJ HelloVision	Cable TV	2012	270	144A/Reg S
12	Hyundai Rotem	Industrial	2013	575	144A/Reg S
13	Samsung SDS	IT services	2014	1,100	144A/Reg S
14	Cheil Industries	Leisure and fashion	2014	1,410	144A/Reg S

International Offerings: Pros and Cons

From the issuer's point of view, selling shares to international investors in its IPO has both pros and cons. The primary benefits of offering the shares to international investors include the positive effect on pricing by bringing in a larger pool of investors and the opportunity to broaden the international shareholder base. International institutional investors also tend to hold the shares for a longer period than retail investors, helping to stabilise the share price following the IPO. These benefits are mostly highlighted in larger offerings, where it is necessary to find sufficient demand for the offering beyond the amount of capital available in the domestic market.

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On the other hand, international offerings increase the risk of investor lawsuits under US or other securities laws that may be more investor friendly than the Korean law. International offerings also entail the additional cost of preparing offering documents in English in accordance with the international standard, the fees of international counsel and accounting firms and expenses for global roadshows. Accordingly, only the large IPOs, usually with an offering size of more than $300 to $500 million tend to have an international tranche. For this reason, most of the issuers that chose to have an international tranche were established companies affiliated with large Korean conglomerates, or chaebols, rather than start-up companies.

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Underwriting Procedures

As these offerings are sold to both Korean and international investors, issuers need to engage international investment banks, as well as Korean securities firms, as underwriters. They enter into two separate underwriting agreements with the issuer—a standard Korean-style underwriting agreement covering the entire offering and an international underwriting agreement covering the international tranche. While the offering mechanics and subscription procedures are set out in the Korean underwriting agreement, the international underwriting agreement contains standard representations and warranties of the issuer, U.S.-style indemnity provisions for misstatements or omissions contained in the disclosure documents, and typical closing conditions and termination provisions found in international securities offerings. In order to comply with Korean regulations, underwriting agreements are first signed at the time of filing the Korean securities registration statement, which are subject to the confirmation of pricing and signing of the final underwriting agreement. The final underwriting agreement with the final price is signed immediately after pricing.

In addition, two sets of offering documents are prepared. For Korean investors, a Korean securities registration statement including a Korean prospectus, is filed with the Financial Supervisory Service of Korea (FSS), which is the regulator overseeing the financial markets. For international investors, an offering circular is prepared in accordance with the international market standards, including English financial statements prepared under Korean international financial reporting standards (IFRS) and management's discussion and analysis (MD&A) of the financial information. Considerable effort is taken to ensure that the Korean offering document is consistent with the international offering document, as any inconsistent statement could increase legal risk. In this process, certain sections of the offering circular, such as the risk factors and MD&A are often translated into Korean and included in the Korean prospectus.

As with many other countries, the Korean prospectus is reviewed by the FSS, and sometimes the FSS provides material comments that can delay the offering process. Therefore, it is essential to prepare the prospectus carefully and build a cushion into the timetable to reflect any material comments from the FSS. In addition, the Korea Exchange reviews the eligibility of the issuer's shares for listing before the offering process begins and sometimes it takes a considerable amount of time to clear the Korea Exchange's review process. These offerings are typically not registered in any other country and sold only to institutional investors outside of Korea relying on Rule 144A/Regulation S under the U.S. Securities Act.

Some of the peculiar aspects of the Korean IPO process can raise issues in the context of the international offering. In Korean IPOs, the shares start trading a few days after the closing, which can be up to two weeks after pricing. The investors are exposed to any adverse developments affecting the issuer during this period, while they are not able to trade the shares. Another Korean regulatory requirement that often raises issues is the requirement to include underwriters' valuation of the issuer in the Korean prospectus, which underwriters can be uncomfortable with.

Looking Ahead

It is expected that large Korean IPOs will continue to include an international tranche because it can bring in additional demand for the offering. It depends on the market conditions how many of these IPOs will appear from Korea each year. If the Korean equity market conditions improve, we may be able to see an increase in the number of sizeable IPOs from Korea, including those of chaebol-affiliates, privatisation of state-owned enterprises and start-up technology companies.

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Another recent trend of overseas equity financing involves secondary listings of global depositary receipts on foreign exchanges, such as the Singapore Exchange, by companies already listed on the Korea Exchange. In 2011 and 2013, OCI and Youngone issued global depositary receipts (GDRs) in this manner, which enabled them to issue shares at better prices than in domestic offerings. In 2014, Hanwha Chemical and Industrial Bank of Korea also issued GDRs that were listed on the Singapore Exchange and the Luxembourg Exchange, respectively. While these GDRs are initially listed in foreign exchanges, most of them are soon converted back to the original shares and traded on the Korea Exchange. Similar to IPOs offered to foreign investors, offering of GDRs can broaden the issuer's international investor base and help increase long-term demand for the stock. This trend may continue among issuers that have stable financial results and business portfolios attractive to foreign investors.

Dong Chul Kim is a partner in the corporate practice of Paul Hastings and is based in the Seoul office. He specialises in debt and equity capital market transactions and mergers and acquisitions, and has represented a number of international investment banks and Korean corporate clients. Recently, Kim represented the underwriters in the $1.1 billion IPO and listing of Samsung SDS on the Korea Exchange, represented the underwriters in the $340 million GDR offering by Hanwha Chemical and represented the underwriters in the $298 million GDR offering by the Industrial Bank of Korea. He graduated from Columbia Law School and Seoul National University.

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If you have any questions concerning these developing issues, please do not hesitate to contact the following Paul Hastings Seoul lawyer:

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