Morning Brew x Fidelity
Fresh Invest Podcast
EP1 Sam Shore Transcript
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Alex Lieberman [00:00:13] What is up, everyone? This is Alex Lieberman, cofounder and CEO of Morning Brew. And this is Fresh Invest, your new favorite investing podcast sponsored by Fidelity Investments and powered by Morning Brew.

Alex [00:00:28] Here's what you can expect from Fresh Invest. Each week, I will dive into a massive business topic making headlines, and work through the impact that topic has on my portfolio. Fresh Invest is the jet fuel you need as a young investor. And today's topic is about as topical as it gets. We're talking IPOs and the current rush to take private companies public. We've been seeing them in the Brew's headlines almost daily. Some of them household names, others so obscure, we can almost hear the whoosh over our heads as they pass by. Dozens of companies across a myriad of industries are rushing to ring the IPO bell this year.

Alex [00:01:08] And that begs an array of questions for young investors like myself, trying to understand what it all means for the market and how it impacts your decisions for your portfolio. How should I be thinking about Ant Group's record-breaking $300 billion listing talked about in a recent Brew? And, did it make sense to invest into the IPO for companies like Snowflake and Asana and Palantir? Or is it worth giving the shares some time to breathe?

Alex [00:01:35] At its core, I want to explore the intricacies of the IPO process, what happens leading up to it, and what to look out for in the days and months that immediately follow. I want to understand whether these IPOs are even an accessible investment for someone looking to get in, and if so, how to approach it altogether.

Alex [00:01:55] A few weeks ago, Fidelity let me ask one of their very own about this whole IPO phenomenon. In my conversation with Sam Shore, he broke down all the components of an IPO, the reasons behind the current boom, and the implications it has for us as investors. Let's get to our conversation.

Alex [00:02:14] Time to talk IPO frenzy. Sam, thank you for joining the conversation.

Sam Shore, Active Trader Strategy Desk at Fidelity Investments [00:02:21] Good morning. Happy to join you today.

Alex [00:02:22] So, before we break down just the IPO market broadly, can you just give me some context on what you're up to, what you do, and how this all relates to IPOs in general?

Sam [00:02:35] Absolutely. I work with Fidelity Investments as part of Fidelity's Trading Strategy Desk. And really what I do day in and day out is helping individual investors who are looking to actively manage their own portfolios, using the tools that we offer at Fidelity. In conjunction with that, we also offer small-group coaching sessions for our traders at Fidelity, available at Fidelity.com/coaching. And certainly this involves discussing IPOs, especially with the increasing number of names that we've seen coming public in recent weeks.

Alex [00:03:03] It seems as if there have been a ton of IPOs in recent weeks or even months. First of all, is this the right impression that I have? And, if so, why do you think there has been such a proliferation of companies going public recently?

Sam [00:03:17] Yeah, I definitely don't think it's wrong that we've seen more and more companies coming public. And it makes a lot of sense if you start to think about the moment in time that we're at. We've seen a lot of different businesses—because of a lot of the COVID restrictions, people working from home—where their growth has accelerated substantially faster than they might have predicted.

Sam [00:03:39] And because of this, they need additional capital to maintain this growth and continue operating their business. And so, going public at this point in time allows them to reach out to a larger investor base in order to sustain that growth that's really ramped up on them. Certainly, fortunately for them, but unexpectedly in a lot of ways.

Alex [00:03:59] Just to be clear, fast-growing companies can raise private capital, right? So I guess what I'm trying to understand is, is there not still the opportunity for businesses to raise money from private investors rather than go public?

Sam [00:04:14] There is, of course, but there's a lot larger investor base that is available when they start to tap the public equity markets. And, a lot of times, some of these private capital raises, they're having to give up more than they might like. Maybe it's a seat on the board. Maybe it's a larger ownership interest in the company. Anything along those lines. Whereas when they choose to go public, they can get the larger investor base and in some cases, depending upon how the offer is structured, perhaps give up a little less control than they might otherwise have to.

Alex [00:04:47] As a young investor that's started to put some of their money to work, how should I think about participating in IPOs, and honestly, is it something I can even participate in if I wanted to?

Sam [00:05:00] So certainly there is the ability to get IPO shares sort of when they're allocated at that IPO price. You do have to work with a financial firm and see if the broker that you're working with has access to the shares. That being said, even if you aren't able to participate in that way, you can still buy the shares on the market. And we've also got to remember, a lot of times with these IPOs, these are companies that have newer growth prospects. Maybe they don't yet have earnings. So it might be a slightly riskier portion of your portfolio.

