Postbank: how a promising stock market flotation was bungled

The deal should have been Europe's best listing this year. Instead it may have dented investor sentiment and the reputation of investment banks, writes **Patrick Jenkins**

Barely a fortnight ago, Klaus Zumwinkel was smiling broadly as he sat centre-stage in front of an expectant Frankfurt press corps and declared: "I know all about IPOs. This is my second one."

Mr Zumwinkel, who has served 14 years as chief executive of Deutsche Post and piloted the initial public offering of the post office in 2000, was launching a two-week book-running period for what should have been one of Europe's biggest and best IPOs this year – the flotation of Postbank.

Sure enough the shares debuted yesterday, but in a shrunken offering, at a lower price, propped up by a potentially costly convertible bond, and two days late.

The truth is Mr Zumwinkel did not know all about IPOs and ignored the advice of those who did – namely the investment bankers from Deutsche Bank and Morgan Stanley, who were co-ordinating the deal, as well as a coterie of 17 other banks in the IPO syndicate. He cast aside the consensus valuation of Postbank at €4.5bn to €5bn (£3bn to £3.3bn) and himself set the range at €5.2bn to €6bn, stunning and alienating the market in the process.

It did not help that Deutsche Bank twice shook investor sentiment, first by considering bidding for Postbank at a knock-down price itself, even as it piloted the IPO; then by leaking an internal memorandum that put a controversially low valuation on the bank.

Together, a slipshod investment bank and a bloody-minded chief executive had turned the Postbank flotation into a comic-book tale on how not to run an IPO.

The deal however, raises serious questions about the damage to investor sentiment, to the reputations of the investment banks, particularly that of Deutsche Bank, and to Mr Zumwinkel's image as the man who had turned the German post office into one of the biggest logistics empires in the world.

A few months ago, it had all looked so promising. Postbank was a solid bank, with a focus on low-risk retail clients and none of the bad debt problems that had dragged down bigger rivals in the German market, from Commerzbank to WestLB. Profitability had improved steadily – to €356m last year from a loss of €21m five years ago – and there was the prospect of a new income stream from taking over the back-office processing work of Deutsche Bank and Dresdner Bank. Best of all, Postbank commanded an enviable market share in an otherwise highly fragmented sector.

That profile has ensured the attention of covetous rivals since the late 1990s, when Postbank was first due to be privatised. But takeover approaches have been rejected and privatisation never happened, with ownership transferred instead to Deutsche Post.

Then in April, Gerhard Schröder, the German chancellor, egged on by the rhetoric of his French neighbours about the creation of "national champions", asked Josef Ackermann, chief executive of Deutsche Bank, whether he would like to merge his bank with Postbank and beef it up into a heavierweight champion.

Aides say that Mr Ackermann was non-committal. Some non-executive members of his board urged him to press ahead with a deal while others, particularly the more internationally-focused, were less enthusiastic. In the end, Deutsche Post's ambitious price tag and the challenges of integrating a bank whose distribution is bound to post office counters, were too much to stomach and the bid was aborted.

Klaus Zumwinkel, chief executive of Deutsche Post, issued a statement that took a sideswipe at both Deutsche Bank and investors, insisting he would "not be dictated to"

In theory, a flicker of interest from a trade buyer could have been good for the IPO process, stimulating investor interest. But the reverse seemed to be true. Suggestions that Deutsche Bank had only wanted to pay €4.3bn for the whole of Postbank flew in the face of Mr Zumwinkel's long publicised belief that the bank was worth €5bn-€6bn.

There were also inevitable accusations of conflict of interest between Deutsche Bank's role in leading the IPO process and its emergence as a potential bidder.

Some observers saw this as the point at which the Postbank flotation began to unravel. But the central drama was yet to come.

Last month, FT Deutschland, the Financial Times's German sister paper, published details of Deutsche Bank's "preliminary offering summary", an internal document that had been leaked to investors and showed Postbank's "expected market capitalisation" to be €4.4bn-€5.3bn.

Deutsche Bank insisted this was an early assessment of investor sentiment, not an official valuation. Other banks had received similar feedback. Morgan Stanley's investor research, it later emerged, had come up with a range of €4.5bn-€4.8bn.

