# Dot-com bubble

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The **dot-com bubble** (also referred to as the **dot-com boom**, the **Internet bubble** and the **information technology bubble**)[1] was a historic speculative bubble covering roughly 1997–2000 (with a climax on March 10, 2000, with the NASDAQ peaking at 5,408.60[2] in intraday trading before closing at 5,048.62) during which stock markets in industrialized nations saw their equity value rise rapidly from growth in the Internet sector and related fields. While the latter part was a boom and bust cycle, the **Internet boom** is sometimes meant to refer to the steady commercial growth of the Internet with the advent of the World Wide Web, as exemplified by the first release of the Mosaic web browser in 1993, and continuing through the 1990s.

The period was marked by the founding (and, in many cases, spectacular failure) of a group of new Internet-based companies commonly referred to as *dot-coms*. Companies could cause their stock prices to increase by simply adding an "e-" prefix to their name or a ".com" to the end, which one author called "prefix investing."[3]

A combination of rapidly increasing stock prices, market confidence that the companies would turn future profits, individual speculation in stocks, and widely available venture capital created an environment in which many investors were willing to overlook traditional metrics, such as P/E ratio, in favor of basing confidence on technological advancements.

The collapse of the bubble took place during 1999–2001. Some companies, such as pets.com, failed completely. Others lost a large portion of their market capitalization but remained stable and profitable, e.g., Cisco, whose stock declined by 86%. Some later recovered and surpassed their dot-com-bubble peaks, e.g., Amazon.com, whose stock went from 107 to 7 dollars per share, but a decade later exceeded 400.[4]

## Contents

# Bubble growth

Due to the rise of commercial growth of the Internet, venture capitalists saw record-setting growth as *dot-com* companies experienced meteoric rises in their stock prices and therefore moved faster and with less caution than usual, choosing to mitigate the risk by starting many contenders and letting the market decide which would succeed. The low interest rates in 1998–99 helped increase the start-up capital amounts. A canonical "dot-com" company's business model relied on harnessing network effects by operating at a sustained net loss and to build market share (or mind share). These companies offered their services or end product for free with the expectation that they could build enough brand awareness to charge profitable rates for their services later. The motto "get big fast" reflected this strategy.

This occurred in industrialized nations due to the increasing lack of digital divide in the late 1990s, and early 2000's. Previously, individuals were less capable of accessing the Internet, many stopped by lack of local access/connectivity to the infrastructure, and/or the failure to understand use for Internet technologies. Absence of infrastructure and lack of understanding are two major obstacles that previously obstructed mass connectivity. For these reasons, individuals had limited capabilities in what they could do and what they could achieve in accessing technology. Increased means of connectivity to the Internet than previously experienced before allowed the ICT (Information Communicative Technology) to progress from a luxury good to a necessity good. As connection grew, so did the potential for venture capitalists to take advantage of the growing field. The functionalism, or impacts of technologies driven from the cost effectiveness of new Internet websites ultimately influenced the demand growth during this time.

# Soaring stocks

In financial markets, a stock market bubble is a self-perpetuating rise or boom in the share prices of stocks of a particular industry; the term may be used with certainty only in retrospect after share prices have crashed. A bubble occurs when speculators note the fast increase in value and decide to buy in anticipation of further rises, rather than because the shares are undervalued. Typically, during a bubble, many companies thus become grossly overvalued. When the bubble "bursts", the share prices fall dramatically, and many companies go out of business. The prices of many non-technology stocks increased in tandem and were also pushed up to unrealistic valuations relative to fundamentals.[5]

American news media, including respected business publications such as *Forbes* and the *Wall Street Journal*, encouraged the public to invest in risky companies, despite many of the companies' disregard for basic financial and even legal principles.[6]

Andrew Smith argued that the financial industry's handling of initial public offerings tended to benefit the banks and initial investors rather than the companies.[7] This is because company staff were typically barred from reselling their shares for a lock-in period of 12 to 18 months, and so did not benefit from the common pattern of a huge short-lived share price spike on the day of the launch. In contrast, the financiers and other initial investors were typically entitled to sell at the peak price, and so could immediately profit from short-term price rises. Smith argues that the high profitability of the IPOs to Wall Street was a significant factor the course of events of the bubble. He writes:

> "But did the kids [the often young dotcom entrepreneurs] dupe the establishment by drawing them into fake companies, or did the establishment dupe the kids by introducing them to Mammon and charging a commission on it?"

