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umir Chadha has been literally going up the investing curve. Kicking off his investing career with Goldman Sachs, the capitalist in him quit that highly lucrative and cushy job to co-found his own India-focused venture fund called WestBridge Capital in 2000. Chadha and his partners grew the fund before it merged with Sequoia Capital in 2006. In early 2011 he spun off from Sequoia to reboot WestBridge but this time with a bigger canvas in mind. Having been there, done that in venture investing, if there was one notable takeaway for Chadha, it was that as a startup you got to play for scale. Taking that lesson to heart, Chadha took the conscious choice to deep-dive into the bigger public market instead of ventures in the private space. WestBridge now manages about \$1.5 billion, and has created an enviable mid-cap investing track record. Interestingly, despite having cut his teeth in technology and being based in Silicon Valley, Chadha is averse to investing in tech for reasons he explains to us when we meet him at his office at 400 South, the tallest building in San Mateo.

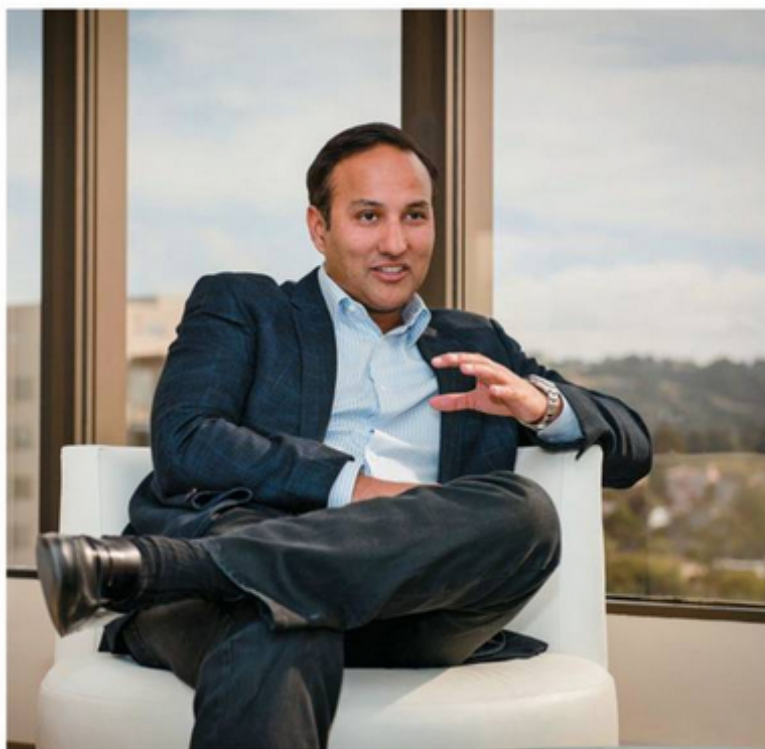
>>> After moving out of Sequoia Capital, you rebooted WestBridge in 2011. At that point of time, one of the things you mentioned was that the PIPE [private investment in public equity] opportunity seemed to be quite bigger. Was it driven by the market condition then or was the underlying thought different?

It was driven by a couple of things. First and foremost, in investing you also want to focus on a big market. India has a huge number of listed companies — over 4,000 — which means there is a massive opportunity to find good stocks. In other countries you don't find this — in Brazil, there may be 500 listed companies, in Indonesia, it's a couple of hundred. In India, for historical reasons, it is easy to get listed and we don't have Sarbanes-Oxley and all that stuff that inhibits promoters from coming to the public market, like in the US.

We like to focus on high quality mid-caps and there are a lot of them in India. Second, the Indian market is highly volatile. So, if you are a patient long-term investor, it actually works to your advantage. Because when things get depressed, they get so depressed that there arises a great opportunity to buy. And when they get euphoric, they get so euphoric and that is a good time to sell. Third, even though most people think of us as a public investor, our philosophy is that we want a shareholding in India's best mid-sized companies. Whether they are public or private is secondary. But we do think there are a lot more public companies in India of scale than there are private companies. So, in the past four years since we started this new fund, our portfolio is 90% public and 10% private.

