# 2000 IPO Market Ends Wild Ride on Down Note

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The IPO market was a roller coaster ride in 2000. The year saw 339 IPOs by U.S. companies, a 29% decline from the 480 IPOs in 1999. Boosted by the largest IPO by a U.S. issuer in history - AT&T Wireless raised $10.62 billion in April - gross proceeds declined only 10% from $61.63 billion in 1999 to $55.46 billion in 2000, and average deal size increased from $128.4 million to $163.6 million. The overall IPO market also benefited from a record 107 IPOs by foreign companies raising $52.68 billion. In total, 2000 produced 446 IPOs with gross proceeds of $108.15 billion, compared to 537 IPOs raising $95.33 billion in 1999.

## The size and vitality of the IPO market in 2000 fluctuated widely throughout the year, mirroring the volatility in market conditions in general and for technology stocks in particular.

- In the early part of the year, rosy growth projections and easily available capital led many fledgling technology companies to the IPO market. The first quarter saw 142 IPOs, with 21 IPOs tripling from their offer price on their first day and 52 IPOs doubling, as profitability and sound business plans were often cast aside. In the first quarter, the average IPO nearly doubled on its first trading day. The tech-laden Nasdaq reached its all-time high of 5,132 on March 10.
- April saw a sharp downturn in the stock markets, and market turbulence for technology and Internet stocks chilled the IPO market for most of the second quarter. The low point for the Nasdaq in the second quarter came on May 24, when it dropped to 3,043. The quarter included 104 IPOs, with the average IPO increasing only 35% on its first trading day. Even with suppressed valuations, the second quarter saw only five IPOs triple on their first day and 11 IPOs double.
- Helped by a summer rally that pushed the Nasdaq to 4,289 on July 17, the IPO market rebounded nicely in the third quarter. The 142 IPOs in the third quarter matched the first quarter total, and the average IPO increased 39% on its opening day. E-commerce IPOs remained largely unpalatable following the dot-com retrenchment that began earlier in the year, but fiber optic and Internet infrastructure companies were well received.
- With deteriorating capital markets and concerns about slowing economic growth, the IPO

market ended the year on a down note. Only 58 IPOs priced in the fourth quarter - and a paltry nine IPOs in December - compared to 161 IPOs in the fourth quarter of 1999. Gross proceeds in the fourth quarter were $17.45 billion, or 63% less than the gross proceeds of $47.62 billion in the fourth quarter of 1999. The average IPO inched up only 14% on its first trading day in the fourth quarter. The Nasdaq dropped over 30% during the course of the fourth quarter and closed the year at 2,470, more than 50% below its all-time high.

As the market soured on technology companies, the mix of companies completing IPOs shifted throughout the year. Technology IPOs, which hovered around 70% of all IPOs for the first three quarters, fell to 48% of IPOs in the fourth quarter. Proceeds from tech IPOs fell even more sharply, declining from 68% of IPO proceeds in the second quarter to 37% in the third quarter and to 15% in the fourth quarter. Internet-related IPOs followed a similar trend, declining from 61% of IPOs in the first quarter to 34% in the fourth quarter.

The "irrational exuberance" of the latter half of 1999 and early 2000 created an unsustainable number of technology start-ups turned IPO. In order to compete against established rivals with well-known brand names and existing data and product distribution networks, many of these companies had strategies calling for huge capital outlays to create brand awareness or build new networks. The fourth quarter technology rout, following April's pummeling of tech stocks, left these companies with little or no access to new capital, and as a result many of these once high-flying stars are now experiencing massive layoffs, distressed sales or bankruptcies.

**Monthly and Quarterly Totals**

The monthly and quarterly totals show a rather dismal end to the 2000 IPO market:

| **Month** | **Number of IPOs** | **Proceeds (millions)** |
|---|---|---|
| January | 21 | 4,085.6 |
| February | 55 | 8,673.0 |
| | 66 | 19,390.1 |

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| March | | |
| **First Quarter 2000** | **142** | **32,148.8** |
| April | 37 | 17,655.0 |
| May | 25 | 2,477.0 |
| June | 42 | 11,194.1 |
| **Second Quarter 2000** | **104** | **31,326.2** |
| July | 49 | 11,016.2 |
| August | 65 | 10,719.2 |

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| September | 28 | 5,482.3 |
| **Third Quarter 2000** | **142** | **27,217.8** |
| October | 27 | 8,873.3 |
| November | 22 | 5,695.6 |
| December | 9 | 2,884.0 |
| **Fourth Quarter 2000** | **58** | **17,452.9** |
| **2000 Total** | **446** | **108,145.7** |

**Fourth Quarter Lowlights (and Highlights)**

In the first quarter of the year, IPOs gained close to 100% on average on their first day of trading. That figure plummeted to 14% in the fourth quarter. Even Transmeta, the only IPO to "shoot the moon" in the fourth quarter, was trading close to its offer price by the end of December, erasing most of its 115% first day gain.