In spite of this, however, a few company founders made vast fortunes when their companies were bought out at an early stage in the dot-com stock market bubble. These early successes made the bubble even more buoyant. An unprecedented amount of personal investing occurred during the boom, and the press reported the phenomenon of people quitting their jobs to become full-time day traders.[8][9][10]

# Free spending

According to dot-com theory, an Internet company's survival depended on expanding its customer base as rapidly as possible, even if it produced large annual losses. For instance, Google and Amazon.com did not see any profit in their first years. Amazon was spending to alert people to its existence and expand its customer base, and Google was busy spending to create more powerful machine capacity to serve its expanding search engine. The phrase "Get large or get lost" was the wisdom of the day.[11] At the height of the boom, it was possible for a promising dot-com to make an initial public offering (IPO) of its stock and raise a substantial amount of money even though it had never made a profit—or, in some cases, earned any revenue whatsoever. In such a situation, a company's lifespan was measured by its burn rate: that is, the rate at which a non-profitable company lacking a viable business model ran through its capital.

Public awareness campaigns were one of the ways in which dot-coms sought to expand their customer bases. These included television ads, print ads, and targeting of professional sporting events. Many dot-coms named themselves with onomatopoeic nonsense words that they hoped would be memorable and not easily confused with a competitor. Super Bowl XXXIV in January 2000 featured 16 dot-com companies that each paid over $2 million for a 30-second spot. By contrast, in January 2001, just three dot-coms bought advertising spots during Super Bowl XXXV. In a similar vein, CBS-backed iWon.com gave away $10 million to a lucky contestant on an April 15, 2000 half-hour primetime special that was broadcast on CBS.

Not surprisingly, the "growth over profits" mentality and the aura of "new economy" invincibility led some companies to engage in lavish internal spending, such as elaborate business facilities and luxury vacations for employees. Executives and employees who were paid with stock options instead of cash became instant millionaires when the company made its initial public offering; many invested their new wealth into yet more dot-coms.

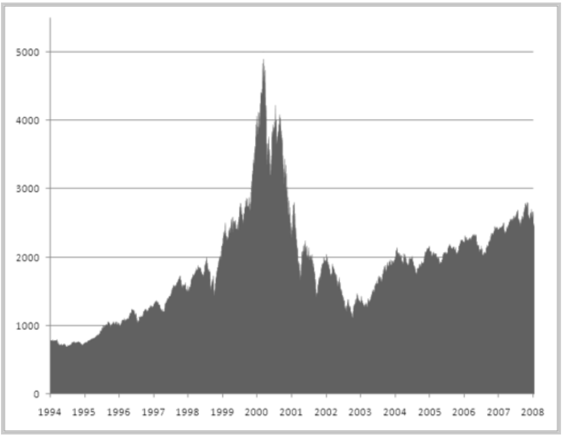
Cities all over the United States sought to become the "next Silicon Valley" by building network-enabled office space to attract Internet entrepreneurs. Communication providers, convinced that the future economy would require ubiquitous broadband access, went deeply into debt to improve their networks with high-speed equipment and fiber optic cables. Companies that produced network equipment like Nortel Networks were irrevocably damaged by such over-extension; Nortel declared bankruptcy in early 2009. Companies like Cisco, which did not have any production facilities, but bought from other manufacturers, were able to leave quickly and actually do well from the situation as the bubble burst and products were sold cheaply.

