An Empirical Analysis of IPO Lockup Expirations

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After an initial public offering, most existing shareholders are subject to a lockup period in which they cannot sell shares for a specified period of time (usually 180 days). These shareholders include inside owners as well as venture capital investors who typically sell all their shares as soon as the lockup period expires. This causes a large increase in the supply of shares and downward pressure on the stock price. Since lockup expirations are completely known and observable, the permanent drop in the stock price may challenge the efficient market hypothesis.

We examine 882 share lockup agreements expiring between 2000 and 2006. Our analysis reveals a permanent increase in average trading volume and a negative abnormal return around the lockup expiration. However, these findings are extremely more dramatic during the 2000-2001 period and much less dramatic for the 2002-2006 period than researchers found in the 1990s. We offer some possible explanations for this, analyze cross-sectional data to determine if the effect is more pronounced upon firms with certain characteristics, suggest why investors should be conscious of lockup expirations, and explore the value of post-venture distribution management.