



A Prescription To Fix VC-Backed IPOs?

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<http://www.pehub.com/38539/a-prescription-to-fix-vc-backed-ipo-market/>

The National Venture Capital Association this morning released a four-point plan to revive the slumped market for VC-backed IPOs. Two of the pillars are aimed at public authorities (tax incentives & SOX/RegD reform), while the other two are aimed at the private sector (ecosystem enhancements like helping form more boutique I-banks & creating new liquidity paths via secondary direct markets like InsideVenture, SecondMarket, etc.).

What's important to realize about NVCA's presentation (posted below) is that it argues that VC-backed problems are systemic, rather than recessionary. For example, the Spitzer-prompted separation of research and investment banking has caused massive drainage of the analyst pond, thus making it far more difficult for VC-backed companies to obtain coverage. And as much as I hate relaxing regs that were designed to protect investors, I'll concede that small-cap companies should not be under the exact same rules a large-cap companies. Or at least they should have a more streamlined process (particularly vis-a-vis SOX compliance).

But let me also make a few additional points:

1. One of the biggest problems for VC-backed IPOs is that the public markets require actual cash-flow. Often it even wants profitability (gasp). Venture capitalists may find such requirements short-sighted — after all, an unprofitable company can still become a great investment — but they were largely borne of VCs pushing an abundance of crap into market during the dotcom boom.
2. Speaking of those “glory days,” they were the exception when it comes to VC-backed IPO volume. Just take a look at Page 6 of the NVCA presentation. What you'll notice is that VC-backed IPO volume for most of this decade has mirrored VC-backed IPO volume during much of the 1980s (when

companies like Dell, Cisco, MedImmune, etc. went public). Sure there have been fewer than 10 VC-backed IPOs since the beginning of 2008, but that's obviously more recessionary than systemic.

3. One more note on the late 1990s: Capital gains rates were higher than they are today. As such, I simply don't buy NVCA's argument that the "carried interest as ordinary income" proposal will have much impact on the VC-backed IPO market. (note: carried interest is taxed at just 15% today, and I don't see VC-backed IPOs flying off the shelves).

4. Finally, the NVCA is trying to make both a macro-economic case (most VC-backed company job growth comes post-IPO) and a VC industry case (IPOs produce best returns for investors). And both cases are sound. That said, most VCs I know have given up on making investments with an IPO in mind. Instead, they want to help their companies build with an eye toward eventual trade sale. Not that an IPO is ruled out, but it's more a dream than anything else.

Let me use a tortured baseball analogy: A general manager tries to get a guy who hits lots of homeruns to bat cleanup. The hope is that he'll end of hitting grandslams, but you don't sign a guy who "hits grandslams" — because that's mostly a question of circumstance. Same goes for VCs, with trade sales as homeruns and IPOs as grandslams.

5. I briefly discussed this plan on CNBC this morning, alongside Dixon Doll. The video is [posted here](#).