In the struggle to become a technology hub, many cities and states used tax money to fund technology conference centers, advanced infrastructure, and created favorable business and tax law to encourage development of the dotcom industry in their locale. Virginia's Dulles Technology Corridor is a prime example of this activity. Large quantities of high-speed fiber links were laid, and the State and local governments gave tax exemptions to technology firms. Many of these buildings could be viewed along I-495, after the burst, as vacant office buildings.

Similarly, in Europe the vast amounts of cash the mobile operators spent on 3G licences in Germany, Italy, and the United Kingdom, for example, led them into deep debt. The investments were far out of proportion to both their current and projected cash flow, but this was not publicly acknowledged until as late as 2001 and 2002. Due to the highly networked nature of the IT industry, this quickly led to problems for small companies dependent on contracts from operators. One example is of a then Finnish mobile network company Sonera, which paid huge sums in German broadband auction then dubbed as 3G licenses. Third-generation networks however took years to catch on and Sonera ended up as a part of TeliaSonera, then simply Telia.

# The bubble bursts

Over 1999 and early 2000, the U.S. Federal Reserve increased interest rates six times,.[12] The dot-com bubble burst, numerically, on March 10, 2000, when the technology heavy NASDAQ Composite index peaked at 5,048.62 (intra-day peak 5,408.60), more than double its value just a year before.[13] The NASDAQ fell slightly after that, but this was attributed to correction by most market analysts; the actual reversal and subsequent bear market may have been triggered by the adverse findings of fact in the *United States v. Microsoft* case which was being heard in federal court.[14] The conclusions of law, which declared Microsoft a monopoly, were widely expected in the weeks before their release on April 3.[15] The following day, April 4, the NASDAQ fell from 4,283 points to 3,649 and rebounded back to 4,223. At the time, this represented the most volatile day in the history of the NASDAQ.




The technology-heavy NASDAQ Composite index peaked at 5,048 in March 2000, reflecting the high point of the dot-com bubble.

On March 20, 2000, the NASDAQ had lost more than 10% from its peak. In its cover story "Burning Up" the financial weekly *Barron's* quoted Napster-cofounder Sean Parker: "During the next 12 months, scores of highflying Internet upstarts will have used up all their cash. If they can't scare up any more, they may be in for a savage shakeout. An exclusive survey of the likely losers". The article pointed out that "America's 371 publicly traded Internet companies have grown to the point that they are collectively valued at $1.3 trillion, which amounts to about 8% of the entire U.S. stock market".[16]

By 2001, the bubble was deflating at full speed. A majority of the dot-coms ceased trading after burning through their venture capital, many having never made a profit. Investors often referred to these failed dot-coms as "dot-bombs".[17]

# Aftermath

On January 10, 2000, America Online (now Aol.), a favorite of dot-com investors and pioneer of dial-up Internet access, announced plans to merge with Time Warner, the world's largest media company, in the second-largest M&A transaction worldwide.[18] The transaction has been described as "the worst in history".[19][20] Within two years, boardroom disagreements drove out both of the CEOs who made the deal, and in October 2003 AOL Time Warner dropped "AOL" from its name.

Several communication companies could not weather the financial burden and were forced to file for bankruptcy. One of the more significant players, WorldCom, was found engaging in illegal accounting practices to exaggerate its profits on a yearly basis. WorldCom's stock price fell drastically when this information went public, and it eventually filed the third-largest corporate bankruptcy in U.S. history. Other examples include NorthPoint Communications, Global Crossing, JDS Uniphase, XO Communications, and Covad Communications. Companies such as Nortel, Cisco, and Corning were at a disadvantage because they relied on infrastructure that was never developed which caused the stock of Corning to drop significantly.

Many dot-coms ran out of capital and were acquired or liquidated; the domain names were picked up by old-economy competitors, speculators or cybersquatters. Several companies and their executives were accused or convicted of fraud for misusing shareholders' money, and the U.S. Securities and Exchange Commission fined top investment firms like Citigroup and Merrill Lynch millions of dollars for misleading investors. Various supporting industries, such as advertising and shipping, scaled back their operations as demand for their services fell. A few large dot-com companies, such as Amazon.com, eBay, and Google have become industry-dominating mega-firms.