Alex [00:05:34] Let's make the assumption that I can get allocation through whatever platform I'm using. Do I actually want to invest in these companies right after they go public?

Sam [00:05:45] So certainly that's going to vary from company to company. But, you do, of course, before the offering, get to take a look at the information that the company has with the offering. There's a document called a preliminary prospectus—or an S-1, if you're getting really sort of technical—and that details the company's business prospects, risks that they see to their business, as well as the financials of the company.

Sam [00:06:12] And then the other thing, of course, to consider is, what is the price at which they're choosing to go public? A company might be appealing at a price of $20, but maybe they're offering shares at $30. And maybe you don't think that's a price that you want to pay for that company.

Alex [00:06:27] And just to get a sense, how is the price at IPO determined?

Sam [00:06:32] We've got to remember at the end of the day, the motivation for a lot of these companies going public is to get a broader investor base, but also to raise capital for the company. So the company will typically work with investment banks. They'll come out with an expected pricing range to try to generate interest in their IPO. If they find out there's a lot more interest than they expect, well they might raise that price because they realize they can get more capital for the company by doing so.

Sam [00:07:02] Conversely, if there's less interest, then you might see a price at the bottom end of the range or below the range. But that sort of trade-off is, well, at what price can they entice enough investors to participate and still make it worthwhile for the company to go public, to go through the bother.

Alex [00:07:20] Got it. And so, you know, there's a term I'm familiar with from just looking at IPOs in the past, which is this idea of the lock-up period relating to early stockholders within these recently public businesses. Could you just provide some more context on how lockups work?

Sam [00:07:39] So typically those lockups are imposed on pre-IPO investors, company executives, or company employees. And really, it just means after we IPO, here's a set period of time where you still have to continue owning the shares. And what that means to you, really, is these are additional shares that have the potentiality to hit the market in the future. So you might say, you know what? I've looked at this IPO. Maybe it's already started trading. I'm purchasing shares. I'm happy with current pricing.

Sam [00:08:14] But you've got to remember, there's the potential for greater dilution and greater availability of shares on the market in the future after some of these lockup periods end. And so you sort of have to have in the back of your mind, well, do I think there will be continued demand for these shares to support some of this additional supply of shares that might come onto the market six months or a year after the IPO?

Alex [00:08:38] And is that generally the thought process behind just lockup regulation existing? Is it around this concept that the bodies that oversee IPOs and public companies, that they don't want there to be a potential precipitous drop in price with too much supply hitting the market? Or are there other reasons that this exists?

Sam [00:08:58] Really, that's the biggest factor, is no company wants to be the IPO where they go public and the stock price closes down substantially from where they priced, and the next few days of trading it continues going down. Certainly companies want the investors who purchase into their company to be happy that they did so and continue to hold the shares.

Alex [00:09:20] So, we've talked about the prospectus, or S-1, that any potential investor has access to prior to IPO. I guess beyond me just pouring through the S-1 and gleaning insights for myself, is there anything else that you'd recommend that I do in evaluating whether I should invest in a company headed into its IPO?

Sam [00:09:40] I've got to headline by saying while it's probably pretty dry reading in a lot of cases, the S-1 is straight from the horse's mouth. So I would definitely encourage looking at that. But in addition, you've got to ask yourself, well, what do I really think about this company? Maybe you look at the market or the industry that that company is in. What is the place for that company in that industry? How do they compare to other competitors that exist in that industry now? Is this company coming public better or worse than those companies?

Sam [00:10:12] And then you can also, of course, take a look at, well, what are people saying about the IPO in advance? Now, you've got to take some of that with a grain of salt. Some of these people do have vested interests. They may also be shareholders. But it doesn't mean that you can't sort of absorb all the information out there around the IPO.

Alex [00:10:30] So I have a question that probably will sound a little bit, you know, tactical or in the weeds, but, could you potentially walk me through the IPO process? So just like thinking about when a company or its founders decide, hey, we want to go public. Like you said, we have a ton of growth. We want access to more capital in the public markets. From that decision point in time to actually the act of going public the day of, what is all the stuff that happens in-between?

Sam [00:10:57] So certainly there are a bunch of nitty-gritty steps. I'd say the sort of major things from when they make that initial decision is, one, they're going to work with some sort of investment bank. And that investment bank is going to help with a number of the steps between the decision that they want to go public and the first day of trading. Big things along that line are they're going to file the initial preliminary prospectus, of course. There's a cooling-off period after they do so, where they can't really advertise or hype the IPO too much.