But Mr Zumwinkel was furious and instructed his lawyers to look at how they could claim recompense. There was a heated telephone exchange with Mr Ackermann, during which Mr Zumwinkel rejected Deutsche Bank's offer to resign the mandate. With only a week to go before the book-running began, it was too late to change banks. He did, however, issue a statement that took a sideswipe at both Deutsche Bank and investors, insisting that he would "not be dictated to".

Ten days later, Mr Zumwinkel forced through a price range of €31.50 to €36.50 per Postbank share. People close to Mr Zumwinkel say he was determined not to take advice from bankers whom he felt had betrayed him. He also had fond memories of Deutsche Post's own flotation four years ago.

"The trouble is Zumwinkel still believes the [Deutsche] Post float was a success," says one banker not involved in the Postbank IPO syndicate. "But the truth is, he screwed investors with Deutsche Post and he thought he could do it again."

Deutsche Post was floated at €21 a share and has fallen steadily to today's value of below €17.

Kevin Lapwood, logistics analyst at ING, says: "Zumwinkel is a German grandee. He makes it quite clear he doesn't have too much time for investors and I don't think investors have too much time for him."

The stand-off with potential investors in Postbank ended abruptly at the weekend when Mr Zumwinkel acknowledged that two weeks of frantic book-building had flopped. "The market is always right," he said. "The market decides the price it will pay."

Postbank shares were listed yesterday at a knock-down €28.5 and rose slightly €28.85.

Now that a face-saving muddle-through process has been achieved, it would be easy to dismiss the technicalities of Postbank's true value and the titillating power struggle between investment banks and their clients as unimportant. But the aftershocks of the saga will be felt widely.

Back in March, when the second of Germany's planned IPOs this year was cancelled despite a clutch of successful deals in the UK and across continental Europe, bankers dismissed talk of a German malaise. Both of the pulled flotations – X-Fab and Siltronic – were technology deals, and in jittery markets investors were nervous about technology.

Postbank, the pundits said, would be the true test of IPO sentiment, setting the tone for European listings for the rest of the year. A successful flotation, and the markets would stay open; a failure, and there was a danger the IPO window would close. But in the event, experts believe the unusual turn of events in Postbank has probably made it an unreliable barometer.

Christian Strenger, a supervisory board member at DWS, Germany's biggest fund manager, believes the future of IPOs in Germany and Europe remains unharmed: "Even if this IPO hadn't happened, it would not have been the end of the world. Germans take things too much to heart."

Among Germany's battered band of small investors, who ended up buying nearly half Postbank offering, such sensitivity is understandable. They have, after all, been hard hit, not only by the underperformance of the big privatisation shares – Deutsche Post and Deutsche Telekom – but also, and more brutally, by the Neuer Markt high-technology busts.

The lower-than-planned launch price for Postbank mitigates the risk of another hit. But if it does underperform, the delicate exercise of persuading private investors back to the stock markets, could be set back for years.

Deutsche Post, meanwhile, is left in an odd position. It has spent the past nine months preparing for an IPO that may yet fail in its mission to crystallise the value of an under-rated asset. Postbank has sat in Deutsche Post's books at €4.88bn, yet at €28.5 a share the market has valued it at €4.7bn.

Mr Zumwinkel insists the three-year convertible bond, which will raise a further €1bn, increases that valuation to €5.2bn. But sceptics say that unless Postbank's shares rally strongly over the next three years, the bond could prove an expensive exercise in flattering the valuation – and Mr Zumwinkel's ego.

The question for Deutsche Bank and Morgan Stanley as lead banks in the IPO is whether the rough and tumble of the flotation process has hurt their reputations.

Although Deutsche Bank was widely vilified at the time of the leaked memo, Mr Zumwinkel's growing petulance deflected the heat. But the danger, now the stock has floated, is that he follows through his thinly veiled threat of taking legal action against Deutsche Bank. Even without that risk, rivals seem to believe the almost automatic right Deutsche Bank has had in recent years to be named as a lead bank for any German capital markets transaction could have been hurt by both the abortive acquisition attempt and the memo.

One banker at a big US group says: "Given that any decent sized deal normally needs a domestic bank joint-leading with an international bank, this could be very good news for the likes of Commerzbank or Dresdner."

Some bankers wonder that the global co-ordinators did not withdraw from the deal once it became clear they were so at odds with Mr Zumwinkel.