>>> How do you say the public market in India is deep when of the 4,000-odd listed companies, only about 1,500 stocks are traded regularly?

We love stocks that are not actively traded as they tend to be mispriced. We usually buy a chunk, typically 5-25%, in a listed entity with a long-term view of the promoter and the company. So, for us, the entire listed universe matters. For example, four years back, we had bought shares of Astral Poly Technik. When we bought a 12% stake in the company, it had a ₹300 crore market cap and was hardly traded. Today, it has a ₹5,000 crore market cap. We sold half of our stake last year with a fantastic gain. By the way, that listed universe of 4,000 stocks is growing as there were no new issues for three years. Our expectation is that this year we will see 50-60 more



**“ The Indian listed universe of 4,000 stocks is growing as there were no new issues for three years**

companies getting listed. It is a naturally growing number as more companies get listed as the economy grows.

>>> What is long term for you?

Long term can be very long or short depending upon the situation. But, generally, we take a five-to 10-year view. The way our current fund works is that, unlike a private equity fund, it is an ever growing fund. So, in many cases, we may end up hold something for 20 or 30 years. Some of our companies we may never sell. So, our fund is designed to be a little bit more like the wealthy families in India, where if you are investing your own money, just leave it there, you don't have to sell. But sometimes, we may sell very quickly if a stock runs up a lot in a very short period. We sell because in a public market there is always the opportunity to buy it cheaper. Hence, unlike a PE fund, we enjoy a lot more flexibility and that is a huge advantage.

**>>> Is that due to the profile of your investors?**

It is the profile of the investors but also owing to the structure of the fund. Private equity funds are raised with fixed time periods. Basically at the end of ten years you have to exit everything. At best, a company, which you may want to hold for another five years, can be extended by a year or two, but beyond that you have to sell everything. Our structure, when it makes sense, allows us to hold some of the best investments for long.

**>>> What do you look for in companies?**

We look for high quality franchisee businesses that can generate superior return on capital over the long term. For us, that means companies with unfair advantages. Typically, we look for a very strong brand with a great reputation, a very strong distribution network, the type of things that make it very hard for a competitor to come in and eat their lunch. Take the case of Astral, one of the things we loved about it was that when we spoke to plumbers in India — our team went and spoke to 1,000 plumbers across the country — they said they loved Astral. Because over a decade Astral has gone out and reached out to them, built the brand and these are the decision makers. So, when we get the pipes replaced in our house, none of us know which pipe is going inside our house, except for the plumber. So, Astral built this very powerful brand in India. That is why they were able to grow 40% a year for eight years in a row. They could scale the business beautifully. It is very hard for a competitor to come tomorrow and change all these plumbers' minds. Because over many years they have built a lot of comfort with the brand, it is reliable and very high quality. If a company has a long term competitive advantage like that, it can win in the market place and make money for our investors.

**>>> While you are comfortable with the illiquidity risk, how do you deal with promoter risk because in mid- and small-caps there is always the risk of siphoning off money, related party transactions, and so forth? How do you make that call?**

Of the 4,000 companies, we have invested only in 25 companies and, of them, only 12 really matter. We get to say "no" a lot. There is no pressure to invest because

we have a very concentrated portfolio, a really small number of high quality companies. Our top 12 companies account for about 75% of our asset value. So, we don't hold a huge number of investments. We are not afraid to put a lot of money into these companies because we believe in them. Or, if we don't believe in them we don't invest. We are not like a mutual fund in India that will typically own 80 stocks in the portfolio. We find that a riskier approach. We don't want 80. We want the top 10 or 15, so we are really choosy.

