



# Cashing in on aftermarket bargains!

by Siu-Yee Ng

It wasn't a surprise that 2000 failed to repeat the mania of 1999. The IPO market never repeats itself.

And there's no doubt that 1999 was the best year for IPOs – ever!

Let's examine the trends in the new issues market. In 1999, two records were set – dollar volume and aftermarket perfor-

mance. A total of US\$100.6 billion was raised, breaking the previous record of 1993, US\$57.86 billion. Following the record set in 1993, *Wall Street only raised US\$33.84 billion the following year – failing to match or beat 1993's IPO performance.*

The average 1999 year-end gain in the aftermarket was 199.5% per issue. (The previous record was set in 1995, when the average gain per deal was 39.4%.) In 1996, IPOs registered an average gain of 16.8% each, failing to springboard off 1995's stellar performance. Once again, we see that the IPO market doesn't make back-to-back records.

Also consider the overall 1999 market performance. The IPO market lives and dies by the NASDAQ Composite Index. And last year, the red hot Composite ran up 85.6% to close at 4,069, up from 2,192 on December 31, 1998 – a record single year gain. This benefited the new issues market. The NASDAQ continued to soar in the first quarter of 2000.

127 IPOs debuted in the first quarter of 2000, raising US\$28.3 billion. The average deal raised US\$220 million, much more than the 59 deals raising US\$10.5 billion during the first quarter of 1999. Most deals in the first quarter of 2000 were priced above the expected range. But with the market correction in late March and April, there were doubts about whether the new issues market would be able to continue grabbing huge premiums in future debuts.

Whether they admit it or not, everyone knew that the lofty valuations of the Internet companies could not last forever. With so many companies competing in so many

specialized niches, it was obvious that winners and losers would emerge after the dust settled.

By the end of the first quarter of 2000, dot-coms were no longer Wall Street's darlings. An Internet strategy was no longer a business plan in and of itself. Instead, a practical business plan

together with tangible profits became the hallmark of companies with solid valuations.

## Playing the game

Even before the market selloff in March, new issues were experiencing a slowdown. The IPO market goes in an endless cycle. With the success of IPO debuts at the end of 1999, underwriters brought many young companies public in the first quarter 2000. This not only caused an oversupply problem, the overall quality of the companies was also in question. The inevitable result was that the new issues market went into the next cycle of decline.

The market was hot in the first quarter of 2000, and it seemed any new company could make it. Overall, this depressed returns for new issues, adding to the market turmoil by the end of the quarter.

Investors have seen this correction before. After the Asian crisis in October '98, the IPO front was quiet, with few high-flying debuts. Remember **eBay, Inc. (EBAY:NASDAQ)**? This online auction company debuted in September 98, and by October was trading as low as US\$25.00. The market recovered, and now eBay is a household name. eBay reached a 52-week high of US\$255, **and that's after a 3-for-1 stock split.**

Just like last year's market selloff in April and May, we experienced another one this

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**If the Fed hopes to achieve a soft landing for the economy, we might even see a rate cut. This would be great for the IPO market!**

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Call (410) 234-0691

9 a.m. to 5 p.m. Eastern Time

email: editor@taipanonline.com

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year. Let's look at a few plays we had in *The IPO Trader* or in *Taipan* where we took advantage of market volatility. **Numerical Technologies (NMTC:NASDAQ)** debuted on April 7 – a time when the market was spiraling downward. Nevertheless NMTC priced at US\$14 and opened at US\$23 before closing at US\$35.56 on the first day. On April 12, the *IPO Trader* bought NMTC under US\$30.50 and sold on May 4 at US\$50, for a 64% gain.

**Sangamo BioSciences, Inc. (SGMO:NASDAQ)** debuted on April 6, pricing at US\$15, and remained flat on the first day. We saw an opportunity for an aftermarket play, recommending a buy under US\$11.50 in the May issue of *Taipan*. We should see Sangamo rally in the next couple months. Sell above US\$50. On October 13 *The IPO Trader* saw a short-term trading opportunity. We bought SGMO under US\$22 and sold on October 20 at US\$35, for a quick 59% profit in just one week!

