Tech startups such as Zomato and Paytm unlikely to become the next HDFC Bank or TCS after IPOs, says Shankar Sharma

Shankar Sharma on Zomato IPO: Globally, if you look at Grubhub, which is a similar company to Zomato, that also didn't do well at all in the post-listing aftermarket. Typically overhyped IPOs don't do too well in the aftermarket, and Burger King was a good example

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Shankar Sharma, co-founder and vice chairman of First Global, said companies like HDFC Bank and Tata Consultancy Services have been built over decades of sensible management, not by burning cash.

In an interview with Moneycontrol's Kshitij Anand, Sharma said overhyped IPOs typically don't do too well after listing.

Edited excerpts:

Q) Retail frenzy, FOMO, TINA? Or is there any other abbreviation you want to give to the price action we are seeing with respect to Zomato? What is driving the frenzy? We saw a similar story with Burger King – it is down in double digits from its high.

A) Yes, and you're absolutely right. I am an old type in this IPO game. I do understand that IPOs of this kind and this nature usually come in at a time when there is very easily liquidity in the markets and people are flush with easy profits of the secondary markets and that's the right time to hit people with large-size IPOs, which is exactly the right thing to do from Zomato's perspective.

I think they are right on their money in terms of launching their IPO and so is Paytm, for that matter. This is absolutely the best time for them. Now, whether this is the best time for investors or not is a different question. What may be right for the company may or may not be right for the investors.

And, when you look at a stock like Zomato, which is a concept stock because it is still a loss-making company, Indian markets typically are quite stringent about profitability and India does not have a great history of rewarding companies that make losses and Burger King makes losses, which is why the stock has not done well.

The retail frenzy is because Zomato has touched people's lives in the last 12 months. So there is sort of familiarity with the name and to that extent, people want to participate with whatever money they have to buy a piece of it. How that works out will be a very, very interesting question.

Q) You are a market veteran and invest in companies across the globe. Zomato is nothing new for you and we have peers with similar businesses across the globe which are more matured. So why did you not invest in Zomato when the who's who of the financial world is investing?

A) Yeah, sure, one cannot accuse institutional investors of always being very intelligent. In fact, I have always believed that they're less intelligent than many retail investors.

They are basically largely momentum players and most investors just put in money because they have the fear that if their competitor has put in money and the stock goes up, then their NAVs will not look that good. So it just becomes simply a game of trying to match your neighbour rather than intrinsically look at something and say, 'No, I don't like this, I don't want to participate.' Very few fund managers that I know have that kind of analytical bent of mind and the skill to stay out of a party.

Reliance Power attracted a billions of dollars of bids and we know how that panned out. I'm not saying Zomato goes that way. All I'm saying is let's not accuse institutional investors of great wisdom – I think that will be a big mistake.

I think it's just simply a matter of competitive frenzy and you don't want to be left out despite the data showing that typically overhyped IPOs don't do too well in the aftermarket, and Burger King was a good example.

Globally, if you look at Grubhub, which is a similar company to Zomato, that didn't do well at all in the post-listing aftermarket. Uber is not the same business, but it has had Uber Eats and it is still a new-age startup company, which listed, it has been a total dog. Lyft has seen a disappointing listing.

If you look at DoorDash, that has been a very tepid listing. DoorDash is similar to Zomato. So if you look at global comparables, those listings have been extremely disappointing for overhyped startup companies.

The other thing is those valuations have been far lower than Zomato also, one very important thing to keep in mind this time.

Q) When a dividend yield fund invests in the Zomato IPO, what would you call that – momentum investing or fundamental investing?

A) What do you think one should call that? This is just, in Hindi which we call, bhedchal investing. There is no logic. I can understand a normal fund that says okay, I will put x percentage, maybe half percent, of my fund into a momentum period, that is fine.

But a dividend yield fund putting money into it is really unpardonable. I mean you're going against the broad mandate around which you have raised your money.

I do understand there will be pockets available to you even in that fund to put money into non-dividend paying companies, but a dividend fund should at least have a profitable company – whether it pays dividends or not is another matter. But a loss-making company which will probably never pay dividends for the foreseeable future, to put money into that is a bit of a stretch.

Q) In H2 of 2021 there will be a flurry of companies to hit D-Street such as Policybazaar, Paytm, Ola and many more. Can these turn out to be the next TCS or HDFC Bank of D-Street?

A) I really doubt it. Those companies have been built on self-generating cashflows – very, very, very important – not on businesses that have burned through a lot of cash.

The history of such companies… very, very few of them actually delivered in the listed market because the rules for listed markets are very different, completely rather different, like night and day. No listed company can burn cash the way an unlisted company can. And the problem is unless you burn cash – because your business models are basically trying to sell below cost of production – if you stop burning cash, your top line stops growing – that is the biggest challenge. TCS and HDFC Bank never burned cash, not even one day. They were profitable from the very first day. And, they have built it over decades of sensible management, not through burning cash.

There will be a place for such companies – there is no doubt. India should encourage startup listings, and I've said this many, many times. But to say that they'll become TCSes of the world, I think we should be careful about that.

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