# Determinants of Successful IPOs in the US Market

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**Abstract.** This paper will discuss the impact of internal and external factors on the IPO process. Primarily aimed at discussing the impact of Investment banks, Regulator Agencies, Company Executives and Other Financial Intermediaries on the IPO process. As regulators' rules change, companies and financial intermediaries need to respond in a timely manner to ensure successful IPOs. On the other hand, trusted financial intermediation and stable company management will help companies in preparing for IPO more smoothly. Investment banks will guide companies in choosing the right markets and act as a bridge between other financial intermediaries to ensure a smoothly running IPO. Other financial intermediaries such as law firms and accounting firms help companies improve their legal and financial information to meet the requirements of regulators. After the IPO, companies also need investment banks to help them issue securities, and law firms and accounting firms to guide companies to complete corporate governance standards such as statements.

**Keywords:** IPO; investment bank; regulatory agencies; company executives; other financial Intermediaries.

## 1. Introduction

Since the 20th century, the financial system of the United States has begun to develop gradually, and today it has grown into the world's oldest, most complex and most developed financial system. By the end of 2021, more than $23 trillion worth of assets were in the American financial system [1]. From investment to insurance, almost everyone takes advantage of the financial services industry in some way, and according to statistics, the insurance and financial services industry accounts for $1.5 trillion or 7.4% of the total GDP of the United States by 2021, and about 6.6 million Americans are employed in the financial and insurance industry [2]. In 1990, Carter and Manaster mentioned that for any company, the first time for a private company to obtain money through the public stock market is IPO (Initial public offering) [3]. In 2002, Ritter and Welch discovered by analyzing data from a financial point of view, companies choose an IPO because they seek to generate capital for the business and establish an open market so that founders and other shareholders can eventually convert part of their value into cash, and from a non-financial perspective, the comapny may be doing it to increase publicity [4]. The first public offering by a North American bank in the United States occurred about 1783. In 2021, a total of 1,073 companies completed IPOs in the United States, raising a total of $317 billion [5]. As of July 2022, Alibaba Group Houlding, which was the largest IPO ever and appeared on NYSE as a listing in 2014, raising nearly $22 billion, and Visa went public in 2008 with $4 billion and ranked second [6, 7]. The success of an IPO is definitely not achieved by one party's efforts, and likewise, an IPO can fail due to many factors. In 2007, Demers and Joos mentioned a factors that may cause an IPO to fail include, but are not limited to time variables, accounting-related variables, market variables, information intermediaries, issue stock price and company age [8]. This article will discuss the impact that investment banks, regulators, corporate executives, and other financial intermediaries have on the corporate IPO process.

## 2. Investment Bank

When a privately held business decides to conduct an IPO, it needs the help of some financial institutions to complete it. Investment banks will be the best helpers for a business when it comes to IPO. Investment banks are financial firms that primarily handle mergers and acquisitions, corporate restructuring, bond issuing, underwriting, trading, and investment banks are also the primary financial intermediaries in the capital market. Before 1933, there was no explicit provision in the United States that required only investment banks among financial institutions to sell securities. Mentioned in the Morgan consortium books before 1933, the United States did not clearly demarcate the boundaries between commercial banks and investment banks until 1933, when Democratic Senator Carter Glass and Rep. Henry F. Kennedy Jr. B. Steagall's Glass-Steagall Act would completely separate commercial banks from investment banks [9]. The role of investment banks is to help companies successfully complete IPOs and issue shares, and investment banks also provide underwriting. Investment banks' pre-issuance and underwriting responsibilities in corporate IPOs include IPO counseling, due diligence and roadshows. In the process of listing counseling, the investment bank needs to be responsible for the progress management of the entire project, formulate the timetable, coordinate with the intermediaries, be responsible for solving various unexpected problems, and help the enterprise establish a good system in all aspects so that it can be better listed. In the IPO, the investment bank also assumes the responsibility of the sponsor, according to the regulations, the sponsor needs to perform a series of due diligence duties, so it needs to conduct financial due diligence with the auditor, assist in making the company's profit forecast, model the company's financial situation, and understand the internal control situation; At the same time, they also have to due diligence on the company's operations and laws together with lawyers, such as visiting the company's main place of business and conducting interviews with management. As a very significant promotional event before a company issues shares, it is arranged by underwriters in order to introduce more investors to the issuer's situation and thus understand their investment intentions. Investment banks are required to continuously visit potential investors in various places during the roadshow and assist issuers in lobbying to enhance their investment confidence.