The stock market crash of 2000–2002 caused the loss of $5 trillion in the market value of companies from March 2000 to October 2002.[21] The 9/11 terrorist destruction of the World Trade Center's Twin Towers, killing almost 700 employees of Cantor-Fitzgerald, accelerated the stock market drop; the NYSE suspended trading for four sessions. When trading resumed, some of it was transacted in temporary new locations.

More in-depth analysis shows that 48% of the dot-coms companies survived through 2004.[22] With this, it is safe to assume that the assets lost from the Stock Market do not directly link to the closing of firms. More importantly, however, it can be concluded that even companies who were categorized as the "small players" were adequate enough to endure the destruction of the financial market during 2000–2002.[22] Additionally, retail investors who felt burned by the burst transitioned their investment portfolios to more cautious positions.

Nevertheless, laid-off technology experts, such as computer programmers, found a glutted job market. University degree programs for computer-related careers saw a noticeable drop in new students. Anecdotes of unemployed programmers going back to school to become accountants or lawyers were common.

Turning to the long-term legacy of the bubble, Fred Wilson, who was a venture capitalist during it, said:

> "A friend of mine has a great line. He says 'Nothing important has ever been built without irrational exuberance'. Meaning that you need some of this mania to cause investors to open up their pocketbooks and finance the building of the railroads or the automobile or aerospace industry or whatever. And in this case, much of the capital invested was lost, but also much of it was invested in a very high throughput backbone for the Internet, and lots of software that works, and databases and server structure. All that stuff has allowed what we have today, which has changed all our lives...that's what all this speculative mania built".[7]

# List of companies significant to the bubble

*For discussion and a list of dot-com companies outside the scope of the dot-com bubble, see dot-com company.*

- Boo.com – spent $188 million in just six months[23] in an attempt to create a global online fashion store that went bankrupt in May 2000.
- Books-a-Million - Saw its stock price soar by over 1000% in one week simply by announcing an updated website on November 25, 1998. The company's share price rose from around $3 previously to an all-time closing high of $38.94 on November 27 and an intra-day high of $47.00 on November 30, before quickly pulling back to around $10 two weeks later. By 2000, the share price had returned to $3.[24][25][26][27]
- Broadcast.com – Acquired by Yahoo! for $5.9 billion in stock, making Mark Cuban a multi-billionaire. The site is now defunct and redirects to Yahoo!'s home page. [1] (http://broadcast.com)
- e.Digital Corporation (EDIG) – Long-term, unprofitable OTCBB-traded company founded in 1988 previously named Norris Communications. Changed its name to e.Digital in January 1999 when stock was at $0.06 level. The stock rose rapidly in 1999 and went from closing price of $2.91 on December 31, 1999, to intraday high of $24.50 on January 24, 2000. It quickly retraced and has traded between $0.07 and $0.165 in 2010.[28] As of 2013, the stock continues to trade low, ranging between $0.12 and $0.19 a share[29]
- Freeinternet.com – Filed for bankruptcy in October 2000, soon after canceling its initial public offering. At the time Freeinternet.com was the fifth-largest ISP in the United States, with 3.2 million users.[30] Famous for its mascot Baby Bob, the company lost $19 million in 1999 on revenues of less than $1 million[31][32]
- GeoCities – Purchased by Yahoo! for $3.57 billion in January 1999.[33] Yahoo! closed GeoCities on October 26, 2009[34]
- theGlobe.com – Social networking service, that went live in April 1995 and made headlines by going public on November 1998 and posting the largest first day gain of any IPO in history up to that date. The CEO became in 1999 a visible symbol of the excesses of dot-com millionaires
- GovWorks.com – Doomed dot-com featured in the documentary film *Startup.com*
- inktomi – Valuation of $25 billion in March 2000
- InfoSpace – In March 2000 this stock reached a price $1,305 per share, but by April 2001 the price had crashed down to $22 a share[35]
- Kozmo.com – offered one-hour local delivery of a number of retail items, from March 1998 to April 2001
- Lastminute.com – IPO in the UK coincided with the bursting of the bubble
- The Learning Company, bought by Mattel in 1999 for $3.5 billion, sold for $27.3 million in 2000[36]

