Trends in the PIPE Market

Susan Chaplinsky

Darden Graduate School of Business,

University of Virginia
Private Investments in Public Equity

- Negotiated sales of securities - usually equity or securities that convert to publicly traded common stock - by listed firms to private investors
- Typically issued under Reg D to accredited investors
- PIPEs include common stock issued at a discount (private placements) but often include many more complex terms
- Generally issued by distressed firms
  (Hillion and Vermaelen, JFE, 2004; Brophy, et. al, RFS, 2009; Chaplinsky and Haushalter, RFS, 2012)

Outline for discussion:

1. Review basic trends in size and quality of issuers
2. Examine changes in contract structures
3. Explore blurring of lines between private & public market
Unless otherwise indicated, all data on PIPEs are from Sagient Research, placementtracker.com.
The chart illustrates the issue volume of SEOs (Secondary Equity Offerings) versus PIPEs (Private Investment in Equity) from 2000 to 2011. SEO issue volume data is provided by Dealogic.

The graph shows a significant increase in SEO volume in 2007, followed by a decline in later years, contrasting with the relatively steady volume of PIPEs. The percentage of PIPE volume to overall volume, indicated by the red line, shows a trend that aligns with the overall volume trends.
Quality of Issuers – Financial Performance

Cash Burn

Percentage Cash Flow Positive
Increase in Contract Choices

Volume in $ billions


Rights
Debt/Pref Stock
ATM
SEL
CVT - Install
RDs
CMPO
CVT - Resets
CVT - Fixed
CS
Relative Decrease in Structured PIPEs
Reasons for Reduction in Structured PIPEs

- Bad Press: Toxic converts, death spirals
- Regulation
  - **NASD**: March 2002 Structured equity lines and floating rate convertibles and resets viewed as “future priced securities.” Require Shareholder Vote if dilution exceeds 20%
  - **SEC Enforcement**: November 2002 First enforcement action (Rhino Advisors) (Bengstsson, Dai, and Henson, 2012)

- Nov. 2007: Citibank sold $7.5 B floating rate convertible to Abu Dhabi
  11% Dividend, Conversion Price= $37.24 vs Closing Price = $31.70, 17% Premium, Hard Floor at $31.83, 5% Dilution
- Aug. 2012: Knight Capital sold $400M in convertible preferred
  2% Dividend, Fixed Conversion Price=$1.50, Closing Price=$4.05, 63% discount, 72% Dilution
Blurring of the Lines –
Growth in Shelf Registered PIPEs

Columbia Business and Law School                  September 20, 2012
Time to Registration Effective Date

Average Days Closing to Effective 97.4

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<th></th>
<th>CS</th>
<th>CVT - Fixed</th>
<th>CVT - Variable</th>
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<tbody>
<tr>
<td>Time to Registration</td>
<td>90.5</td>
<td>116.8</td>
<td>102.3</td>
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2011 offers (Medians):

- **CMPO**
  - Purchase Discount: -3.9%
  - Dilution: 21.8%
  - Gross Proceeds (MM): $31.9
  - Market Cap (MM): $164.3
  - ΔStock Price Closing: 0.7%

- **RDs**
  - Purchase Discount: -2.8%
  - Dilution: 17.1%
  - Gross Proceeds (MM): $6.4
  - Market Cap (MM): $64.7
  - ΔStock Price Closing: -30.1%

- **CS**
  - Purchase Discount: -11.3%
  - Dilution: 16.5%
  - Gross Proceeds (MM): $5.0
  - Market Cap (MM): $47.1
  - ΔStock Price Closing: -38.5%