Before a company goes public, investment bank need to prepare a prospectus. The Securities and Exchange Commission must receive a prospectus, which is a binding legal document that provides comprehensive information on investments marketed to the general public (SEC). The prospectus is open to all investors to assist investors in making more knowledgeable investing choices, as it includes a plethora of pertinent details on the investment or security. Prospectus contains a succinct explanation of the history and firm’s financial data, also include business name that issued the shares and the total shares outstanding issued, and the underwriting banks' names and financial companies. On the other hand, investors can be informed of the risks associated with investing through the prospectus and can further determine whether the business is promising in through the company's financial situation. For example, the raw data in Table 1 comes from Apple's annual report.

**Table 1.** Valuing Apple's current stock price based on the DCF valuation method

| Years | 2021 | 2022 | 2023 | 2024 | 2025 | 2026 |
|---|---|---|---|---|---|---|
| Dividend | 0.22 | 0.4995 | 1.1340 | 2.5747 | 5.8456 | 13.2719 |
| Growth rate | | 127.04% | 127.04% | 127.04% | 127.04% | 127.04% |
| Dividend payout ratio | 15.20% | ROE | 149.81% | Plowback ratio | 84.80% | |
| Growth rate | 127.04% | rf | 1.49% | re | 31.97% | |
| rm | 26.89% | β | 1.2 | | | |
| Terminal growth rate | 5% | Dividend for 2027 | 13.9355 | Price for 2026 | 51.6705 | |
| Intrinsic value | $20.30 | | | | | |

Since Apple is a leading company in the US IT industry, future sustainable expansion of the business should remain at a level extremely comparable to that of the whole sector. Therefore, the US IT industry's terminal growth rate was selected as the terminal growth rate. By analyzing the financial data in Apple's annual report, after calculation, you can get Apple's financial data, such as ROE, Plowback ratio, growth rate, etc. The calculation shows that Apple's intrinsic value is $20.3 per share. Assuming that when Apple's stock is worth $22 per share, investors will not consider buying

Apple stock and choose to sell it. Investors can also value stocks by analyzing the financial data in the company's prospectus. There are many valuation methods, such as the price-to-earnings ratio valuation method, PEG valuation method, DCF valuation method, etc.

After the company is listed, the issuance and underwriting of shares will be an extremely important part. Only when a company's stock is successfully sold and appreciated can it represent that the company's listing financing is successful. An investment bank, as an underwriter, is the only financial institution entitled to sell securities. The underwriting process is in wherein an investment bank first purchases or underwrites the issuing entity's securities before putting them up for sale. In return for their services, the underwriters will get a premium, ensuring that the issuer of the securities can raise the necessary funding.

## 3. Regulatory Agencies

If a company wants to IPO, it must be checked by a regulator, and the company can only complete the IPO if the regulator believes that the company is eligible. In United States, there are two biggest stock exchanges which is NYSE and NASDAQ, have different listing conditions and regulatory requirements. The NASDAQ is divided into three different tiers, each with its listing requirements. Any business that wishes to be listed on the NASDAQ must fulfill the criteria and carefully abide by the corporate governance guidelines. The firm has the option to go through an initial listing eligibility check before submitting a full application. To evaluate if the firm satisfies the digital listing requirements and whether there are any regulatory concerns, listing eligibility personnel will analyze public documentation. A formal application is not the same as the first listing eligibility evaluation. In Table 2 (source: Colonial Stock Transfer Website), companies must satisfy each of at least four separate financial requirements, with no exceptions to meet the NASDAQ Global Select Market initial listing criteria.

