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Why Individual Investors Lose on IPOs

By KATHY M. KRISTOF
TIMES STAFF WRITER

"White-hot."

That's how investment bankers described the initial public offering of Netscape Communications. Individual investors who bought shares Wednesday—Netscape's first day of trading—can attest to that.

They were the ones who got burned.

Unfortunately, that's not unusual in the fast-paced and treacherous world of initial public offerings. All too often, individual investors who are intent on buying the hottest deals end up buying high and selling low.

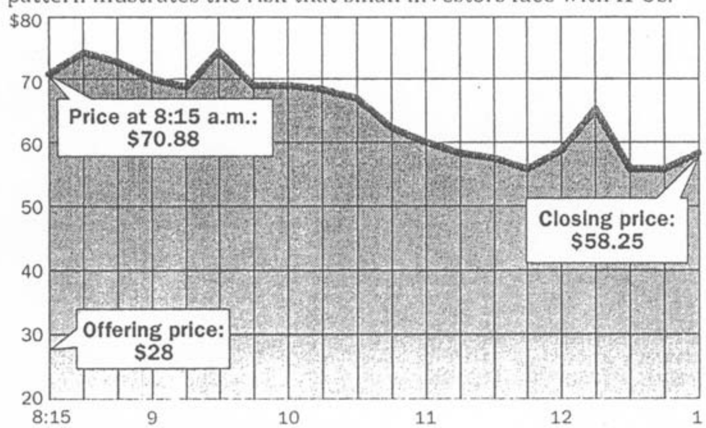
The reason that happens is simple. Individuals are at the end of the line when it comes to being offered the best deals, says Lloyd Greif, president of Greif & Co., a Los Angeles-based investment banking firm. By the time retail customers are able to grab a share of the stock, the big money—arguably the "smart" money—has come and gone.

The Netscape deal was a case in point. The deal was fully subscribed-in other words, every share was purchased and accounted for by a contingent of favored institutional customers—before the stock ever hit the street. These institutions got the shares at just $28 each. But—in a process called "flipping"—the moment trading started, they sold—at prices ranging from $71 to $75 a share.

That's when retail investors had their chance to get in. Within hours, however, the deal cooled. The company's stock price slid into the mid-50's, before recovering somewhat and closing at $58.25. The hapless individuals who bought at $75 realized a whopping 22% single-day loss.

Roller-Coaster Ride

Investors who bought Netscape Communications shares early in its first day of trading Wednesday were soon disappointed. The pattern illustrates the risk that small investors face with IPOs.



Source: Bloomberg Business News

Unusual? Hardly. A recent study by David L. Babson & Co., a Cambridge, Mass., investment counseling firm, found that IPOs are frequently a bad deal for investors.

Their study of 513 such deals found that in 56% of IPOs, the stock prices fell from the closing price on the first day of trading.

"The best day of [an IPO's] performance basically comes on the first day of trading," the study found.

"Unfortunately, for most individual investors without much clout with brokers, getting in on an initial offering is extremely difficult. After that, both the companies' fundamentals, and their stock prices, tend to deteriorate."

Why can't individuals get in on the ground floor? Because institutions have more money and more clout. Individuals come and go in the IPO market, Greif adds. But institutions consistently snap up the bulk of every IPO.

As a result, they're offered the deals everyone wants.

"Because they are favored clients of the brokerages, they get the first chance to buy it. And they, of course, get the chance to 'flip it,' " says Greif. "Retail investors are at the end of the queue. By the time it gets handed to them, it's like a time bomb. Each person further down the line who gets it is closer to the fuse."

Investors Get Caught Up in the Netscape

■**Wall Street:** Software company makes an impressive debut, as its stock soars from $28 at the offering to as high as $74.75 in a trading mania.

By JULIA PITTA
TIMES STAFF WRITER

In one of the most impressive debuts Wall Street has ever seen, investors Wednesday frantically snapped up share of Netscape Communications Corp., the 15-month-old Mountain View, Calif., company that makes software for browsing the Internet.

During its first day of trading, Netscapes' stock rocketed as high as $74.75 from the initial public offering price of $28, before settling down to $58.25 per share by the market close.

More than 13.8 million shares changed hands in frenzied trading on the Nasdaq stock market, meaning the 5 million Netscape shares initially offered effectively turned over twice.

Even with the price drop late in the day, Netscape had the fourth-biggest first-day increase in trading price in history—a 108% gain.

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