- Lycos – Purchased by Spanish telecommunications provider Telefónica for $12.5 billion in 2000[37] to expand its Terra Networks online platform. It was sold in 2004 to Seoul, South Korea-based Daum Communications Corporation for $95.4 million in cash, less than 2% of Terra's initial multi-billion dollar investment.[38]
- MicroStrategy – Shares lost more than half their value on March 20, 2000, following their announcement of re-stated financials for the previous two years. A *BusinessWeek* editorial said at the time, "The company's misfortune is a wake-up call to all dot-com investors. The message: It's time, at last, to pay attention to the numbers".[39]
- Open.com – Was a big software security producer, reseller, and distributor, declared in bankruptcy in 2001
- Pets.com – Former dot-com enterprise that sold pet supplies to retail customers before entering bankruptcy in 2000
- Pixelon – Internet streaming video company that hosted a $16 million launch party in 1999 hosting celebrities such as The Who and the Dixie Chicks. Failed less than a year later when it became apparent that its technologies were fraudulent or misrepresented[40]
- Startups.com – "Ultimate dot-com startup" that went out of business in 2002
- Think Tools AG – One of the most extreme symptoms of the bubble in Europe: market valuation of CHF 2.5 billion in March 2000, no prospects of having a substantial product (investor deception), followed by a collapse[41]
- Tiscali – Important Italian telecommunications company whose share price grew from €46 (IPO in November 1999) to €1,197 in four months. They fell to €40 afterwards in less than two months and have continued plummeting to well under 0.2 euros.[42]
- VA Linux - A provider of built-to-order Intel systems based on Linux and other open source projects. They set the record for largest first-day IPO price gain; after the price was set at $30/share, it ended the first day of trading at $239.25/share, a 698% gain (9 December 1999). After that, its stock declined consistently. After several business transitions it became Geeknet. It provides the backdrop of the documentary Revolution OS.
- Webvan, Online grocer that operated on a "credit and delivery" system; the original company went bankrupt in 2001. It was later resurrected by Amazon.com
- WorldCom, a long-distance telephone and internet-services provider that became notorious for using fraudulent accounting practices to increase their stock price. The company filed for bankruptcy in 2002 and former CEO Bernard Ebbers was convicted of fraud and conspiracy.
- Xcelera.com – Swedish investor in start-up technology firms that was one of the[43] "greatest one-year rise of any exchange-listed stock in the history of Wall Street"[44]

# See also

## Terminology

- Dark fiber
- Digital Revolution
- E-commerce
- E-learning
- The Long Tail
- Techno-utopianism
- Technology hype
- Web 2.0

### Media

- e-Dreams
- ebay.com
- SatireWire

### Culture

- Dot com party
- Dot-com commercials during Super Bowl XXXIV
- 2000 Webby Awards

### Venture capital

- List of venture capital firms

### Economic downturn

- Financial crisis of 2007-2010
- Subprime mortgage crisis
- United States housing bubble

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# External links

- Top 10 dot-com flops (http://www.cnet.com/4520-11136_1-6278387-1.html?tag=cnetfd.sd) – CNet's list of ten most notable failed dot-com companies
- Startup Dot Com Movie (http://www.imdb.com/title/tt0256408/) – documentary of a failing company.
- Warren Buffett: 'I told you so' (http://news.bbc.co.uk/2/hi/business/1217716.stm) – BBC article, 13 March 2001.
- Time Flies Dept.: Dot-com craze peaked 10 years ago (http://www.networkworld.com/community/node/58280)

| 2000s economic history | E-commerce | Economic bubbles | Economic disasters in the United States
| History of the Internet | History of the United States (1991–present)
| Information technology management | Internet terminology | Online companies
| Stock market crashes

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