THE OFFSHORE INVESTOR: DIVERSIFYING YOUR SHAREHOLDER BASE

By Victoria Geddes*

The emergence of the OTCQX International over the last 3 years as an active and reputable trading platform for ADRs, makes a listing worth considering as a cost effective option for Australian companies seeking to increase their profile with US investors.

Building a share register which offers diversification of ownership by type of investor is central to creating liquidity and active demand for a company's securities. Overseas investors have long been recognised as being a vital part of that mix, but for many small to mid cap Australian companies the challenge has been to find a way to effectively engage with these investors.

The OTCQX International market is tailor made for such companies as it is reserved for established foreign companies with shares that are already listed on "qualifying stock exchanges" outside the US and have a Level 1 sponsored ADR programme.

Benefits of Listing

A listing on the OTCQX International is marketed as providing the following benefits:

1. Companies can leverage their home country disclosure into the US market without the costly "harmonisation" that SEC registered companies must undertake.
2. Price transparency with market maker quotes and sizes available in real time.
3. OTCQX companies can get "blue sky" compliance which enables brokers to discuss and recommend companies to their clients.
4. Increased home market liquidity.

More significantly listing costs are around one tenth of those associated with listing on a traditional exchange. There is a US$5,000 application fee and an annual listing fee of US$15,000.

From an investor relations perspective, the OTCQX listing is a starting point that allows non-US companies a platform from which they can build their profile amongst US investors. This is facilitated by the company's Principal American Liaison (PAL), an investment bank which is appointed to act as their adviser in the US market.

Of the dozen or so qualified PALs, only three have been actively targeting Australian companies – Bank of New York Mellon, Merriman Curhan Ford and Madison Williams. Sponsors typically offer advisory and marketing services including dedicated research coverage, research distribution, targeted roadshows with US institutions, retail broker luncheons and investor conferences and webinars.

Many US institutional investors prefer to invest in OTCQX ADRs instead of foreign shares as trading in their home market reduces the cost of investing in an internationally diversified portfolio. It not only avoids costly currency conversions and high transaction costs but also removes a constraint for those institutions which are restricted by their mandates to investing in companies with a US listing.

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US based retail investors can buy OTCQX ADRs by trading through online brokerages such as E*Trade, TD Ameritrade, Charles Schwab and Fidelity.

Australian OTCQX listings

Australia is second only to Canada as the country with the greatest number of listings in this market. Since 2007, 14 Australian companies have listed on the OTCQX International.

Market Cap < US$100 million	$m
QRxPharma	86.7
CMA Corp	83.2
Living Cell Technologies	61.7
Phosphagenics	59.2
Bravura Solutions	36.8
EnviroMission	11.1
Intec Ltd	4.3
Pryme Oil and Gas	2.8

Market Cap > US$100 million	$m
Eastern Star Gas	668.4
Linc Energy	650.4
White Energy Company	519.6
Industrea	342.1
Gold One International	209.4
Starpharma	147.1
Pryme Oil and Gas	2.8

This doesn't include OZ Minerals' listing on the **OTCQX International Premier**, a separate market which is principally designed for large market capitalization companies (in excess of US$500 million) and includes such well recognised companies as BG Group, Marks and Spencer, Tate & Lyle and Benetton Group.

Does the Reality match the Promise?

In September 2009 ASX published a study under its Market Insights series, titled **"The impact of ADR listing on liquidity"** which specifically examined the changes in liquidity in the home market after trading in a company's ADR commenced. The study examined 122 active Australian issued ADRs between 1983 and 2008 and found that *"listing an ADR improves liquidity and hence the visibility of the firm"* and that evidence of a reduction in the Proportional Bid-Ask Spread also indicated a *"reduction in transaction costs, reflecting improved efficiency of the market as a whole".*

Given the broad diversity of Australian companies, both by size and industry, that have elected to join the OTCQX International, the obvious questions that need to be asked are what were they hoping to achieve by doing so and have their expectations been met thus far?

So we asked the three companies that have been listed the longest – Linc Energy, Starpharma and Phosphagenics – for their feedback.

The primary reason given for listing was to increase their profile and visibility in the US market and diversify the shareholder base. All three were taking a longer term view on this and, depending on the sector of the market they were in, had experienced mixed results to date. Linc Energy was the most positive about their listing, noting that they had found US investors much more proactive and willing to act compared to domestic institutions. Phosphagenics on the other hand acknowledged that they were not far enough along the path to commercialisation for their listing to have any real effect. **Interestingly increasing liquidity was not mentioned as a reason for listing and none were able to provide evidence of any substantive improvement in home market liquidity.**

While it is not possible to raise capital via the OTCQX, Linc Energy's experience suggests that the increased profile generated by market makers associated with OTCQX promoting the stock, had contributed to the strong support from US investors for several placements in recent years.

Conclusion

An OTCQX listing would appear to have little downside in terms of cost and additional compliance. As with any listing, however, such benefits as improved liquidity and a more resilient share price are dependent on the extent to which a company (and its PAL in the US) actively supports its stock and whether the fundamentals of the stock and/or sector are attractive to the market at the time.

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