Throwing away a big deal that could net lucrative fees would appear to be madness. But consideration is also likely to have been given to the complex of delicate relationships that criss-crosses the Frankfurt banking scene. Mr Zumwinkel sits on Morgan Stanley's board. Rivals bidding for the Postbank mandate complained that his appointment, which took effect within two months of the IPO banks being appointed, could have coloured the decision-making in the beauty parade – a charge that both groups reject.

For Deutsche Bank, the web is more tangled still. Ironically, it has been the much called-for consolidation in German banking that has added some of that complication, with Deutsche just having transferred much of its back-office processing work to Postbank.

Then came the bid discussions and the memo – both of which increased the pressure on Deutsche to make the IPO a success.

Yet for once, that famed German business network – the so-called Deutschland AG – did not extend into the investment community. Vital to the rebuilding of a strong economy after the second world war, the network, underpinned by a vast array of cross-shareholdings and non-executive board positions, broke down when it came to backing the Postbank flotation.

Insurance groups Allianz and Munich Re, the saviours of many an endangered transaction, stayed away, in line with their new policy of reducing their shareholdings and focusing on shareholder value. International investors that were supposed to offset slack German demand only materialised once the price was cut.

"The trouble is that domestic investors still play a lead function in an IPO," says Stephan Sturm, head of investment banking at CSFB in Germany. "Foreign investors like the Germans to come in first."

In Postbank's case, investors repeatedly and publicly said that the original price range was too high. Mr Zumwinkel dismissed such talk as investor tactics to push down the valuation, despite advice from bankers that the gap between his and their valuations was far bigger than normal and no one was subscribing at the price he wanted.

Ultimately, however, observers believe the dismissive response of German and foreign investors alike to an excessively ambitious initial price range can only have a positive influence on Germany's capital markets.

"In 1999, you could virtually sell rotten apples [on the stock market]," says Mr Strenger at DWS. "Today, the IPO game has become a lot more refined everywhere. In Germany, this is a lesson in how market forces will prevail and how they are guided by the international context."

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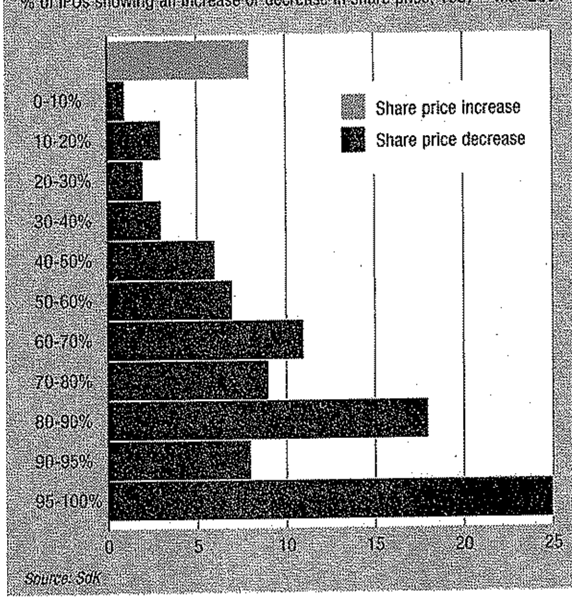
German IPO performance

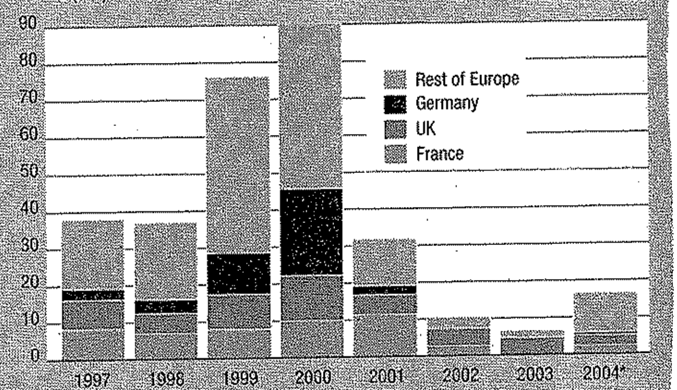
% of IPOs showing an increase or decrease in share price, 1997 – Mar 2004



Source: SdK

European IPOs

Volumes ($bn)



Number of issues

	1997	1998	1999	2000	2001	2002	2003	2004*
France	45	83	60	70	17	7	0	3
UK	109	58	77	216	76	53	61	50
Germany	29	75	159	136	24	6	0	2
Europe**	128	141	197	231	76	46	29	42

Source: Dealogic

* Year to June 22 ** Excluding France UK and Germany