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IPO season: which stocks to avoid as listings ramp up

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The US and the wider world are deep in the throes of initial public offering (IPO) season, with recent floats for Beyond Meat, which produces plant-based meat substitute products, and ridesharing giants Lyft and Uber.

Shares in Uber, already a well-established private company, were priced at $45 at IPO, giving it a valuation of $82 billion (£64.4 billion).

Few groups have commanded such lofty price tags. Investors would have to look back to Facebook's infamous IPO in 2012 – which saw it plunge on day one after processing errors caused it to rack up losses of $200 million in the first two hours – to find a larger float in recent history.

Last year marked a jump in listings on the US market after 190 companies went public, the most since 275 were listed in 2014. That said, we are far from the bubble era, when 486 floated in 1999 and 406 in 2000.

This year, the IPO market has only started to gain momentum in recent months. There was a muted start to 2019, largely due to the US government shutdown and the sharp sell-off in late 2018, which spooked would-be listers. Indeed, the current trend suggests fewer companies will list in 2019 than 2018, although the big deals may well push the overall value higher than the previous year.

Picking your way through IPOs has always been tricky. Outside all the euphoria and hype – much of which is stoked by those who are flogging the shares – many companies quickly vanish into obscurity, with only a handful of shining lights going on to become the most successful companies in the world. Nonetheless, some of those coming to market this year, particularly Uber, could be just that.

The runners

Lyft, Uber, Pinterest, Zoom, Greenlane, Slack, Airbnb, WeWork, Peleton, Bumble and Beyond Meat are all either happening or have happened this year.

The tech-heavy similarities to 1999 aside, the first few names have experienced mixed outcomes since listing. Lyft, the US-based ride-sharing company, has lost almost a third of its value since floating last month, down from around $78 a share to $53 now.

In comparison, Beyond Meat had an impressive debut, with shares surging on day one. Today, its share price has risen by 35% since IPO, around $89 per share.

All eyes are now on Uber, the company putting not only taxis and cabs around the world under threat but also the wider transportation industry.

Anthony Ginsberg, managing director of

GinsGlobal Index Funds, which runs the HAN-GINS Innovative Technologies ETF, said both Uber and Lyft have some initial challenges for investors to consider. Nevertheless, he views their growth profiles as hugely positive.

'Uber and Lyft currently do not make any profit, but their revenue growth and global expansion is impressive. Uber's revenues reached $11.3 billion in 2018, up 43% from the previous year (although, admittedly, it is lower than the 61% growth in 2017).'

'It is loss-making – the company lost $1.8 billion in 2018, down 15% from a $2.2 billion loss in 2017 – but both Uber and Lyft's revenue growth is following in the footsteps of Amazon,' he added.

Ginsberg pointed out that Amazon consistently lost money for its first several years as a public company.

'The likes of Uber and Lyft also operate in a highly disruptive space – ridesharing,' he said. 'This market opportunity is truly global, offering economies of scale and where first mover advantage and brand recognition is key to securing sizable market share.'

Ginsberg also believes that Uber has another advantage with its off-shoot food delivery app, Uber Eats, which he said should not be discounted by investors.

'Uber Eats is growing fast – representing $1.5 billion, or about 13%, of the company's total 2018 revenue. Uber Eats' revenue grew by 149% from the previous year's $587 million total,' he explained.

There is no doubt that, like Amazon, Uber and Lyft's current plan is for market share, not profits. As disruptive technology companies scale up globally, their capital expenditure rises, in order to build out infrastructure and distribution.

With this in mind, Neil Goddin, manager of the Kames Global Equity fund, takes the view that focusing on profits is not the right way to view these companies.

'There seems to be increased scrutiny of the financial health of the company – especially if it is cash flow positive or not,' he said.

'For us, this misses the point. If a company is loss-making today because it is building itself scale economics or strong network effects, then it is not the right metric to look at.'

So, should investors hold back from investing in Uber? Adrian Lowcock, head of personal investing at Willis Owen, said the valuations attached to Uber could leave investors in the red for some time to come.

'Investors looking at these IPOs need to consider whether they want to take the risk as, given the valuations being mooted, even if they turn profitable, investors could still lose money if they pay too much to buy them at the beginning,' he said.

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Anthony Ginsberg, GinsGlobal Index Funds

Goddin added that it was impossible to know if a company is listing at the right time for both itself and for its would-be investors. But he said there was no denying Uber and its ilk were achieving their main goal to cut prices in established industries.

'The question is are these tech unicorns cashing in at the top of the market (and, arguably, the right time for themselves)? Investors trying to buy into these IPOs will likely have to either be very fast at selling or very choosy in terms of which IPOs they participate in,' he said.

Playing the long game

Of course, there are some outright bulls out there putting Uber on a future valuation of $120 billion. Ginsberg said the long-term potential for Uber could be akin to Amazon.

'Amazon first reported a quarterly profit in the fourth quarter of 2001, and at just $5 million. This was more than four years after Amazon went public. Chief executive Jeff Bezos ignored Wall Street analysts clamouring for quicker profits and prioritised Amazon's product offering, distribution infrastructure and geographic expansion,' he said.

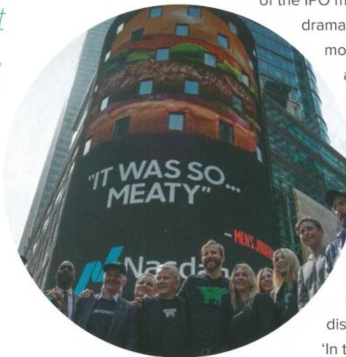
'In the early years, this was clearly done at the expense of short-term quarterly profit targets, but today Amazon is worth approximately $1 trillion, making it one of the world's most valuable companies and Bezos the world's richest person.'

He added that Tesla, nearly a decade into its listing, is an example of how long this can take. However, this should not deter investors.

'Tesla remains unprofitable, too, but has seen its market value rise dramatically since its initial public offering in 2010,' he said.

Sit up and pay attention

A final point to consider is that the very nature of the IPO market has changed dramatically in recent years. Far more businesses are tried and tested before coming near the public markets, now allowing for proof of concept to be well-established. This, in turn, has resulted in some lofty valuations (for example, Uber), but for investors, it also means nothing can be dismissed out of hand.



'In the US alone, there are around 160 different companies now with private market valuations in excess of $1 billion. That's different to the late 90s and early 2000s, when some of these companies would go public with little financial history,' Peter Bourbeau, manager of the Legg Mason ClearBridge US Large Cap Growth fund, said.

'Of course, within that, some businesses demand our attention because they are so disruptive,' he added.

'So while we won't buy all the IPOs that cross our desk, we are certainly paying attention and looking through all them.' •