The ASX – Unreconstructed?

The old adage about "if it ain't broke, don't fix it" comes to mind with regard to the seemingly senseless stream of new "regulations" that the ASX is trying to foist on the marketplace. They look more designed to strangle at birth the nascent recovery in mining markets with the sole intention of making life easier for the regulatory *nomenklatura*.

In all the brouhaha about the many shortcomings of the TMX Group, Australia is occasionally held up as a paragon of virtue. We have not been of that persuasion as we find the grinding cost of the many "publication and circularization" rules in Australia to be a crippling burden on juniors (particularly the down and out ones). Added to that is the propensity of Australian companies to overly compensate directors even when the cupboard is bare.

However, the ASX has mightily benefitted, as we have written in the past, from the epic proportions of the Super (Superannuation) Fund pools of cash which now measure in the trillions of dollars and for which Canada has no equivalent. This has instantly given most ASX-traded stocks an immediate leg up and certainly held stocks at higher valuations both in good and bad markets than would be the case for a lookalike junior miner on the TSXV or AIM.

It was clearly all too much of a good thing and the ASX in its smugness has decided to kill the goose that laid the golden egg with a tablet of new commandments with which it has descended from whatever mountain regulators climb to get their instructions directly from divine sources.

So while the Toronto Venture Exchange might, at worst, be accused of benign neglect of its junior miners, the ASX has seemingly engaged in a pro-active game of Whack-a-mole to ensure that the junior mining sector in Australia does NOT come out of the other end of the mining crisis in a fit state to recuperate.

The Chicken & Egg of Project Studies

In the beginning there was the financing.. no, hang on… in the beginning there was the project.. no, no.. how did you get to a project without money? Such is the state of turmoil within the brain of the ASX regulators these days. The latest innovation is that it will seemingly NOT be allowed to publish project economics for which the financing is not in place. This seems truly bizarre. It actually implies that miners will have to raise money on a wing and prayer (hundreds of millions?) while declining to tell investors about the project and its economics. This seems to be diametrically opposite to the principle of informed markets. All well and good for established miners but for up and coming players, this is the kiss of death to their financing efforts if they must keep their consultants' reports to themselves.

Listings Rules Changes

In mid-May the ASX compounded the error of its ways in the aforesaid measure with a slate of "improvements" designed to "strengthen the ASX listing rules framework and maintain an appropriate balance between the interests of issuers and investors in promoting efficient capital raising, maintaining market integrity and providing a market that is internationally competitive". However these changes appear retrograde as they will impact small-cap IPO candidates and start-ups as well as those looking to do backdoor listings, making life much tougher (if not impossible) for them.

The main measures proposed are:

- Increase the financial thresholds for listing
- Require audited accounts from entities applying under the "assets test"
- Introduce a minimum free float requirements

- Change the spread of shareholders rules
- Apply the same working capital requirements to all entities applying under the "assets test"

The whole thing is a bit of a rush job as the proposals were put forth in mid-May and submissions from interested parties are due to the ASX by 24 June 2016. It is expected that final changes to the Listing Rules will be released in early August 2016, and will come into effect on 1 September 2016.

The first obvious effect is that it is going to choke off the repurposing of down and out listed shells as backdoor listings of newer bigger prospects. Since time immemorial the mining sector has been driven by the shells of failed ventures having new life breathed into them and saving promoters the struggle of jumping through all the hoops that a *de novo* listing involves. These new rules are demanding minimum free float requirements and then at the same time discounting the fact that a shell may have a vast number of existing shareholders by talking down the relevance of these smaller holders.

Increasing the spread parcel size will disenfranchise small shareholders and impact most heavily on back-door listings, since the listed shell typically has a low valuation, meaning a low parcel value for most of its shareholders. A larger parcel size will mean there are fewer qualifying shareholders to contribute towards spread.

Then the proposal to introduce a new requirement for entities seeking admission under the assets test to produce audited accounts for the last three full financial years will most likely present practical difficulties in relation to back-door listings.

This is then further compounded by a requirement that the candidates for listings pass an 'assets test' threshold with Net Tangible Assets (NTA) of at least AUD$5mn which is likely to have an impact on the ability of junior mining companies to proceed with a listing, as most junior mining companies seek to be admitted to the official list of ASX on the basis of the NTA test given that they are unlikely to have generated any substantial profits in their formative years.

The ASX is proposing to hike the ‘assets test’ thresholds to an NTA of at least $5 million or a market capitalisation of at least $20 million. This is a big jump from the current threshold NTA of at least AUD$3mn (after deducting the costs of fundraising), or a market capitalisation of at least AUD$10mn. This makes new listings candidates bulk up pre-listing (i.e. dilute) and/or spend much more time in the private sphere before listing, which comes with the attendant danger that financing windows (as we have seen in recent years) bang open and shut like shutters in a hurricane.

So in essence the ASX is making it harder to do a backdoor listing while also partly barring the front door at the same time. An Australian broker that we met the other day said he was spending more time looking at TSX stocks as they were way cheaper and the regulatory regime was better. Howzat!

Conclusion

As if the mining sector does not have to deal with than to now face an egregious wave of over-regulation that will constitute a stiff headwind on the voyage to recovery. Ironically the measures being introduced are not being done to protect consumers/investors but rather to “tidy up the market” which should be read as save the Australian exchange’s staff the effort of having to deal with trifling and piffling issues of trivial juniors. These people have better things to do.

In effect this is the Europeanisation of the Australian equity market. A form of creeping ossification where musty, too big to fail, blue chips lumber onwards while the up and coming juniors are regarded as vermin that scurry around the ankles of the Great & Good.

The ASX is tempting fate here. As we have seen in other markets (most notably Canada and the US) when it's the marketplaces' owners themselves that become overweaningly confident and distant from their investors and listed companies then that is when challenger exchanges arise from the dust and give the entrenched bureaucrats of the legacy exchanges a run for their money. With the latest moves the ASX has strapped on the suicide vest and wondered out into the Never Never to self-implode. It really is on a Walkabout away from reality of modern capital markets.

Australia's loss may yet be Canada's (or London's) gain.