**Table 2.** NASDAQ global select market financial standards

| Financial Requirements | Standard1: Earnings | Standard 2: Capitalization with Cash Flow | Standard 3: Capitalization with Revenue | Standard 4: Assets with Equity |
|---|---|---|---|---|
| Listing Rules | 5315(e) and 5315(f)(3)(A) | 5315(e) and 5315(f)(3)(B) | 5315(e) and 5315(f)(3)(C) | 5315(e) and 5315(f)(3)(D) |
| Pre-Tax Earnings | Aggregate in prior three fiscal years above or equal to $11 million, and each of the prior three fiscal years above or equal to $0, and each of the two most recent fiscal years above or equal to $2.2 million | - | - | - |
| Cash Flows | - | Aggregate in prior three fiscal years above or equal to $27 million, and each of the prior three | - | - |

| | | | | |
|---|---|---|---|---|
| | | fiscal years above or equal to $0 | | |
| Market Cap | - | Average above or equal to $550 million over prior 12 months | Average above or equal to $850 million over prior 12 months | $160 million |
| Revenue | - | Previous fiscal year above or equal to $110 million | Previous fiscal year above or equal to $90 million | - |
| Total Assets | - | - | - | $80 million |
| Stockholders' Equity | - | - | - | $55 million |
| Bid Price | $4 | $4 | $4 | $4 |

In Table 3 (source: Colonial Stock Transfer Website), companies that want to meet the NASDAQ Global Select Market initial listing criteria need to satisfy the following liquidity criteria.

**Table 3.** Liquidity requirements

| Liquidity Requirements | Round lot shareholders or Total shareholders or Total shareholders and average monthly trading volume over past twelve months | Publicly Held Shares | Market value of publicly held shares or Market value of publicly held shares and stockholders' equity |
|---|---|---|---|
| IPOs | 450 or 2,200 | 1,250,000 | $45 million |

In Table 4 (source: Colonial Stock Transfer Website), companies must fulfill all the requirements for at least one of the four original NASDAQ Global Market listing criteria listed below.

**Table 4.** NASDAQ Global Market standards

| Requirement | Income Standard | Equity Standard | Market Value Standard | Total Assets/ Total Revenue Standard |
|---|---|---|---|---|
| Listing Rules | 5405(a) and 5405(b)(1) | 5405(a) and 5405(b)(2) | 5405(a) and 5405(b)(3) | 5405(a) and 5405(b)(4) |
| Income from continuing operations before income taxes (in latest fiscal year or in two of last three fiscal years) | $1 million | - | - | - |
| Stockholders' Equity | $15 million | $30 million | - | - |
| Market Value of Listed Securities | - | - | $75 million | - |
| Total Assets and Total Revenue (in latest fiscal year or in two of last three fiscal years) | - | - | - | $75 million and $75 million |
| Publicly Held Shares | $1.1 million | $1.1 million | $1.1 million | $1.1 million |
| Market Value of Publicly | $8 million | $18 million | $20 million | $20 million |

| | | | | |
|---|---|---|---|---|
| Held Shares | | | | |
| Bid Price | $4 | $4 | $4 | $4 |
| Shareholders (round lot holders) | 400 | 400 | 400 | 400 |
| Market Makers | 3 | 3 | 4 | 4 |
| Operating History | - | 2 years | - | - |

In Table 5 (source: Colonial Stock Transfer Website), companies must meet each criteria for at least one of the three criteria below to meet the NASDAQ Capital Market initial listing criteria.

**Table 5**. NASDAQ Capital Market standards

| Requirements | Equity Standard | Market Value of Listed Securities Standard | Net Income Standard |
|---|---|---|---|
| Listing Rules | 5505(a) and 5505(b)(1) | 5505(a) and 5505(b)(2) | 5505(a) and 5505(b)(3) |
| Stockholders' Equity | $5 million | $4 million | $4 million |
| Market Value of Publicly Held Shares | $15 million | $15 million | $5 million |
| Operating History | 2 years | - | - |
| Market Value of Listed Securities | - | $50 million | - |
| Net Income from Continuing Operations (in the latest fiscal year or in two of the last three fiscal years) | - | - | $750 thousand |
| Publicly Held Shares | $1 million | $1 million | $1 million |
| Shareholders (round lot holders) | 300 | 300 | 300 |
| Market Makers | 3 | 3 | 3 |
| Bid Price OR Closing Price | $4<br>$3 | $4<br>$2 | $4<br>$3 |

In Table 6 (source: Colonial Stock Transfer Website), companies must meet one of the following financial criteria to meet the New York Stock Exchange initial listing criteria.