**Rosetta Inpharmatics (RSTA:NASDAQ)** debuted on August 3, pricing at US\$14, opening at US\$16.25 and closing at US\$17.88 on the first day. We bought RSTA on Aug. 10 at US\$16 in *The IPO Trader*. Then we sold on September 6 at US\$31 for a 91% profit. We're in RSTA again under US\$21, positioning ourselves for a biotech rally in the next few months.

My point is that even with a market correction, IPO investors can still make money. Look at the weakness in the IPO market as a buying opportunity. Investors can buy leading companies at reasonable prices. It's important to stick with the hot sectors and pay attention to the company's fundamentals. New issues are volatile, but playing for short term gains is possible. And it also helps to recognize the cycle the market is in.

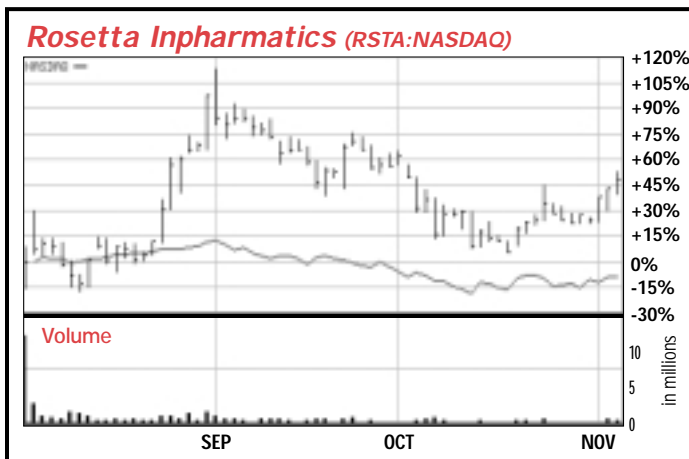
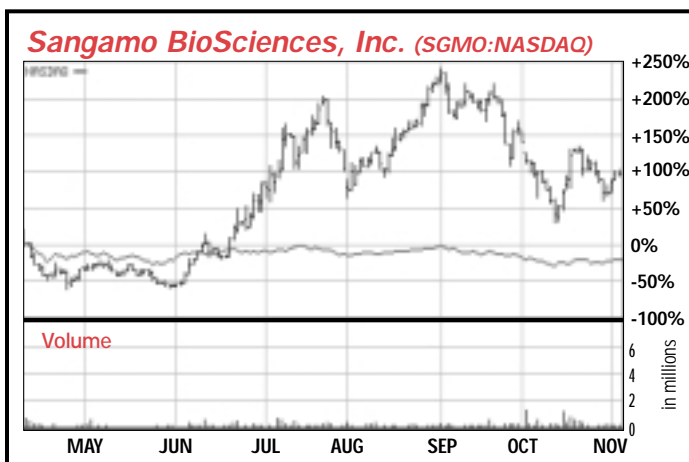
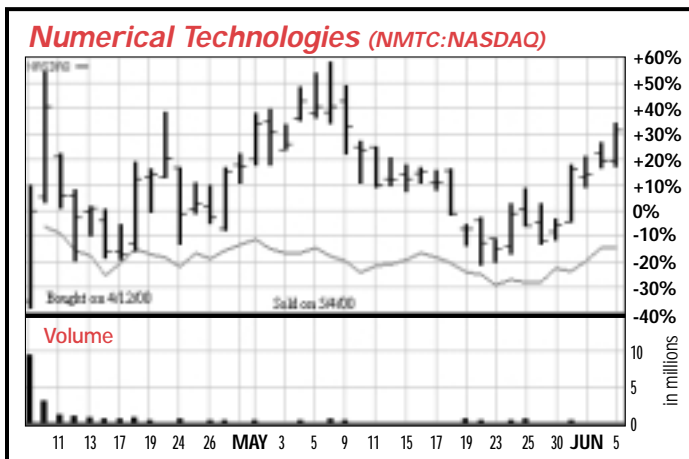
### Three key factors

There are some other strategies for playing the IPO market. New issues are subject to three volatile influences.

