

Best practice recommendations
for emerging markets IPOs

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Preamble

The following recommendations and suggestions are designed to help issuers as well as participating banks and advisors to address the special characteristics of an emerging markets company's initial public offering (IPO) and thus to contribute to a successful IPO. They do not constitute mandatory procedures for conducting an emerging markets IPO. The specific features of each issuer should always be taken into account. Therefore, the following recommendations should not be treated as a comprehensive list of the issues to be considered in emerging markets IPOs. For the purpose of these recommendations, emerging markets IPOs are IPOs of companies whose management, ownership structure and operations are predominantly located in an emerging markets country.

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Recommendations for intermediaries supporting an IPO and their working procedures

1. General requirements

The advisory team involved in an IPO should hold capital market expertise in the German market as well as expertise in transactions involving the country where the issuer operates. This can either be provided by advisors with an international focus, who combine teams in Germany with teams on site, or by the involvement of competent local advisors.

Issuers should continue to be supported by professional advisors after the IPO (especially auditors, legal advisors, IR advisors and Designated Sponsors).

2. Auditors

The auditor should be able to conduct auditing activities within the company or group, or through cooperation partners in both the country where the group holding company is headquartered and in the relevant country. Both a local team with local expertise and the auditor who signs the auditor's report should be involved. This auditor should also inspect the company on site. The collaboration between the local auditor and the auditor who signs the auditor's report should be designed such that both parties hold responsibility for the consolidated financial statements within the scope of their contractual relationship. An example would be the local auditor approving the

final consolidated financial statements (potentially including completion of all forms and notes) via inter-office opinion to the auditor signing the report, thus placing the issuer's auditor in the position of assuming responsibility.

Depending on the issuer's financial history, different set-ups and procedures might be used here.

Far-reaching checks for possible irregularities (fraud) should be an integral part of audit activities. Among other sources, irregularities may arise from different views on corporate governance and general lack of well-developed internal controls. The audit approach must take these factors into account as a whole and be focused on the special features of the relevant country. This includes the following aspects for example:

- Fictitious assets: verification that assets exist through site visits by the auditor who signs the report.
- Fictitious or missing written bank confirmations: confirmations from third parties, especially banks, should be presented to the auditor directly (in person) by well-informed bank staff. Consideration should be given as to whether to obtain confirmation directly from the third party's headquarters (rather than from a local branch).
- Fictitious sales revenue and receivables: the existence of receivables and sales revenues – alongside the usual confirmation of balances – should also be verified through direct conversations with business partners.
- Incomplete information: the local auditor, in particular, should check and guarantee that the issuer's relationships to related parties are completely disclosed. This is often a particular challenge in emerging markets due to the often complex ownership structures and interrelationships between businesses. Legal advisors should be consulted in this context with respect to the necessary content of prospectuses and the results of legal due diligence.



3. Legal advisors/due diligence and prospectus preparation

It is advisable for all IPOs, and especially those in emerging markets, to involve legal advisors with capital market experience, both on the side of the issuer and the bank. Together with the issuer and the other parties involved in the transaction, legal advisors design and make comments on the prospectus, and implement the corporate legal structure for the IPO. Legal opinions and disclosure letters in accordance with German law are submitted by the legal advisors at certain stages of the transaction, as well as their counterparts in accordance with local law by the local legal advisors. Based on the auditing activities carried out (particularly legal due diligence and participation in prospectus meetings), the disclosure letter contains a negative declaration with regard to errors in a prospectus. Close cooperation with local foreign lawyers is essential here. The submission of the legal opinions and disclosure letters has the purpose of giving information and uncovering risks, and also serves to defend the consortium banks.

The primary basis for the prospectus and thus for the legal opinions and disclosure letters submitted by the legal advisors is a legal due diligence. It should be conducted by experienced teams of local and German lawyers. The German team has an important monitoring function in this context. Legal due diligence normally also includes site visits and interviews with the issuer's management staff.