The fourth quarter saw a number of large foreign telecommunications companies make disappointing U.S. debuts. Investor enthusiasm for foreign telecom deals was dampened by a sector-wide decline in telecom stocks and concerns over the spending spree by telecom companies for third-generation mobile-phone licenses during 2000.

The $856 million IPO by Telekom Austria AG lost 12% on it first day of trading in November and a total of 32% by year end. The following day, Spanish mobile operator Telefónica Móviles, S.A. came to market with a $2.8 billion offering priced at the low end of its expected range and ended its first day of trading 3% below its offer price. Another disappointing fourth-quarter IPO was Norway's Telenor ASA which, despite touting itself as the leading telecom company in one of the world's most advanced telecommunications countries, also slipped below its offer price.

A few companies that debuted in the fourth quarter did, however, prosper. Based on year-end closing prices compared to offering prices, the most successful IPOs of the quarter were: Specialty Laboratories, Inc. (up 107% from its offer price at year-end), Watson Wyatt & Company Holdings (up 88%), Synplicity, Inc. (up 81%) and Coach, Inc. (up 80%). Nine companies ended the quarter up more than 50% from their IPO prices while 26 companies (45% of fourth-quarter IPOs) ended the quarter below their offer price.

***Year End Winners and Losers***

Nearly two-thirds of all IPOs in 2000 ended the year below their initial offering price. The average 2000 IPO was trading 19% below its offering price at the end of the year, with 173 IPOs trading at least 50% below their offering price at year-end and 38 down more than 90%. However, the average 2000 IPO outperformed the Nasdaq, which declined 39% for the year and 52% from its March high. In contrast, the average 1999 IPO gained 181% during 1999 and only 22% of 1999 IPOs were trading below their offer price at December 31, 1999.

Some issues - including several high-tech offerings and a doughnut company - ended the year with very impressive gains. The biggest winners of 2000, based on year end closing prices were:

| Company | IPO Date | IPO Price ($) | 12/31/99 Price ($) | % Change |
|---|---|---|---|---|

| | | | | |
|---|---|---|---|---|
| Embarcadero Technologies, Inc. | 4/19/00 | 10.00 | 45.00 | 350% |
| Krispy Kreme Doughnuts, Inc. | 4/4/00 | 21.00 | 83.00 | 295% |
| First Horizon Pharmaceutical Corporation | 5/31/00 | 8.00 | 30.75 | 284% |
| Sonus Networks, Inc. | 5/25/00 | 7.67 * | 25.25 | 229% |
| Sun Life Financial Services of Canada Inc. | 3/22/00 | 8.50 | 26.63 | 213% |
| Stanford Microdevices, Inc. | 5/24/00 | 12.00 | 36.00 | 200% |
| Praecis Pharmaceuticals Inc. | 4/26/00 | 10.00 | 29.25 | 193% |

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|---|---|---|---|---|
| Community Health Systems, Inc. | 6/8/00 | 13.00 | 35.00 | 169% |
| Uticom, Inc. | 4/4/00 | 13.00 | 34.06 | 162% |
| Cabot Microelectronics Corporation | 4/4/00 | 20.00 | 51.94 | 160% |

* adjusted for 3 for 1 split on October 10, 2000

Although impressive, none of these IPOs comes near matching the top performers of 1999, which saw 16 IPOs increase more than 1,000%. Of course, the run-ups by 1999's IPOs proved short-lived for investors who held the stocks through 2000, as the top-ten IPOs of 1999 declined an average of 79% during 2000. The biggest year-end winners from 2000 all were launched in the first half of the year. The best performing IPO of the second half of 2000, SpeechWorks International, ended the year up 145%.

**California, Massachusetts and Foreign IPOs Lead Rankings**

IPOs by companies based in California, Massachusetts and foreign countries dominated the overall IPO market in 2000. California produced 131 IPOs with proceeds of $12.9 billion in 2000, representing 29% of the total number of IPOs and 12% of the total proceeds. California was followed by Massachusetts with 33 IPOs — the second most from any state and the highest per capita rate of IPOs for any state in the country. Next in the 2000 IPO state rankings were Texas (17 IPOs), New York (14 IPOs) and Florida (13 IPOs).

