Volatile Q4: Are Tech Stock IPOs Too Risky?

Description

It's been quite the time for tech stock IPOs. **Palantir Technologies's** direct listing is the latest hot tech stock to hit the markets, and although its debut wasn't traditional, it was sensational, nonetheless. Palantir stock leaped 50% above its US$7.25 reference price at one point, ending Wednesday up 31%. But the new ticker was negative by 1% the next day. Friday saw the new stock down 3%.

Momentum in new tech stocks is therefore predictable — not only in its wildness, but also in its unreliability. Buying into stocks like Palantir, as well as IPOs such as **Lightspeed**, offers the chance to multiply an investment many times over. But it's not reliable growth. And as the markets become increasingly frothy as we head into Q4, the risk involved could become increasingly unpalatable.

A number of new names have recently debuted, continuing a run of tech offerings hitting the North American stock markets. But are they a buy in a choppy fall? Investors will have to weigh number of factors. TSX investors seeking near-term upside should check their appetite for risk before anything else. Many of the new tech stocks appearing on the markets exhibit extreme volatility, putting investors in the line of danger.

Tech stock growth is never a "sure thing"

One of the most enduring images of early comedy movies was Buster Keaton surviving a wall falling on him. Somehow, the lucky guy was always standing right where the open window happened to be. It's a good analogy for investing. Being that lucky guy in the stock markets is the difference between striking gold and getting completely squished.

Investing isn't exactly gambling, but there's still a lot more left to chance than many shareholders are comfortable with. That's why Dividend Aristocrats are popular. They're predictable and provide years of steady wealth creation.

But a good growth stock will always beat the sturdiest dividend stock. The problem is finding names that offer both a reasonable entry point and a compelling growth thesis. One way to identify suchstocks is to comb hyped-up sectors for reasonably priced up-and-comers.

This strategy gives investors a way to gain exposure to fast-growing industries but at lower cost. Lightspeed is a good example of this, since the e-commerce name provides a lower entry point than the comparable but overvalued **Shopify**.

Look for ground-level events

Aside from near-term capital risk, investors should also check these companies' stories. Does the tech segment of a portfolio already contain similar names? Overexposure to any single industry can critically weaken a portfolio. Some rare exceptions to this rule come from high-volatility growth spaces. Consider the hunt for a coronavirus vaccine, which will see multiple names generate near-term upside in the coming months.

Or consider 5G and the green economy, in particular the electric vehicle market. Both of these high-growth industries can support multiple names. Watch for ground-level entry points in these types of areas. Burgeoning industries allow speculative investors to mix and match among competitors. However, it also means that positions should be reduced to lessen capital risk.

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