4. Investment banks/consortium leaders

- The consortium leader should have sufficient local expertise to carry out due diligence on site, or should appoint external advisors (e.g. to carry out a separate financial due diligence and commercial due diligence) who have sufficient local expertise.
- In the event that external advisors are involved, the consortium leader should have the expertise required to examine and evaluate the documents prepared by these advisors. The use of external third parties is not a substitute for checks by the consortium leader.
- Furthermore, for identified critical questions the supervising consortium leader should conduct its own supplementary due diligence on site (company, finances and market) or, where appropriate, consult local experts with demonstrable expertise related to the market, company and/or system as well as technical know-how. The use of external third parties is not a substitute for plausibility checks by the consortium leader. In addition to their expertise in the sector and industry, the advisors involved in this due diligence should also have experience in the preparation of due diligence reports in the country where the issuer's operating activities are mainly located. Data collection for due diligence purposes should take place primarily in the country where the issuer's operating activities take place. It is recommended that spot checks be carried out on important data sent by the company and that these be conducted by independent third parties or in-house specialists (e.g. experienced analysts).
- It is further recommended to arrange for the executive board and supervisory body of the issuer to implement binding improvement measures in the company's organisation with a "milestones plan" in order to remedy potential shortcomings in risk management and reporting systems identified by the audit. Local circumstances, legal requirements and the shareholders' right to information are to be taken into account when determining the proportionality of such risk management and reporting systems.

Recommendations for preparing an IPO

5. Investor relations advisors/PR advisors

To simplify coordination, it is advisable to appoint an agency to be responsible for all communications. This agency should ideally cover the entire spectrum of corporate, financial and crisis-related communication. This also includes expertise in designing and launching websites, as well as in financial reporting for the period after the IPO.

The agency should also have experience in coaching managers from emerging markets companies. Helping to prepare the management for presentations as well as press and analyst conferences is an important element of a successful IPO.

An IPO leads the emerging market issuer into a new legal environment and an unfamiliar market. It thus requires particularly extensive preparation. It is particularly important that the issuer is aware before, during and after the IPO of the information and transparency requirements of the advisors, intermediaries and investors involved. The issuer must implement suitable measures for fulfilling these requirements. In this respect we recommend the following:

1. Due diligence/preparation of prospectus

It is mandatory to produce a securities prospectus as a liability document for an IPO. It is essential that this is accurate and complete, not only for liability reasons but also to protect investors. Here it is particularly important that the bank accompanying the IPO carries out due diligence in conformity with market practice. To ensure that this aspect of the IPO is conducted efficiently, we recommend the following:

- As it cannot always be assumed that emerging markets issuers are familiar with German or European law, the management should be given extensive



information about liability and the significance of the securities prospectus.

- The issuer's management should be informed in detail by the bank and the lawyers involved about the procedure and requirements with regard to due diligence.
- The management should be advised explicitly that it is absolutely essential to provide comprehensive information about all aspects of the issuer and to make all necessary documentation available in its entirety.
- The management should be informed explicitly that, in addition to the documents requested for due diligence, access must also be provided to documents and information that were submitted to authorities or registers in the period relevant for the prospectus.
- It must be ensured that the main results of due diligence are provided in the prospectus. A smooth flow of information must be ensured here for all participants. Due to the complexity of emerging markets IPOs, this should be taken particularly into account when setting up the timeframe.
- The issuer should be advised that the individuals involved in due diligence must be closely involved in preparing the prospectus.
- The drafting sessions for the prospectus should take place at the location of the issuer's operating companies and should involve the expertise of the issuer's specialist departments. Heads of management must be intensively involved in preparing the prospectus.
- In the event of language barriers, important sections of the prospectus should be translated into the local language so that they can be verified by the management and approved by the specialist departments.

