BACK TO BUSINESS

Illustration: Henry Wong

THE VIEW
RICHARD HARRIS

Glowing and growing

Alibaba's golden age may well last for some time, at least while emotion trumps stock fundamentals

The exotic and mysterious tales of *One Thousand and One Arabian Nights* featured one Ali Baba.

To cut a long story short, Ali profited from outwitting a den of Forty Thieves and naturally the good guys lived happily ever with both cash and love interest.

The modern-day Alibaba was placed on the New York Stock Exchange valuing the company at US$250 billion, a fortune that both Ali Baba and the Forty Thieves could not imagine. The question is whether investors are going to live happily ever after.

In a placing like this, the large institutional investors usually get in at the head of the queue. Their price was US$68, a figure already at the high end of the range.

The process of matching the first bids and offers last Friday took three hours, with the opening price slowly creeping up until it was finally struck at a princely US$92.70. The stock traded throughout the afternoon to end at US$93.89. These fortunate investors made a comfortable 38 per cent gain on their shares with the little guys losing out.

But in an oversubscribed placing like Alibaba, even the big investors get scaled back. So the institutions aren't necessarily the big winners, as the millions made on the trade become a rounding error when you are running billions. Some institutions received no shares at all.

> **Behavioural finance will be a better predictor than price-earnings ratios**

The people walking around with smiles on their faces are the management, investors like Softbank of Japan and Yahoo of the United States; and the banking and underwriting teams who walked off with about US$250 million in fees. The rest of us have to figure out the strategy of how to get our hands on the shares in the secondary market.

But do we want them? The shares were reportedly placed at a share price to Alibaba earnings per share ratio of 29 times, which became 40 times after the initial rise.

This is expensive, but then again, the company has grown like a weed – doubling in the past three years. Who knows where it will be in another three years? Investors are always willing to pay up for growth.

Western investors are typically unhappy with owning a share's economic rights – they don't actually own a share of the company itself. That story begins with China's unwillingness to let unreliable foreigners own Chinese shares directly (and touches on the laudable unwillingness of the Hong Kong stock exchange to list a share without all of the ownership rights).

29

Alibaba's shares were reportedly placed at this price-earnings ratio, later rising to 40

Alibaba investors own a piece of paper, based on trust, with a limited ability to enforce their rights.

For once, the big institutions don't seem to care.

Our hope with Alibaba is that we get another bite of the cherry lower down, but it may not be a very big bite and you have to be quick.

We had a bite with Twitter, which placed at US$26, then hit US$73, before falling to US$30 six months later. It has since risen to US$52.

The bankers did a good job on Facebook by placing it at US$38 in May 2012, only to see it collapse to US$19 by the end of August. It is now US$78.

The most likely scenario is that there will be a fairly short consolidation period, as the price is unlikely to go down with everyone looking at it.

Patience may be needed to await a more general market fall, when any stock on 40 times will react negatively.

The highly sophisticated stock market is unlikely to let fundamentals spoil the story so we should turn to behavioural finance to learn a lesson from history.

In the late 19th century, the golden stocks were coal and steel. The "must-buy" stocks at the turn of the century were Big Oil and then movies.

Cars boomed in the 1920s and the '50s, together with television and airlines. The swinging '60s had to hold the globalising Nifty Fifty, with the late 70s spawning Microsoft Corp.

The mobile-phone era captured the '80s and '90s markets. The golden stocks of our age are the online technology stocks – they are darlings of the market.

Alibaba is most certainly a darling.

The share is likely to continue to price on emotion rather than fundamentals. Behavioural finance will be a better predictor than price-earnings ratios.

But be encouraged, nothing lasts forever. By 2026, Alibaba may just be another boring utilities stock.

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