**Table 6**. New York Stock Exchange financial standards

| Financial Standards | I: Earnings Test Rule 102.01C(I) | II: Global Market Capitalization Test Rule 102.01C(II) | Real Estate Investment Trusts Rule 102.05 | Closed-end Management Investment Companies Rule 102.04A | Business Development Companies Rule 102.04B |
|---|---|---|---|---|---|
| Adjusted Pre-tax Income | Aggregate for last three fiscal years >=$10million; Each of the two most recent fiscal years>=$2million; Each of the prior three fiscal years >$0 | - | - | - | - |
| Global Market Cap | - | $200 million | - | - | $75 million |
| Stockholders' | - | - | $60 million | - | - |

| | | | | | |
|---|---|---|---|---|---|
| Equity Market Value of Publicly Held Shares | See chart below | See chart below | See chart below | $60 million | $60 million |
| Distribution Standards Rule 102.01A-B | Shareholders | Publicly held shares | Market Value of Publicly Held Shares | Minimum Share Price | |
| IPOs | 400 round lot | 1.1 million | $40 million | $4 | |

Thus, according to the criteria of the different markets in the table above. Investment banks will coach companies to help them find the most suitable market. At the same time, enterprises will also make some suggestions to enterprises according to market standards to help enterprises meet standards. Therefore, it takes 1-3 years for a business to prepare for an IPO, mostly because the financial situation of the company does not meet the market standards.

## 4. Company Executives

In the process of the company's IPO, executive leadership and the company's board of directors must work together to support the efforts of financial institutions. The involvement of senior management is often required when making strategic decisions or setting the tasks of a company's business units. In the overall process of the IPO, senior management needs to deploy the company's strategic objectives and ensure that the company's development always meets the requirements of listing on the stock exchange. Besides, financial institutions often require the cooperation of senior management when conducting due diligence or when enterprises need to provide legal and financial documents. The senior management team's makeup, quality, and reputation are crucial factors in the enterprise IPO process. Better and more prominent executives will be a reliable signal to communicate the value of an IPO to investors. Academics Cohen and Dean found in a 2005 study that the level of corporate management, such as the management experience, experience and age of executives, will directly affect the price reduction level of IPOs [10]. It is worth mentioning that the educational experience of the executive team and the level of education and culture will indirectly enhance the attractiveness of the enterprise. For some companies, there are some problems in the deployment of the company's strategic goals, and IPO listing has become the core goal of the company, moreover, the company's long-term development goal is quite hazy. In this case, if there is a problem with the company's IPO progress, or if the IPO is forcibly suspended, it will have a negative impact on the executive team. The top management team leaving the firm and stealing employees from the rival company once the listing is abandoned would worsen the team's disintegration. As a result, one of the key factors in determining whether a firm can successfully execute an IPO is the team's stability. To do this, businesses should develop a logical understanding that going public is not the end of the road for the firm, but rather a significant step in that direction. Second, companies should build a long-term vision that is recognized by their employees, and only when the executive team sees the future of the company, will they be willing to work hard for it for a long time. On the other hand, compensation management is also a core element that enterprises need to pay attention to, stable and good salary structure, long-term incentives and short-term incentives, can ensure the stability of executives.

A number of SEC and stock exchange regulations must be followed by the board of directors of a public business to ensure their independence and competency. The boards of directors of most private companies do not meet these criteria, so boards need to plan ahead to meet the conditions for a company's IPO. First, some private firms have a board structure that is rather loose, and other corporations have a board of directors that does not include mostly of independent directors. or unbiased committees. As a result, most businesses that want to curry out an IPO have to enlist a few or more additional newly appointed directors who satisfy the criteria for independence and expertise. Second, exchanges and SEC rules require public companies to establish the audit committee must include three independent directors at a minimum who satisfy the higher independence standards for individuals on the audit committee set out by the SEC. Each Audit Panelist must be capable of comprehending and reading basic financial statements and possess a working understanding of finance. A participant on the audit committee must be knowledgeable in fiscal management or accounting to serve on the NYSE, and NASDAQ requires a member of the Audit Committee to require financial experience, i.e., accounting or finance-related job experience that is relevant, professional qualification in accounting, or another background or experience that is comparable Therefore, the board of directors needs to prepare in advance and comply with all SEC and stock exchange rules. In this process, financial intermediaries also coach the board.

