Bullish on India: IPOs become attractive exit option again as tech stocks soar

The recent bull run is significant because it follows a long bearish period when public shareholders questioned the profitability of these companies. The improved financial performance of tech companies is now forcing other new entrants to focus on better financials before approaching the market.

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While valuations of tech companies in India have come under fire, investors are extremely bullish on the country

The improved financial performance of new-age tech companies, which led to a surge in their stock prices, has boosted the confidence of private equity and venture capital investors in the prospects of successful exits through public listings.

Zomato achieved its first-ever quarterly profit after tax, while companies like Delhivery, PB Fintech (Policybazaar), and One97 Communications (Paytm), notably reduced losses in the June quarter. As a result, the stock prices of these firms have surged by anywhere between 26-61 percent this year as public shareholders acknowledged their improved financial performance, giving some of their investors, like SoftBank, handsome returns.

Take a look at this. SoftBank, a common investor in the four companies mentioned above (Zomato through Blinkit) is alone sitting on gains of close to $550 million in the first six months of 2023. Paytm, in fact, also turned into a breakeven investment for SoftBank for the first time since its listing, *Moneycontrol* reported in July.

With Paytm's share price rising even further, it will turn into a profitable bet for the Japanese investor.

IdeaForge, meanwhile, a VC-backed drone manufacturer, saw a blockbuster debut on the Indian bourses. The company, which also counts Infosys as a backer, saw its stock listing at a premium of over 90 percent, giving its investors robust returns, which further instilled confidence among a slew of start-up investors. Ideaforge is a profitable start-up and in FY23, the company saw its revenue rising close to 16 percent to Rs 186 crore. Its profit meanwhile was about Rs 32 crore for the period.

The bull run is significant because it follows a long bearish period when public shareholders questioned the profitability of these companies, which raised concerns about the acceptance of high-growth tech firms on India's stock exchanges.

"Public markets in our country are mature and deeply value fundamentals. They value real growth along with profitability. When a company delivers on the above promise, they are rewarded by the Indian public markets and vice versa," said Navjot Kaur, Associate Director at Epiq Capital, a VC which has backed Lenskart, among other late-stage startups.

"As private investors we believe that if a company can deliver on fundamentals, they will continue to perform well in public markets, which in turn is a path to liquidity for venture capital investors," she added.

Getting IPO ready

The bull run has also prompted late-stage companies considering IPOs (initial public offerings) in the near-term to focus more on their financials.

For instance, Meesho, another SoftBank-backed unicorn, had initially expressed interest to go public in FY24 (2023-24), the current financial year. But the company pushed back the plan. Meesho has reduced its monthly burn significantly over the past year and in fact, in July, it turned profitable, but its profit after tax (PAT) number was in low single digits, *Moneycontrol* had reported earlier.

"While we hit the profitability goal earlier than our expectations, we still want to have a long enough track record of profitability before we go to the public markets," Dhiresh Bansal, CFO, Meesho told *Moneycontrol*.

"From a scale and growth perspective, today we are in a position where we could decide to go public but we want to be profitable for a reasonable period of time and grow simultaneously, before testing the public markets. For us that period could be 12-18 months or so, but then it is also a question of how the public markets behave at that point in time," he added.

It is not just Meesho, SoftBank is readying another four of its portfolio companies—Of Business, Swiggy, Firstcry and Lenskart-- for IPOs "very soon," Navneet Govil, managing partner and CFO of SoftBank Vision Fund told The Economic Times newspaper in an interview last week.

"We are seeing a promising pipeline of potential IPO candidates in the tech space. The pause in Tech IPOs has given a very good opportunity for the founders to focus on building businesses and undertake cap table clean-up. Apart from the market timing, the companies are also building towards certain financial milestones and more predictable revenue and earnings. We expect a large number of Tech IPOs in India in the latter half of 2024 and 2025," said Varun Gupta, Managing Director, Digital & Technology Investment Banking, Avendus Capital.

"The recent slowdown in fund-raising has also pushed companies to put a lot more focus on economics and profitability," Gupta added.

Already, Honasa Consumer Ltd, the parent company of Mamaearth, has got approval from India's market regulator for its IPO. Honasa Consumer had filed IPO papers with Sebi in December last year.

