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Zynga Investor Sandy Miller: IPO Pricing More Art Than Science

LinkedIn Inc. melted the tech IPO market deep freeze when it debuted last month, warming the way for other high-growth consumer Internet companies in registration such as daily deals site Groupon Inc., music streaming service Pandora Inc. and online vacation-rentals company HomeAway Inc. Now, social gaming companies Zynga Inc. and PopCap Games Inc. are planning their entries to the public markets.



Sandy Miller

Institutional Venture Partners General Partner Sandy Miller, an investor in Zynga, was mum on the FarmVille creator's plans, but he did speak with Venture Capital Dispatch about his thoughts on the IPO market heating up.

Having opened the San Francisco office for Merrill Lynch and Donaldson, Lufkin & Jenrette where he managed investment banking before becoming a senior partner at Montgomery Securities and co-founding Thomas Weisel Partners, he's seen his share of offerings from both the buy and sell side.

Below is the edited conversation with Miller, who discusses how this fresh batch of companies are being priced, investor appetite for "alpha" companies and whether he believes this has the makings of another tech bubble.

Q. Is this the beginning of a tech IPO wave?

A. Yes. We have the best IPO market we've had in some time, but it's not just related to LinkedIn. It's a combination of having a buildup of really great companies and a lot of buy-side interest from institutional investors, like mutual funds.

Q. How so?

A. In many cases they have large cash positions and they like IPOs because they provide spice and extra alpha to their portfolios.

Q. Let's talk about pricing an IPO. How much is art and how much is science?

A. It's more art right now. We're very early in this new robust IPO market. As we move into more of a cycle the efficiency of pricing improves because there are more comparables.

Q. Any thoughts on the pricing of LinkedIn, Groupon or others now coming out of the gate?

A. Companies are always priced as compared to public comparables, presumably at some discount. The market loves growth and that's why these companies are getting premium valuations. The bulk of tech portfolios today (for major mutual funds) are in big cap companies that are no longer growth companies. Microsoft would be the extreme example of what was once a great growth company is no longer a fast grower.

Q. So there's pent up demand growth companies from investors?

A. Yes. It creates differentiation in the technology fund if they have a meaningful position in a tech IPO. Investors are wary of going back to a bubble environment though.

Q. What about the size of the offering? There has been discussion of Zynga being a low-float IPO, because offering less than 10% of its total shares is below the 24% average among tech companies.

A. The hot companies with large markets have never sold 24% of their shares. Google didn't sell that amount. It's an accurate average, but the variation makes it pretty meaningless. If it's a smaller IPO, you have to sell more of the company.

Q. After many of the smaller investment banks—namely Alex.Brown Inc., Hambrecht & Quist Group, Robertson Stephens & Co., and Montgomery Securities—were acquired, there has been less research coverage available for smaller tech companies. Does that impact companies trying to compete in the public market?

A. There's more limitation on research and it's harder for companies in the middle to get attention. The small ones with no real business model it doesn't effect and the larger ones like LinkedIn and Facebook will still get coverage. Those with \$50 million or \$100 million in value will struggle to get research and coverage in the aftermarket.

Q. Sometimes companies pursue both an IPO and being acquired. Can you discuss that dynamic?

A. Pursuing an IPO sometimes brings in bidders. Maybe a company has been following another company for some time. Once they see the company is going public it's a real catalyst. It doesn't impact the valuation on the IPO.

Q. Are we in an IPO tech bubble now?

A. Having gone through this for 30 years, it seems like what we're going through now is more a return to normalcy. That's healthy. I don't think I want to see a bubble again.