Of the 446 IPOs in 2000, 144 IPOs (32% of the total) were by companies based in the Eastern U.S. (east of the Mississippi River), 195 IPOs (44%) were by companies based in the Western U.S. and the remaining 107 IPOs (24%) were by foreign companies. Eastern U.S. IPOs raised $23.23 billion (21% of the total), Western U.S. IPOs raised $32.23 billion (30%) and foreign IPOs raised $52.68 billion (49%).

**Leading Underwriters**

The underwriters lead-managing the most IPOs in 2000 were:

| **Lead Underwriter** | **Number of IPOs** | **1999 Rank** |
|---|---|---|
| Credit Suisse First Boston [1] | 60 | 1 st |
| Goldman, Sachs & Co. | 58 | 2 nd |
| Morgan Stanley Dean Witter | 43 | 3 rd |
| Merrill Lynch | 35 | 6 th |
| Robertson Stephens | 30 | 4 th |
| Chase H&Q | 28 | 10 th |

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|---|---|---|
| Lehman Brothers | 28 | 7 th |
| Salomon Smith Barney | 24 | 11 th |
| Deutsche Banc Alex. Brown | 21 | 8 th |
| Donaldson, Lufkin & Jenrette | 19 | 5 th |

[1] Includes one IPO originally filed by Donaldson, Lufkin & Jenrette before its acquisition by Credit Suisse First Boston.

**Top Law Firms**

The law firms participating in the most Eastern U.S. IPOs in 2000 were:

| **Law Firm** | **Counsel to Issuer** | **Counsel to Underwriters** | **Total IPOs** | **1999 Rank** |
|---|---|---|---|---|
| Hale and Dorr | 13 | 8 | 21 | 1 st |
| | 4 | 10 | 14 | 2 nd |

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|---|---|---|---|---|
| Testa, Hurewitz & Thibeault | | | | |
| Ropes & Gray | 3 | 11 | 14 | 9 th |
| Shearman & Sterling | 0 | 10 | 10 | x |
| Morgan, Lewis & Bockius | 8 | 1 | 9 | 7 th |
| Mintz Levin | 5 | 4 | 9 | x |
| Skadden Arps | 4 | 5 | 9 | 4 th |
| Davis, Polk & Wardell | 0 | 9 | 9 | 6 th |
| | 0 | 8 | 8 | 5 th |

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|---|---|---|---|---|
| Cravath, Swaine & Moore | | | | |
| Goodwin, Procter & Hoar | 5 | 2 | 7 | x |
| Piper Marbury Rudnick & Wolfe | 5 | 2 | 7 | x |
| Latham & Watkins | 2 | 5 | 7 | 8 th |

[x] not in top twelve in 1999

**Valuation Shifts**

In our year-end 1999 review of the IPO market, we discussed the economy-wide shift of valuation from brick-and-mortar businesses to their online counterparts. We compared the market valuations at December 31, 1997 and 1999 of selected long-established, traditional companies (most of which have now introduced online components) with newer, Internet-based counterparts. The following table updates this analysis to December 31, 2000, starkly illustrating the misfortunes of Internet-related companies in 2000.

| | **Valuation at 12/31/97** | **Valuation at 12/31/99** | **% Change 12/31/97 to 12/31/99** | **Valuation at 12/31/00** | **% Change 12/31/97 to 12/31/00** | **% Change 12/31/99 to 12/31/00** |
|---|---|---|---|---|---|---|

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|---|---|---|---|---|---|---|
| **Book Sales** | | | | | | |
| Barnes and Noble | 2.27 | 1.43 | (37%) | 1.71 | (25%) | 20% |
| barnesandnoble.com | 2.52 [x] | 2.05 | (19%) | 0.19 | (92%) | (91%) |
| Amazon.com | 1.44 | 25.94 | 1,699% | 5.54 | 285 | (79%) |
| **Auction Services** | | | | | | |
| Sotheby's | 1.05 | 1.76 | 69% | 1.37 | 30% | (22%) |
| eBay | 0.72 [x] | 15.21 | 2,026% | 8.84 | 1,128% | (42%) |
| **Toy Sales** | | | | | | |

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|---|---|---|---|---|---|---|
| Toys "R" Us | 8.77 | 3.43 | (61%) | 3.29 | (62%) | (4%) |
| eToys | 2.04 x | 3.14 | 54% | 0.02 | (99%) | (99%) |
| **Air Travel** | | | | | | |
| Delta Airlines | 10.28 | 6.62 | (36%) | 6.17 | (40%) | (7%) |
| UAL Corp. (United Air Lines) | 5.67 | 4.15 | (27%) | 2.08 | (63%) | (50%) |
| priceline.com | 2.28 x | 6.94 | 205% | 0.22 | (90%) | (97%) |
| **Advertising Services** | | | | | | |
| | 1.66 x | 4.92 | 196% | 4.70 | 183% | (4%) |