Trading momentum is the key

influence for the performance of a new issue. Even before an IPO debut, a certain amount of interest will be generated. If the IPO is deemed hot even before it debuts, then the stock will do well. But trading is volatile. There could be huge gains or drops within a few hours.

The second major influence on a new issue is the overall performance of the market it's in. Investors are no longer just looking at the company. If the industry is hot then the IPO will be hot too. Most have rapid sales growth off a small base and large loss growth. Some





of them will become the next big thing, but it's hard to tell which ones. So investors are bidding the entire area. If other public companies in the same industry are performing well then the IPO will likely do well also.

Finally, a small supply affects short-term gains on new issues. When investors have fewer options, they tend to buy into companies regardless of quality. So these companies will perform well in the aftermarket. But when the market is crowded, the earlier hot IPOs tend to fall.

### Sell or buy?

The IPO market is thinning, and many new companies are postponing their debuts. Who can blame them? During the week of April 10, NASDAQ fell every single day. Panic selling rocked the market and it fell below the 4000 mark, which most analysts thought would be a bottom. But the index continued to fall.

There was another panic sell in October as money managers unloaded their losers for tax write-offs. This explains why October is historically one of the worst trading months of the year. It is the end of the fiscal year for money managers and they are dumping their losers and polishing their portfolios for shareholders. The IPO market managed to

survive the bloodbath with an average third quarter IPO return of 62% and a healthy 15% in the aftermarket.

Volatility delays many IPO debuts, but those that do make it out the door will generally be the stronger deals. And those companies that do debut usually trade at reasonable prices, making it possible to build positions in these companies. *When the market rebounds these investments will pay off.* Of course, there will be duds as well – those companies that have simply run out of cash and need to raise additional capital in the public market.

As we head into 2001, IPO investors have a few things working in their favor. High on the list is what will likely be a moderating interest rate environment. Since about half the American population is somehow invested in the market, the economy is more sensitive to wealth effects than at any other time in history. Knowing this, the Fed will need to take it into account when setting interest rate policies. High oil prices, a weak Euro and a tightening of consumers' purse strings make it unlikely that the Fed will raise rates anytime soon. If the Fed hopes to achieve a soft landing for the economy, we might even see a rate cut. This would be great for the IPO market!

## Burning down the house – Our Capstone short is up 71%

by *Christian DeHaemer*

Now we're cooking with gas. **Capstone (CPST:NASDAQ)**, our favorite over-hyped alternative energy company, continues to lurch toward its doom. If you followed *Taipan's* advice and shorted Capstone at US\$90 less than two months ago, **you'd be up a cool 71%**. CPST is presently trading at US\$26.50 and falling.

I love the over-the-top arrogance of this company's leadership. As I write this, the company has offered an additional five million shares in a secondary offering at US\$30 a share.

Of the five million shares sold, 714,286 were sold by the company and 4,385,714 were sold by shareholders.

Capstone even had the nerve to grant the underwriters an option to purchase up to 750,000 additional shares of common stock to cover over-allotments.

### Overhang of supply

The sad truth is that the deal was cut by 30% at the last minute and there still were not enough buying to hold the stock above the opening bid. And it's far from over. Those foolish enough to subscribe to the secondary are flipping their shares, sending Capstone into the mid-twenties.

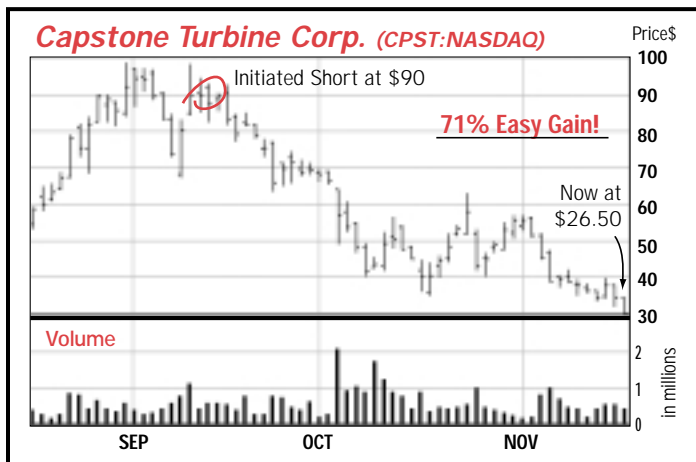
You'd have to be a fool to be long this stock. On the first trading day after Christmas, 64 million additional shares currently held by insiders will become eligible to trade. **This "Flying V" scenario may be enough to send Capstone into the single digits.** I plan to cover sometime before the first of the year.