"Overall the environment has turned far more positive over the last six months with stronger FPI inflows and improved performance by companies," Ghazal Alagh, co-founder, Mamaearth, told *Moneycontrol*.
"I am certain we'll see more start-ups coming in with IPOs, the current fundraising environment has led to companies becoming more efficient and delivering plans ahead of time. Companies will need to continue and focus on strong governance, profitability and predictable business delivery to be rewarded during such times," Alagh added.

Meanwhile, Ola Electric is looking to list early next year and has appointed investment banks Goldman Sachs and Kotak for the same, *Moneycontrol* had reported exclusively in May.

Startups have also started acknowledging the need to improve certain compliance and governance-related practices like appointing experts as top managers, especially following a series of lapses that came to the fore over the past 15 months.

For instance, cloud-kitchen startup Curefoods hired Mallika T Lakshmanan as head of finance to test the IPO waters. Lakshmanan was earlier CFO at Sapphire Foods India, a listed entity, which operates KFC, Pizza Hut and Taco Bell in India.

"The idea is to start behaving like a listed company, including compliances, closing accounting books within 2-3 days after the end of month. A public listed startup should have very strong controls and processes in place because they need to be showing a consistent improvement in financial performance quarter after quarter after being listed," Ankit Nagori, founder, Curefoods told *Moneycontrol*.

Valuations a hurdle

As tech companies prepare for potential listings on the public market and actively work towards that, investors believe that valuations could remain a challenge. Companies might need to adjust their pricing or accelerate their growth to reach valuations that justify a premium compared to their prices in the private market.

"The previous start-up IPOs had inflated valuations and thought of retail investors as the greater fools. If start-ups do not repeat that ideology and their valuations are correct, allowing some room for retail investors to also make money, start-up IPOs should do well," said Devina Mehra, Chairperson and Managing Director, First Global.

Already, in the recent past, US-based asset management companies (AMCs) have marked down the fair values of a number of unicorns including Swiggy, Byju's, Meesho, Eruditus, and Pine Labs among others. In some cases like for Byju's and Swiggy, these AMCs have marked down the valuations by more than half. PharmEasy, meanwhile, has been involved in discussions with prospective investors to raise fresh funds at a fraction of its last private market valuation. If the company goes ahead with the funding, it will be one of the biggest down rounds in India – from $5.6 billion to $730 million.

Valuations have also come under fire with a few investors raising concerns over the actual market size of India. SoftBank's Rajeev Misra, in an interview with Moneycontrol in July, had said that he felt India's market was "definitely" overestimated. Even PhonePe's founder Sameer Nigam, Zerodha's Nithin Kamath, and Cuemath's Manan Khurma corroborated the sentiment. But all of them were bullish on the country in the long-term.

"When public markets are corrected, private markets too get corrected. In that sense, late stage companies also experience a value correction which is important for both late stage investors and also the companies, to prepare them better for the public markets, for those who are planning an IPO," Kaur of Epia Capital said.

India: a long-term story

While valuations of tech companies in India have come under fire, investors are extremely bullish on the country, and some recent developments highlight this. Sample this. PhonePe, India's most-valued fintech start-up, moved its domicile from Singapore to India. Sameer Nigam, its Co-founder and CEO also said that the company would be listing in India.

“We are a Made in India company. Every office, data centre, and employee of ours is here. There is no reason why we should not contribute to wealth creation in this market," he had said in an episode of CNN News18’s Bits to Billions.

PhonePe also paid close to $1 billion in tax for shifting its base to India.

Just as PhonePe, Razorpay, India’s second-most valued fintech start-up, backed by marquee investors like Peak XV Partners (formerly Sequoia Capital India) and Y Combinator, has also begun the process to move its parent entity to India from the US, ahead of its plans to list in the Indian bourses. Another media report said that Groww, another fintech unicorn, was looking to shift its domicile.

“The recent wave of companies flipping their domicile to India is an indication of the rising stock of Indian capital markets for Tech IPOs,” said Gupta of Avendus.

Corroborating Gupta, Devina Mehra of First Global said that she remains bullish on Indian equities primarily because they have underperformed for the past decade or so and still have more legs to run.

“India had a very long period of underperformance from 2010 to 2020 because during that decade, the equity market only compounded 8.5 percent as against a long-term average of around 15 percent,” Mehra said.