Sam [00:11:29] But, in addition to that cooling-off period, they're also going to host a number of, really, investor roadshows to try to entice or inform different institutions about this offering that's going to come public. Then, of course, we already sort of alluded at a little bit, they'll have their preliminary pricing range, and they'll try to get a gauge of how much interest is there from the different investment banks, institutions, and their customers before announcing, well, here's the actual price at which we're going to IPO, which is usually sort of the evening before they intend to begin trading on U.S. exchanges.

Sam [00:12:10] Then, of course, the shares are allocated out to the institutions who've decided they're willing to pay this price or their customers are willing to pay this price. Then, I think we all sort of see on the media the next day where they begin trading. They probably ring the bell at a major exchange. It's sort of a big show of the initial beginning of trading for that given company.

Alex [00:12:29] My final question for you is, I want us to think about not 27-year-old Alex Lieberman, but 21-year-old Alex Lieberman. So Alex just graduated from college. He just moved to New York City. He's working in financial services. So he's proficient around the markets, but not fluent. And he's thinking about, you know, potentially there's a major IPO coming up and he's thinking about like, should he do anything? How should he be thinking about this as a 21-year-old who's making more money than he's made in the past but isn't sure how much should be allocated to something like an IPO? How would you guide Alex?

Sam [00:13:04] I think it's important to remember that IPOs are probably, of your investable assets, a riskier portion of it. Remember, it's a new company. Maybe their growth prospects are uncertain. They might not have earnings yet. So while if it is a company that you really like, you've gone through, you've done all your homework. You did all the reading of the S-1 and have decided, well, this is a company that I'm really interested in.

Sam [00:13:27] Keep in mind, well, what percentage of my portfolio, of my investable assets, am I allocating to this potentially risky idea? Certainly, you'd want it to make a difference. So you wouldn't want to say, well, I'm going to allocate $10 for this. But at the same time, it's probably not wise to say, well, let me move every penny of my investable assets into something that's potentially risky. You want to have sort of the satellite, or smaller portion of your portfolio that's maybe more speculative or designed for more risky investing, that you're utilizing that portion of your capital when looking at an IPO.

Alex [00:14:00] For sure. So basically, what I'm hearing is that thinking about the allocation of potentially some amount of my money into an IPO should really be around, kind of like what is my risk appetite as a 21-year-old, and also truly understanding what is just the risk profile of a newly public company.

Sam [00:14:21] Absolutely. You're probably going to be more willing to take risk than someone four times your age. But, you've got to recognize, well, I've got to have some balance here. The notions behind balancing risk and asset allocation don't sort of fly out the window just because you're 21. But you can certainly afford to take more risk because you have a much longer time horizon.

Alex [00:14:42] Totally. Well, Sam Shore, thank you so much for your time and your insights. Really appreciate it.

Sam [00:14:47] It's been great to join you today.

Alex [00:14:50] That was wild. I feel like I just got 15 years of IPO knowledge in 15 minutes. Let's do a little takeaway tear down. First, I get why so many companies are quick to ring the bell these days. For some, IPOs offer much-needed liquidity during a period of economic uncertainty. And for others, COVID has been the growth catalyst needed to take their business to the major leagues.

Alex [00:15:14] Second, it's not so simple to get, quote unquote, involved in an IPO. As an individual investor, you may or may not have access to shares at the IPO price through your investment adviser. And if you don't, you'll have to wait until the shares hit secondary. The list of learnings goes on. We also talked through lockup periods, post-IPO volatility, and the importance of scanning an S-1. All of these things I'll be keeping in mind ahead of the much anticipated Ant Group IPO.

Alex [00:15:44] As always, thank you for tuning into Fresh Invest. Check out Fidelity.com/FreshInvest for more information and resources. And make sure to join me next week when I dig into gold.

Morgan Chmielewski, Producer of Fresh Invest [00:16:07] Hey, everyone, this is Morgan Chmielewski from Morning Brew. And as the producer of Fresh Invest, I'm here to let you know that this podcast was created on behalf of Fidelity Investments by the Morning Brew Creative Studio, and does not reflect the opinions or point of view of the Morning Brew editorial team. Sources are provided for informational and reference purposes only. They are not an endorsement of Fidelity Investments or Fidelity Investments' products.

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Morgan [00:17:49] See you next time.