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Shades of Yesteryear: PayPal IPO Gains 55%

By Nicholas Johnston

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Two years ago, a young Internet start-up like PayPal Inc., with the backing of blue-chip venture capitalists, a hot technology and more than 12 million users, would have lit up the stock markets on its first day of trading as a public company.

And yesterday PayPal did just that, its stock surging 55 percent from its initial price as investors snapped up shares in the first technology public offering in almost a year.

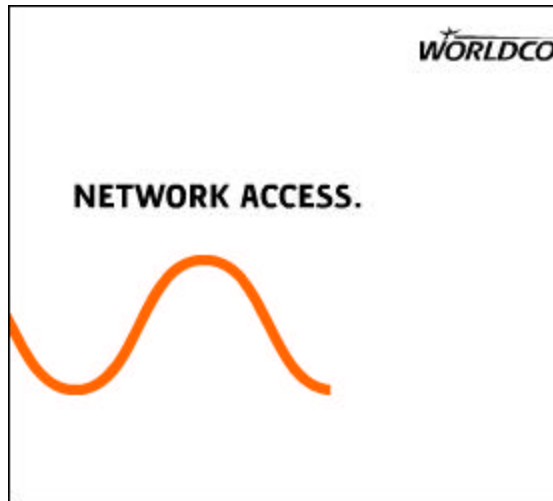
The Palo Alto, Calif., provider of online payment services raised more than \$60 million, giving it a market value of \$1.2 billion. This happened despite accumulating \$264.7 million in losses over the past three years, drawing scrutiny from banking regulators and facing lawsuits that threaten to shutter the firm.

After a dismal 2001 that saw the market for technology-related IPOs all but dry up, investors seemed ready to give the beleaguered high-tech sector another shot. PayPal's strong performance -- it closed yesterday at \$20.09 a share, up \$7.09 from the \$13 price first offered to investors -- opened the possibility of more technology offerings in the coming months.

"I think it's reason to be cautiously optimistic about the IPO market," said Frank Goldstein, corporate finance attorney with Sidley Austin Brown & Wood in the District. "If we get one two more like [this] we can start what I think would be a modest trend for technology companies to go public again."

The \$13 initial share price fell in the middle of the \$12-to-\$14 range set by the offering's underwriters. Trading began at \$15.41, and the stock sold for as much as \$22.44 during a session in which 9 million shares changed hands.

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PayPal's service enables people to send and receive money over the Internet. By using credit cards or bank accounts, members deposit money in their PayPal accounts and can e-mail payments to other PayPal members. Recipients can then either keep the money in their account for future payments or ask PayPal to distribute the money to their bank account or cut a check.

The service has been widely adopted by users of eBay's online auction house, allowing them to pay for items they purchase on the site without having to set up merchant accounts with credit card companies. For providing the service, PayPal charges a transaction fee of around 2.5 percent and a 30-cent surcharge.

In documents filed with the Securities and Exchange Commission, PayPal said a "significant portion" of its business comes from eBay transactions.

PayPal's first attempts at an IPO were delayed last week after a lawsuit, filed Feb. 4 by CertCo Inc., alleged that PayPal's transaction service infringes on a patent held by the New York firm. In the suit, CertCo threatened to file for an injunction that would shut PayPal down. According to documents filed with the SEC, PayPal has filed a counterclaim denying the allegations mentioned in the suit.

Meanwhile, banking regulators in four states have begun taking a closer look at the company, and some have accused PayPal of operating as an unlicensed bank. Louisiana officials ordered the service to suspend operations in the state earlier this month; PayPal succeeded in getting that order temporarily delayed this week.

Officials in California, Idaho and New York have also contacted the firm concerning possible violations of banking regulations.

"Being a new leading-edge technology in the banking area, the regulation is going to lag," says Kyle Huske, a market analyst at IPO.com, a financial news Web site. "That's kind of to be expected."

Officials from PayPal declined to comment.

Since its founding in 1999, PayPal has raised more than \$210 million in venture capital financing from prominent venture backers, including Sequoia Capital, Nokia Ventures and Madison Dearborn Partners. The venture capital community is watching this IPO closely to gauge the market's reaction to a technology offering.

As of Sept. 30 last year, PayPal had \$138.6 million of cash in the bank.

In the past year the company's revenue has sharply increased and losses have declined. In 2000, PayPal lost \$127 million on revenue of \$14.5 million. In the first nine months of 2001, revenue increased to \$64.4 million and, according to some analysts, the company is well on the path to profitability.

"The major draw for this offering was the financial fundamentals," Huske said. "On a cash basis they're actually doing well."

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