In India, over the past 16 years we have invested in 200 companies. We invested in many of the companies when they were small and we were on the board. Now they are listed. We know either the promoters or the board members pretty well from many years. Also, before investing, we do the usual things: a background check, send an investigative firm to check on various

things, and our own calls or references. We spend a lot of time with them, and we either get comfortable or we don't. Any whiff of promoter risk and we walk away.

**“ We look for a strong brand with a great reputation, a strong distribution network, the type of things that make it hard for a competitor to come in and eat their lunch**

**>>> Can you give an example of a company, without naming it, which was a great opportunity but failed to pass muster?** There are so many of them. There was this financial services company that had a very weak audit firm. There were all these rumours about the numbers being fudged. We told the promoter that their stock was trading at

a deep discount. We advised the promoter to change the auditor, hire top-notch professionals, rope in people with credibility on the board and then watch how the stock price goes up dramatically. When you own 60% of the company, why wouldn't you want that to happen? But the promoter wouldn't listen to us. That was a clear giveaway. Sometimes it can happen that some promoters don't understand how investors look at things, but if someone doesn't want to double their wealth by just changing an auditor, there is a very good reason for it. They don't want to change the auditor because they are obviously cooking the books and the auditors are signing off on all kinds of stuff.

**>>> Is there some overarching theme in your portfolio?**

The overarching theme is to invest in companies with long-term competitive and unfair advantages that are very hard to replicate. That is a basic theme and cuts



## “ The overarching theme in our portfolio is to invest in companies with long-term and unfair advantages

across industries. So, we look for some edge. So for example, let's look at Mayur Uniquoters. We love Mayur because it is a clear market leader in artificial leather in India. They have the unfair advantage of having a very successful innovation engine that constantly designs new patterns and materials. Because of that Mayur charges a premium to its customers. It has also done fantastically on operational efficiency. The company runs its artificial leather lines 24 hours a day, seven days a week. In short, the company sweats its assets, runs very efficiently and keeps costs really low.

When you talk to Mayur's customers, you know it has a fantastic reputation. The customers just say, "Look, if you want the best quality in India, it is Mayur. You will get consistent quality of supply, and on-time delivery." That combination of being innovative and superior execution is something that gives Mayur an unfair advantage.

**>>> You have a lot of investments in building materials. Does the current slowdown in real estate worry you?** I think the thing that is not well understood is that companies such as Kajaria Ceramics, Cera

Sanitaryware and the likes were growing 20-40% a year when the slowdown was worse about three years ago. The reason they grew so fast even in those bad years was, firstly, most of them have a bigger focus on residential than commercial. Residential continues to grow well. But within residential, around 60% is driven by replacement demand. So, even if there is a slowdown every 10 years, you will change your tiles. So, that doesn't really change. Secondly, what is not well understood is that these sectors have huge amounts of unorganised players. But they are slowly going out of business because even though they avoid paying tax, what is happening is that their quality is poor, they have no brand and no distribution, and so people are saying, "Look, I'll pay 3-4% more but I want peace of mind so I'll buy good quality stuff." So, companies that have built very strong brands such as Kajaria and Cera have a huge replacement demand that is not affected by slowdown and there is this unorganised sector whose market share they are eating away. Kajaria is still growing at 20% a year, Cera too has grown at 20% this year. In our view, they will continue to grow at healthy rates even if the real estate market is down.

### **>>> What is your exit strategy?**

If prices turn too steep, we cash out. We sold quite a lot of stuff, million dollars worth of stocks, in the past three quarters. So, we have exited quite a bit. If things keep going up we will keep exiting. In mid-caps, in a bear market there are no buyers and that is good because we are the buyers who get these stocks at a discount. In a bull market, there are plenty of takers. You should see how many calls we get for many of our companies saying, "Please, can you give me a block stake!" For a typical structure, take Mayur as an example. The company's promoter owns over 70% of the company and we own 10%. We have the largest non-promoter holding and then there all these small retail shareholders. The promoter is never going to sell, so anyone who wants to own something substantial will come to us. Half the time we are saying 'no', but in the past three quarters, we sold quite a lot.

