The unexpected cost of going public

By Linda Anderson

For many entrepreneurs struggling to secure funding, an initial public offering is the pot of gold at the end of the rainbow. In one swoop financial concerns are cast aside, the fledgling venture can grow into the company it was always meant to be and the young founder becomes a millionaire overnight.

While all this may well be true, research from Shai Bernstein, an assistant professor of finance at the Stanford Graduate School of Business has found that there is a price to pay. Those technology companies that do go public see their innovation slow down and in time they become less daring and less ambitious with their in-house research. In fact Prof Bernstein finds that newly public technology companies become more reliant on outsourcing their technology.

In an analysis of the patent data of almost 2,000 companies Prof Bernstein has discovered that after a technology company goes public it is far more likely that there will be a brain drain with the leading inventors more likely to leave the company. Those that remain show a steep decline in “innovation quality”.

Prof Bernstein compared those companies that completed a public offering with those that began the process but then withdrew their IPO registrations. He discovered that the quality of patents (measured by how often they were cited) declined by 40 per cent over a five-year period after the companies went public. For those companies that remained in private hands the quality of their patents remained the same.

Prof Bernstein suggests one reason for the steep decline in innovation in public companies may be that when companies do go public, their top innovators have often become millionaires overnight and have no incentive to remain at the company. Management incentives may also be different following an IPO, with board members becoming more cautious because they face market pressures and concerns about takeovers.

Does going public affect innovation? can be read at Stanford GSB’s research paper series.

● Advertising is an expensive business. But if companies want to ensure that they are spending their money wisely they could do well to pay attention to research from Thales Teixeira, an assistant professor in the marketing department at Harvard Business School.

Prof Teixeira and colleagues set out to discover if advertisers were striking the right balance when advertising – how much entertainment should be included and how much should be brand promotion?

In partnership with MIT Media Lab and Affectiva – which has developed an online facial tracking system for testing advertising – Prof Teixeira randomly selected 275 people and showed them a sample of 82 advertisements for 30 brands. While they watched the advertisements, webcams using special software tracked every individual’s facial expressions, noting changes – for example, what made them smile or laugh. Measuring these changes then allowed the team to assess what advertisements were perceived to be interesting.

The academic team discovered that while some entertainment was important in securing a viewer’s interest too much entertainment led to a loss of interest and reduced the viewer’s link to the brand.

Viewers do need to associate a brand with fun, Prof Teixeira says, but he warns advertisers that fun is not enough. “You have to show
the brand and then entertain. That’s when the conditioning occurs. The other way around – entertain then brand – doesn’t work as well.”

“Why, when and how much to entertain consumers in advertisements? A web-based facial tracking study” will be published shortly.