## 5. Other Financial Intermediaries

### 5.1 Law Firms

In the IPO process, the role of law firms is quite important, without a lawyer's legal opinion company cannot complete the listing, lawyers' work also runs through the IPO listing, in the process of restructuring, counseling, issuance and listing, the fundamental responsibility of attorneys is to help businesses list in the safest possible manner. A good law firm can help companies structure securities and disclose the necessary information to investors. Lawyers need to prepare for all matters related to the law for IPO listing, including the formulation of the listing plan for the previous legal matters, due diligence, restructuring, restructuring, declaration, issuance of legal opinions and amendment opinions. Law firms can also assist in drafting prospectuses and other documents required by the SEC. It is worth noting that the core of the equity, assets, business restructuring and other sectors of the enterprise is the legal treatment of finance and assets, in which lawyers may appear in various capacities such as asset managers, legal counsel, and creditors' clients. Therefore, the duties of a lawyer include managing the assets of the enterprise, providing legal counsel services, investigating and grasping the assets and financial status of the enterprise, and sometimes filing or appearing in court at the request of the client on related creditor and debt disputes. Lawyers may also act as lawyers for employees of enterprises or relevant tax attorneys to handle labor disputes and tax disputes. Ultimately, the law firm advises its clients on the legal liabilities they incur, especially those arising from becoming a listed organization. Therefore, hiring the right team of legal counsel will help protect companies from many major mistakes during the IPO, such as failing to comply with SEC regulations.

### 5.2 Accounting Firms

Accounting firms also play a very important role in the IPO process. Companies that want to IPO need an accounting firm to issue an audit report on the consolidated financial statements for 3 years and a financial review report for the most recent quarter before listing. Before the IPO, an accounting firm can come in to conduct a preliminary financial and taxation health inspection for the enterprise, and if any irregularities are found, the enterprise shall rectify them in conformity with what the accounting standards demand. In addition, some accountants will assist the financial department of the enterprise to unify and straighten out the accounts according to the requirements of the enterprise. At the same time, the accounting firm will also help the enterprise to establish a reasonable tax structure. If the company has private placement arrangements before listing, accountants can also participate in the work. After a company has successfully completed its listing, regardless of which stock exchange the company is listed on, the company needs an accounting firm to help the company issue future audit reports. Periodic, semi-annual or annual reports require the signature of auditors to be effective. Therefore, the end of the IPO does not mean that the cooperation between the company and the accounting firm has ended, on the contrary, the cooperation between the enterprise and the accounting firm has just begun.

## 6. Conclusion

For any business that wants to IPO, it is not only necessary to have sufficient time to prepare for legal and financial situations, but also to have stable management and trustworthy financial intermediaries. Looking back at history, countless examples show that not only internal problems can lead to IPO failure, but also external problems are very deadly. The success of the IPO must not be accidental, it took several years of hard work to complete. Over time, the negative impact of the epidemic era is gradually weakening, the economy is beginning to gradually recover, and the increase in stock market activity will allow more companies to participate in IPOs in the future. With the significant increase in the number of investments in the market, this is a great opportunity for loss-making businesses, as the arrival of a bull market can motivate investors to inject new money into the company, which will be a good time to turn a profit. This will be a good opportunity for businesses that remain profitable to accelerate company growth, expand operations, increase company prestige, motivate employees and attract high-quality employees through stocks. All kinds of reasons are indicating that in the future, IPOs will be more popular. However, there are also huge challenges behind the benefits, with the increase in the number of companies applying for IPOs will lead to greater supervision of companies by regulators. NASDAQ and NYSE have the authority to tighten the listing regulations. and strengthen the management of a post-IPO code of conduct. The SEC is likely to become more rigorous in its securities oversight and management work. In this case, both businesses that want to IPO and financial intermediaries who coach businesses need to be started as early as possible, especially if it is legal and financially relevant. Having a well-regulated corporate organizational structure and a sound financial accounting system, and fully evaluating the requirements for issuance and listing, will increase the chances of a successful IPO.

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