Why Unicorns Are Not So Special Anymore

***e*Research Corporation** is pleased to provide an article courtesy of **Investing Daily**.

The article is reproduced below, beginning on the next page, or you can go directly to it at the following link: https://www.investingdaily.com/41628/why-unicorns-arent-so-special-anymore

You can also visit the **Investing Daily** website at the link below:
https://www.investingdaily.com/

Preferences | About Us | Contact Us | Privacy Policy

Copyright 2018 Investing Daily. All rights reserved.
Investing Daily, a division of Capitol Information Group, Inc.
7600A Leesburg Pike
West Building, Suite 300
Falls Church, VA 22043-2004
U.S.A.

***e*Research** was established in 2000 as Canada's first equity issuer-sponsored research organization. As a primary source for professional investment research, our Subscribers (*subscription is free!!!*) benefit by having written research on a variety of small- and mid-cap, under-covered companies. We also provide unsponsored research reports on middle and larger-sized companies, using a combination of fundamental and technical analysis. We complement our corporate research coverage with a diversified selection of informative, insightful, and thought-provoking research publications from a wide variety of investment professionals. We provide our professional investment research and analysis directly to our extensive subscriber network of discerning investors, and electronically through our website: www.eresearch.ca.

Bob Weir, CFA: Director of Research

Note: All of the comments, views, opinions, suggestions, recommendations, etc., contained in this Article, and which is distributed by *e*Research Corporation, are strictly those of the Author and do not necessarily reflect those of *e*Research Corporation.

Why Unicorns Are Not So Special Anymore

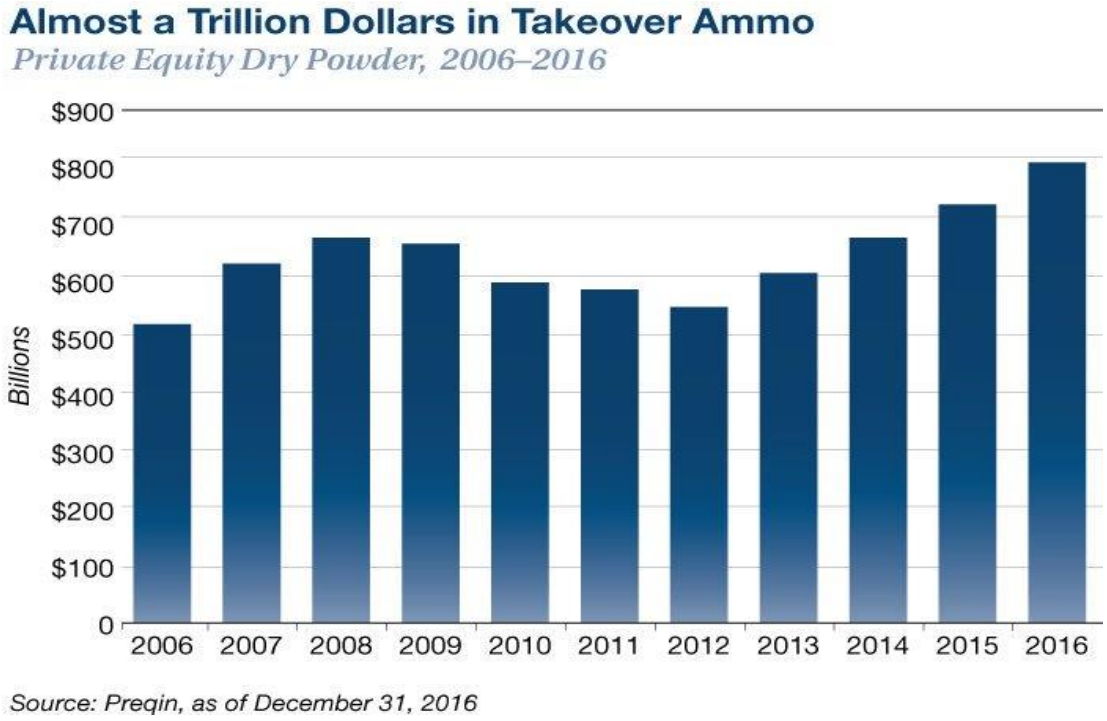
By Linda McDonough (bio at end)
March 28, 2018

Everyone loves unicorns. They are unique and magical and harness special powers. So, it is appropriate that private companies sporting valuations about $1 billion are deemed to be unicorns.