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| Young & Rubicam[1] | | | | | | |
| DoubleClick | 0.27 x | 11.39 | 4,124% | 1.36 | 403% | (88%) |
| **Stock Trading** | | | | | | |
| Merrill Lynch | 24.44 | 30.55 | 25% | 54.91 | 125% | 80% |
| Charles Schwab | 11.23 | 36.00 | 221% | 39.26 | 250% | 9% |
| E x TRADE | 0.31 x | 6.39 | 1,969% | 2.26 | 629% | (65%) |
| **Communications** | | | | | | |
| AT&T | 99.58 | 162.32 | 63% | 64.75 | (35%) | (60%) |

| | | | | | | |
|---|---|---|---|---|---|---|
| America Online | 9.43 | 169.58 | 1,698% | 81.21 | 761 | (52%) |

[x] Company was not public on December 31, 1997. The market valuation for these companies has been calculated by multiplying the company's IPO price by the number of shares outstanding immediately after its IPO.

[1] Young & Rubicam was acquired by WPP Group in October 2000. Calculations for Young & Rubicam at 12/31/00 are based on the announced transaction value of $4.7 billion.

**Outlook for 2001**

During 1999 and the first quarter of 2000, an unprecedented number of companies went from start-up to IPO in two years or less. The ebullient IPO market and venture capital investors eager for quick returns led many companies to go public with untested business plans. Despite this year's sharp decline in market valuations throughout the technology sector, technology will remain a driver of future economic growth. Given the huge levels of venture capital investment in recent years, there will be no shortage of venture-backed companies hoping for liquidity in 2001. Companies with experienced management, strong market positions and profitable business models should be able to go public. But for many others lacking the right stuff in a selective market, deferred IPOs, acquisitions or business failures will be the order of the day.

The 2001 IPO market is likely to be populated by more mature companies. According to VentureOne, in the third quarter of 2000, U.S. venture firms largely eschewed early-stage investing and allocated 75% of their overall funding to companies that had already received at least two rounds of funding. The IPO life cycle is likely to extend, although it will probably not return to historical levels of four to six years. IPO candidates in 2001 will need to focus on creating sustainable, and profitable, business models.

The performance of the IPO market in 2001 will depend on many factors, including the following:

***Market Conditions:*** Nine months after the Nasdaq Composite index reached a record high, investors have been plunged into gloom by a market correction that has wiped out most of last year's record 86% gain. By year-end, the Nasdaq had fallen more than half from its March high and, after a summer rally, 45% since September 1. The Dow declined only 6% during 2000 but also had increased only 25% in 1999. As bad as the fourth quarter IPO market was, unless the broader market gets better, the first quarter is going to be worse. As of the end of December, only two IPOs were scheduled to price in January.

***Slowing Economic Growth:*** The U.S. economy, fuelled by the tech sector, has enjoyed unparalleled growth in recent years, but the signs of weakening are now unmistakable. In late December, the government revised downwards its estimate of overall economic growth in the third quarter to an annual rate of 2.4% from the 2.7% reported a month earlier. Third quarter growth was less than half the second quarter's rate of expansion and was the most sluggish in four years. In recent weeks, both investments in capital equipment by corporate America and U.S. consumer confidence - two engines of the economy - have shown early signs of deterioration. Rising oil prices - more than tripling in the past two years - are also a concern. It remains to be seen whether the Fed's surprise interest rate cut in early January, or President-elect Bush's proposed tax cut, can jump-start economic growth or at least engineer a smooth landing to the longest-running economic expansion in U.S. history.

***Corporate Earnings:*** A spate of earnings warnings at the end of the fourth quarter roiled the markets. In addition to the renewed emphasis on profitability for all companies pursuing IPOs, slowing earnings particularly hit technology companies, whose valuations depend on very high rates of expected earnings growth. Upcoming fourth quarter earnings announcements should help set the tone for the IPO market in 2001.

***PC Sales:*** Slowing growth in PC sales has the potential to affect all Internet and computer-related technology companies. The fourth quarter saw a string of profit warnings from Apple, Compaq, Intel and Microsoft, among others. PC sales in the commercial sector have been sluggish with Windows 2000 failing to boost corporate PC buying. The consumer PC market has begun shifting from a growth to a replacement market, curtailing the high-velocity growth of PC makers.

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*Notes on Data: Hale and Dorr compiled all data in this review unless otherwise noted. Offerings by REITs, bank conversions and closed-end investment trusts are excluded. Offering proceeds exclude proceeds from exercise of underwriters' over-allotment options, if applicable. The data came from a number of sources, including IPO.com, IPOCentral.com, SEC filings and the Washington Service Bureau.*

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