### The "Flying V" lockup trader

The "Flying V" system works so well that my last picks are four for four already. The *Taipan Traders* among you are familiar with my **Handspring (HAND:NASDAQ)** short.

I recommended that Traders short Handspring above US\$90 a share. The stock immediately dropped to US\$69 before climbing back into the high US\$80s. This set the trend, and the massive daily volume – 25% of the float on average – insured that this would be a volatile position.

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But I had one important piece of information in my favor. Information that the large Wall Street institutions don't want you to know about. I knew that on December 17, 2000, more than 100 million shares held by insiders would become available to trade.

Institutions know this as well, but you won't see it in any research report containing a "strong buy" recommendation. You won't see it during the blitzkrieg of BS following the Comdex convention in Las Vegas.

For those who don't know – Comdex is the yearly Mecca for geeks and analysts who pore over this year's new tech toys and award laurels and high stock valuations to the winners. You might remember that at last year's Comdex, Corel (CORL:NASDAQ) announced they were going into the Linux field. In the following weeks their stock shot from US\$3 to US\$44. Today they are back to US\$3.



### Feel the power

That's the traditional power of Comdex. But not this year. HAND unloaded both barrels of analyst "strong buy" recommendations (from the same companies that took them public, of course) and positive press releases.

Their goal is to hold up the stock long enough for the insiders to get out on Dec. 17, 2000. But it won't work. I'm short and sure. **We're up 28% with more to come.**

### It works long too

But that's not all. Those of you who subscribe to *The Hammer* are already aware of MetaWave (MTWV:NASDAQ) – a company that has found a less expensive method of increasing bandwidth for mobile data transmission using "smart antennas."

MetaWave is a stock that fell from US\$40 to US\$10 over the past few months based on an overabundance of stock. But I believe they have a viable product in an emerging field. This is a speculative stock that could go ten to one if it meets expectations.

And due to the massive selloff, I was able pick it up at a market value of only US\$350 million – or US\$10.50 on the share price. I put a buy out when the stock hit one of my

key TA indicators and it immediately shot up to US\$14.50.

I didn't sell because I believe that in the next two months this share price will be in the US\$20s. As I write this, a second buying opportunity is arising as it comes back and retests its low. If you can buy this stock under US\$10.50 I suggest that you do so.

### ViroLogic rocks

You remember ViroLogic (VLGC:NASDAQ) from last month's *Taipan*. They make tests to evaluate and customize the best treatment combinations for HIV and Hepatitis C patients.

ViroLogic recently announced that they have identified the first-ever clinically relevant HIV drug resistance cut-offs. This new development defines the maximum level of reduced drug susceptibility at which a patient still has a high probability of successful response to treatment. At resistance levels above the cutoff, patients are unlikely to respond to treatment.

ViroLogic's cutoffs were determined by using clinical trial data to evaluate the impact of changes in drug susceptibility on treatment outcomes. Before now, it was difficult to know what level of reduced susceptibility corresponded to decreased treatment success rates.

The upshot is that ViroLogic has a battery of test that work and are in high demand. And due to the recent sell-off in conjunction with a "Flying V" event, you were able to buy this stock at or near its lows. This is a company that grew sales 948% last year.

### The "Flying V" of profits

I'm telling you this because I'm confident that my simple supply-and-demand equation for over-hyped stocks is understandable, can be and has been backtested, and, quite simply, it works.

Included with this month's newsletter you will find detailed information about how you can profit from this system, time and time again. I urge you to check it out.

And pay attention to the mail. Your 100+ page forecast issue is due any day. I hope you and yours have a blissful holiday season.