2. IPO readiness analysis

An IPO readiness analysis should be carried out by the issuer. This should cover the following aspects, among other things:

Effective and efficient processes for financial reporting:

- Capital market-ready IFRS accounting including informative and transparent segment reporting
- Ability to substantiate the equity story with verifiable and reliable data (financial and non-financial KPIs)
- Timely production of financial statements (annual, group and quarterly reports) and investor and analyst communications
- Documentation of planning and budgetary processes (minimum three-year planning)
- Enforcement of compliance with the standards set by Deutsche Prüfstelle für Rechnungslegung (DPR, German Financial Reporting Enforcement Panel FREP) in documentation of relevant matters; establishment of processes to answer FREP enquiries

Adequate risk management and internal control system (with relevant documentation)

- Early risk identification system
- Reporting to supervisory board, e.g. in accordance with section 107 of the Aktiengesetz (AktG, German Stock Corporation Act)
- Systematic identification, analysis and reporting of risks

Corporate governance and compliance/investor relations

- Objective should be the corporate governance and investor relations organisation as described in "Recommendations for the issuer's post-IPO infrastructure".

Taxes

- Checking optimal tax structure
- Checking tax strategy and tax planning
- Internal control system (including excise duties)

3. IPO tutoring

On the basis of the IPO readiness analysis it can be helpful to conduct IPO tutoring tailored to the specific issuer's needs. As part of this IPO tutoring, the weaknesses of the issuer identified in the IPO readiness analysis should be addressed and remedied, or a binding plan should be produced to remedy these weaknesses (see the information on the "milestones plan" on page 6). The issues of corporate governance and compliance should also be addressed in this context, as should the construction of a risk management system which is in line with capital market requirements and focused on the company's specific requirements.

IPO tutoring also involves management training on topics relevant to the IPO and issuer and management follow-up obligations after the IPO.

Establishment of adequate reporting should also be emphasised during the IPO tutoring.

The objective should be to have established an adequate risk management and internal control system, as well as adequate reporting, by the time of the IPO at the latest. At the very least, a binding plan should be agreed for setting up the relevant processes in good time.

4. Pre-IPO communication

- In the run-up to the IPO, the issuer should clearly set out the capital requirement and financing structure and provide a detailed explanation of how the funds will be used. This leads to greater requirements for communication and clarification, particularly during the post-IPO phase.
- Training on capital market requirements and IR/PR measures should be obligatory. The particular target group is the management and investor relations manager.

- The information provided to the investor relations agency is often inadequate for producing the communication tools required for the IPO. Sources of information such as the securities prospectus – as the central basis of information – should be complemented by original information from the issuer based on the prospectus (e.g. product descriptions, marketing documents, pictures, analyses of markets and competition etc.)
- Creating the IR website should also be planned at any early stage. It is the first point of call for investors and represents the company externally. Content should be easy to update using a generally accepted content management system.
- Good capital market communications means that the issuer must be actively involved in creating the content of an investor relations website and writing corporate news. This includes structured feedback on drafts submitted to the issuer for review.
- The better the information provided to the agency, the higher the quality of the communications that accompany the IPO and contribute to active marketing. The essential aim when producing communication tools is to achieve conformity with the contents of the securities prospectus while also attractively marketing the shares being issued.

Pre-IPO communication serves to prepare for the communication which is to be provided by the issuer after the IPO and is therefore of utmost importance.

Recommendations regarding the issuer's boards and committees and for its IPO team

1. Executive board and supervisory board

The issuer should have at least one executive board member who has capital market experience and speaks English (CEO or CFO) and who can represent the company externally on the capital market. This executive board member should be tied to the company for at least one year after the IPO by contract (and by incentives where appropriate).

The executive board member should also have sufficient knowledge of the issuer. In this respect, a length of service in the company's executive board of at least one year prior to the IPO has proven beneficial.

An executive board member should be given explicit responsibility for compliance with the subsequent admission requirements.

The supervisory board should have expertise in capital market law, accounting and the industrial sector. All members of the supervisory board should at least be able to communicate in English. The majority of the supervisory board members should be independent (i.e. they should not be related and should not have business relationships with the company or its principal shareholder).

2. Project coordination

The management should be advised that the CEO and/or other executive board members with extensive knowledge of the company ("IPO key individual(s)") are to be fully available to the bank, auditors, lawyers and other advisors throughout the entire process.