But they run the risk of dying once set loose in the wild.

Mountains of capital in private equity funds have resulted in some pretty well-fed unicorns. According to industry tracker Preqin, a record $453 billion was raised by private equity firms in 2017, beating out the prior high of $414 billion in 2007.

After being added to the already robust coffers of private equity, this leaves about $1 trillion dollars looking for a home in new investments. Just think, these newly-added investments could give birth to almost 500 new baby unicorns!



The problem for the overpopulation of unicorns is that their best days seem to be in the confines of private equity. Once introduced into in the "real world" of the stock market via an IPO, many unicorns start to suffer.

Take Snap for example. The company priced its IPO at $17 in March 2017 and, after a very brief (don't blink) move up to $24.40, wilted to its current $16 price. Snap's highest price occurred on its very first day of trading.

Blue Apron might take the prize for the most fragile unicorn. That IPO priced at $10 and is now bumping up against $2.00 after reporting just three quarters as a public company. The first two reports were disastrous, the third, merely dreadful.

What gives?

How can investors be so excited about these super-fast growers and bid them up during the IPO process and even more on the first day of trading only to turn tail so quickly?

The problem lies in the timing of these IPOs. Before the avalanche of private equity dollars, companies typically went public in search of capital from new shareholders. They needed the money to spend on investments to grow their companies. The capital was spent building out factories, opening stores, and hiring teams of software engineers to fine tune their products.

Raising capital at an earlier phase of the growth cycle benefits investors. They jump on early, typically at a lower valuation that the company would receive in a later part of the cycle, and then jump on to enjoy the ride on the growth train. Private equity investors are enjoying this growth but the public is not.

When Coach, now Tapestry, went public in 2000 it had only 106 stores and got just 11% of its sales internationally. The company had a huge runway of growth ahead of it. Over the course of the next 18 years, Tapestry opened 900 more stores, rapidly expanded overseas distribution, and grew revenue tenfold.

Many private companies prefer to stay private. They understand the difficulty of operating under the public eye and the glory and the wrath involved in estimating and delivering results on a quarterly basis. It is only logical that many would prefer the safe confines of being private if it was not necessary to leave the walled garden in search of capital.

With so much capital being fed to the unicorns via private equity, many private companies are delaying IPOs until a much later point in their growth cycle. Sometimes they are using the money raised to grow the company but often the capital is used to pay off debt, or to pay a "one-time" dividend to the private equity investors. Oftentimes, the company does not raise ANY money on the IPO and the deal is a way for insiders to sell shares and to provide insiders liquidity for their shares. Issuing shares to employees is a nice carrot to have for new hires. When these companies are further out in their growth cycle, revenue growth is often declining. Blue Apron had seen its peak growth two years before the IPO. Delaying an IPO meant hitting the public markets just as revenue growth plummeted.

Dropbox, which just priced its IPO last week, is seeing a small deceleration in revenue growth. After a 40% jump in revenue in 2016, growth dropped to 31% in 2017, and to the high 20%s in the December quarter. This does not mean Dropbox will be a dud of an IPO. However, it means that investors need to be more careful about choosing which deals to buy. If a company's best growth days were had in the unicorn field, your capital may be setting itself up for extinction.

#####

Website: https://www.investingdaily.com/

See About the Analyst on the next page.

About the Analyst

Linda McDonough is a veteran hedge fund analyst who loves to break down company financial statements and identify market inefficiencies to uncover big opportunities. She believes in a boots-on-the-ground approach that includes surveying customers, interviewing company executives, or doing whatever it takes to see what others don't. She's now brought her experience as a hedge fund analyst to subscribers of her *Profit Catalyst Alert* service. Her system identifies small- and mid-cap stocks that are about to move due to catalytic events that few others can identify…until it's too late. These events often times result in massive gains for her followers.