# The Rise of the Pre-IPO Space

Supercap.

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Today's most successful investors are often those who take advantage of the pre-IPO (or private) market, rather than waiting for an IPO to buy into equities.

Traditional IPOs have been shrinking in number, and pre-IPOs are one of the fastest-growing types of private equity investment. Between 1980 and 2000, there was an average of 300 IPOs per year, and it's now down to around 100 a year. Meanwhile, today's wealth is building up in private markets, with around 500 unicorns accounting for over $1.5 trillion, as Forbes reports.

If these unicorns were to theoretically go public on the Nasdaq or NYSE, these exchange's valuations would increase by around 25%.

Some investors choose to wait for an IPO to buy shares into a company's public float, but there is mounting evidence that this is a bad idea. In 2018, over four-fifths of IPOs were unprofitable. Pre-IPO deals provide superior returns on average, compared to their IPO cohort. And with more funds opting to invest in private companies, this trend looks set to continue.

**The rise of the Pre-IPO space: why investors should pay attention**

For much of the 20th century, it was common for companies to go public before reaching a certain sales or earning threshold. Private investors could still invest in promising young businesses, but they would have to wait until after going public before having access to stock market liquidity.

In recent years, however, this traditional model has broken down as more and more companies opt to stay private longer. Intuitively, most company growth happens pre-IPO. After all, an IPO is a complex, time-consuming endeavor that typically costs millions of dollars, which only large companies can afford.

**Why the shift?**

Going public is expensive. It involves paying fees to hire lawyers and accountants to prepare a prospectus (the legal document that explains the company's business), engaging with regulators, submitting a large amount of information, holding investor presentations and negotiations with shareholders, and more.

Not only does this process take time and energy away from running the business—but it also incurs significant legal costs. In some cases, going public can even damage a company's long-term profits by distorting its incentives or diluting founder holdings too much.

For these reasons, growing numbers of private companies choose not to go public after building up sufficient assets through their operations—especially once they have reached an agreed valuation with their investors. As a result, these companies are forced to engage in "alternative" capital raises, which can include the sale of shares to institutional investors on the private market.

The rise in popularity of the pre-IPO space is partly due to recent changes in US law that have made it more attractive for private companies to stay private longer and raise less money through IPOs. For example, the Jumpstart Our Business Startups (JOBS Act) passed by Congress in April 2012 was designed to facilitate higher valuations for businesses, and was enacted with this focus on encouraging later stage deals instead of

quick IPOs or M&A transactions.

The result of these trends is that pre-IPO deals have become more common. The rise of companies staying private longer has also been helped by new investors entering the market, and rapidly rising wealth around the world. On average, businesses are staying private 50% longer.

**The benefits of pre-IPO investing**

For investors, the main attraction of pre-IPO deals is that they allow them to get into promising private companies before they go public. By buying shares before a company goes public, investors are able to benefit from their discounted share price without having to pay full market value.

This can be useful for those who are seeking exposure to certain industries or geographies where IPOs aren't common—or if they want more control over their investment than offered by an IPO, where investors have minimal say in running the business once it has gone public.

This is particularly true for private companies that are still working out the kinks of their business model and need to grow before they can go public. Private companies who are achieving milestones on their growth trajectory will be ready to list sooner, giving investors access to these stocks at a time when they're more likely to perform well (and not so risky as to tank in price once listed).

For investors with a long-term investment horizon, this can present an attractive opportunity—especially if they believe that certain industries will become more prominent over time. For example, if you're looking to invest in the future of digital assets or FinTech, it may make sense for you to consider investing in a private company now, rather than waiting for them to IPO later and potentially miss out.

**Pre-IPO Marketplaces**

As a result, pre-IPO marketplaces have become increasingly popular among institutional investors. Investing in private companies before they IPO is certainly a long-term strategy, but it can also be an effective way for investors to gain exposure to certain industries or assets classifications before they hit the public markets.

Leading pre-IPO market platforms include Forge Global, EquityZen, and NASDAQ Private Market.

The Forge Global "deal engine" streamlines the process of finalizing transactions, serving over 300 companies, and conducting over 10,000 client transactions. Following transactions that provide liquidity to sellers, Forge charges a 2-4% transaction fee. After a $2 billion SPAC deal, Forge became the first dedicated trading platform for private shares to become a public company.

EquityZen acts as a broker, arranging transactions between investors and private company shareholders. EquityZen has closed over 15,000 investments, with a total market cap of transacted companies nearing $1 trillion dollars. Since 2013, EquityZen has transacted leading VC-backed companies such as Lyft, Evernote, and hundreds more.

With marketplaces like these acting as "on-ramps" to the pre-IPO space, we can expect to see continued growth in the private market ecosystem.

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