Valuation and institutional support make OzForex float an IPO watershed

Written by Michael Bailey for BRW, 8 October 2013

OzForex founder Matt Gilmour will be trimming his existing shareholding of 17.5 per cent to 4 per cent when the company is floated this month. Photo: Louie Douvis

OzForex, the foreign exchange transfer portal that's been getting up banks' noses since 2003, has come a long way since it debuted onBRW's Fast 100 list in 2005.

Back then, the business born in the sunroom of Matt Gilmour's house on Sydney's northern beaches in 1998 – originally as a foreign exchange information site, then as a transactional site once it was no longer required to hold a $10 million capital reserve, thanks to Howard government reforms – was buzzing off a 2004-05 turnover of $3.4 million, up from $300,000 in 2002-03.

That will all seem like spare change on October 18, when OzForex Group shares will debut on the Australian Securities Exchange at $2 a piece, valuing the company at $480 million in the largest confirmed float of 2013.

Gilmour shares the credit for building the business with Gary Lord, who had worked with him in the 1990s at Bankers Trust's foreign exchange division. Both knew first-hand the raw deal that small to medium-size enterprises were getting on their currency transfers compared with the large institutions.

"At BT, each dealer might have 10 or 15 clients," Gilmour says. "They'd get the red carpet treatment – Hong Kong Sevens and all that rubbish that goes on. I was also on the e-commerce committee, so I'd get to assess online dealing systems that were coming through. Brilliant, instant access to the spot price, so long as you had at least $500,000 to trade at a time."

Meanwhile, the average small importer had to fill in a "TT" (telegraphic transfer form) at the local bank branch. "They'd get whatever the hell the bank said the rate was that day."

At the time, the pair knew consumers were becoming more comfortable with looking beyond the major banks for services such as mortgages and savings accounts.

"We have tried to ride on the coat tails of that trend. It is not really a difficult pitch – to encourage customers to pay a lower price and get higher service levels," Gilmour told BRW.

At 21.7 times its 2013-14 forecast profit of $18.6 million, the upcoming float of OzForex is one of the most highly-valued initial public offerings the ASX has ever known, which makes all the more prescient Gilmour'advice to entrepreneurs in BRW in 2005 to step back and consider the real worth of their businesses. "We were approached by a would-be trade buyer last year, but we think there's too much potential in the business to sell it just yet."

No skin required

Apart from its record-breaking valuation, the OzForex float appears to have flouted another IPO convention. It has attracted more than half a dozen institutional funds management supporters, convinced by advisers Goldman Sachs and Macquarie Capital to stump up as much as $50 million each, despite its owners keeping very little "skin in the game" after the float.

OzForex has been majority-owned by external institutions since 2007, when Macquarie Private Wealth bought a 51 per cent stake from the founding investors for a price that's never been disclosed. In November 2010, US private equity firms The Carlyle Group and Accel Partners became share-holders and Macquarie reduced its stake to 19.9 per cent. Yet all three will completely sell out in the float, while Gilmour and Lord will trim their existing shareholdings of 17.5 per cent apiece down to 4 per cent, taking $40 million off the table each.

The participants in the IPO appear to be backing OzForex on its fundamentals rather than on any major incentivisation of its vendors.

Roger Montgomery worked with Gary Lord at Bankers Trust in the 1990s, and the funds manager has the utmost respect for him and for the global business which OzForex is building. But this flight of private capital has him feeling a little sceptical.

The company is talking up its annual growth targets of 30 per cent, underpinned by expansion in the US where it last year struck a deal to white-label an international money service for Travelex. It already white labels foreign-exchange platforms for Macquarie Private Wealth and ING Direct, and plans to “aggressively” take the service global, chief executive Neil Helm told an analyst conference call as the IPO prospectus was lodged.

Conscious of the need to show there were plenty of people within OzForex who remained incentivised to see it do well, Helm – who joined OzForex from Macquarie in 2007where he’d been convinced the bank should invest after meeting Gilmour at a surf camp – told the analysts he and his management team “weren’t going anywhere” and still saw massive potential in the business.

“But if they’re really going to get 30 per cent growth, we start asking why they’re selling it now?” says Montgomery, the founder of Montgomery Investment Management. “If you’re a private equity manager selling into these sorts of floats, you might say to yourself, ‘we’ll sell it a year before it matures, so we can at least lay our head on the pillow of credibility that we gave the investors something, we didn’t take it all’.”

If he was looking to grow a company globally, Montgomery says he would make an initial public offering of a separate listed vehicle to raise capital to plough back into the underlying company’s growth. “But in [Ozforex’s] case, all the money being raised is going to the vendors. Nothing’s been left in the business.”

The $2 per share asking price for OzForex “seems a little expensive to us”, Montgomery says. “That doesn’t mean it won’t go up a long way”.

However the funds manager has form for picking value in floats. When Myer was floated by its private equity owners at $4.10 a share, Montgomery valued the retailer at closer to $2 a share and was proved right.

Roger Montgomery says OzForex’s IPO price of $2 seems to be ‘a little expensive’. Photographer Michel O Sullivan