One of the IPO key individuals or a third party with good access to the IPO key individuals should act as project coordinator. This project coordinator should speak English and has to ensure that the advisors are given sufficient support from the company to fulfil the information requirements.

With the beginning of the preparation of the IPO, an investor relations manager ideally based in Germany should be involved in the issuer's project coordination as a fixed member of the issue team. He/she should be able to demonstrate appropriate knowledge of the requirements relevant to the capital market or be trained accordingly. He/she should also be able to negotiate in English – and should ideally also be able to handle enquiries in German. The investor relations manager should act in the period after the IPO as the main contact for:

- investors
- analysts
- advisors
- the media.

He/she acts as an interface between capital market participants, advisors involved and the executive board member responsible for capital market communication (e.g. CFO).

Recommendations for the issuer's post-IPO infrastructure

The day of the IPO is not the end of the process for the issuer's adjustment to capital market requirements. IR activities and compliance with subsequent admission requirements play a decisive role. The emerging market issuer therefore has a particular need for a suitable post-IPO infrastructure, which ideally should have already been created by the time of the IPO. Sufficient financial and available personnel resources are to be made available to this end after the IPO as well. In this respect we recommend the following:

1. Corporate governance

- Supervisory board to be comprised of qualified and largely independent members
- Rules of procedure for executive and supervisory boards (including their committees)
- Use of the recommendations of the German Corporate Governance Committee and checking the basis for submitting the Declaration of Conformity
- Checking other compliance systems and regulatory requirements

2. Investor relations and capital market compliance

To ensure capital market compliance, processes should be established for identifying insiders, maintaining insider lists as well as for ad hoc announcements.

The communications agency chosen for the IPO should continue to be appointed after the IPO for corporate and financial communication by the emerging market company. It is important here that the executive board member responsible for communication has a continuous dialogue with the agency – e.g. through regular phone conferences – and that both parties keep each other up to date. The agency is to be informed in a timely manner on current operational and financial issues. The agency reports on enquiries from analysts, investors and journalists.

The agency must be able to support the issuer in fulfilling all ongoing obligations associated with the IPO. This includes – where necessary – writing and translating ad hoc announcements and notices on voting



rights, press releases, quarterly reports, and producing the annual report. The agency also helps to prepare the AGM and updates the IR section of the website.

Furthermore, the agency organises ongoing communication. To this end, an annual plan is set up which includes all mandatory appointments and all voluntary appointments with the financial community.

To conduct personal appointments with analysts, investors and journalists, the company's executive board member responsible for communication should visit Germany and other European countries regularly and take part in appropriate capital market conferences. The agency should answer enquiries about information that is already publicly available on behalf of the company. There should be a continual flow of information between the issuer and the agency for this purpose.

The investor relations manager, in consultation with the CFO, should be able to answer complex investor relations enquiries from institutional investors on current business developments within a maximum of 24 hours.

3. Post-IPO support by service providers

- The consortium leader should require the issuer to provide it with continual information (at least once per year) on the current rights and obligations of the supervisory and executive boards (in accordance with the Stock Corporation Act), transparency and follow-up obligations imposed by law and the stock exchange, especially obligations on the timely preparation of financial reports and the subsequent requirements concerning reporting, risk management and internal control systems.
- Issuers should continue to be supported by professional advisors after the IPO (especially auditors, legal advisors, IR advisors and Designated Sponsors).
- Issuers should also commission equity research and create a sufficient infrastructure for efficient IR activity.

4. Ensuring efficient cooperation between supervisory body and executive board members

- Minimum requirements should be set for ongoing reporting by the company management to the supervisory body, such as the presentation of key company results, conclusion of important contracts, financial figures (actual vs target).
- To maintain the continual flow of information, regular "off the board" discussions should take place between the CEO and the chair of the supervisory body, at least every two months.

It is reasonable to involve the chair of the supervisory body at an early stage in order to make meetings of the supervisory body as efficient as possible. This particularly applies to the budget meeting and the meetings on the accounts.

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