But then, we sell only in a good market. If it is a bad market, we will not sell. So, when the market was really bad in 2011, 2012 and 2013 we invested heavily and we sold nothing. Then last year the

## Consumption play

*WestBridge has loaded up on building materials*

	Mcap (₹ cr)	Holding (in %)	Holding (₹ cr)
SKS Microfinance	6,820	2.76	188
Kajaria Ceramics	5,918	7.41	438
La Opala RG	3,152	4.53	143
Greenply Industries	2,240	3.02	68
Mayur Uniquoters	2,038	6.42	131
Greenlam Industries	902	3.01	27
DFM Foods	538	14.95	80

Note: Holding value as on August 18 and shareholding as of June 2015; Other holdings through participatory notes and less than 1% not included

market became good and we started selling, but very selectively. We look at volatility as our friend. Say tomorrow there is a sharp market downturn, we would love it. We have a lot of uncalled capital and cash. We would just start buying in our own names. When things get too hot we start exiting, if things get cold we use that as an opportunity to buy a lot. That is how we manage our own risk.

**>>> Are you sitting on a lot of cash now?**

We are not sitting on a very high cash level now because our portfolio has done really well. We look at cash divided by the value of our stock. So, the denominator is really large. While the market has done really well, the companies have done exceedingly well. So, we

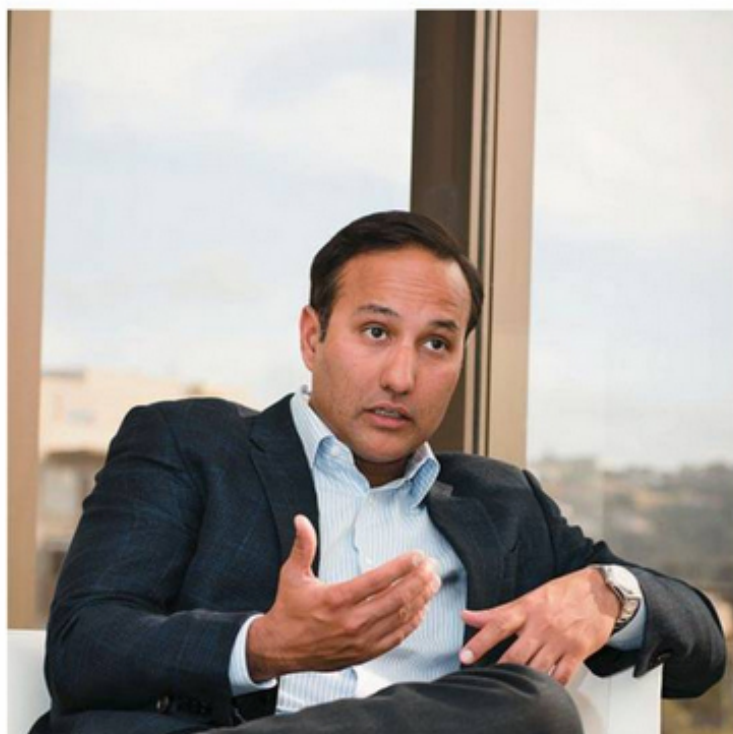
have been really well rewarded in that. But we have a lot of uncalled capital, which we can avail of if we want to buy more.

**>>> Is all of it in the public market or you have some unlisted ventures?**

It is 90% public and 10% private. Three years back, we had invested \$35 million in Dr Lal PathLabs and we are now about to take the company public. It is a very exciting investment. We also invested in a company in Bengaluru called Vistaar Financial Services, which is India's leading lender to micro SMEs. It lends to small dairy farmers and others that no one lends to. Vistaar has grown wonderfully. We are also the largest holder in Chennai-based Aptus Value Housing Finance, which lends small ticket mortgages that the HDFCs of the world don't focus on. It is informal sector lending. So, we have three private companies in the portfolio that we are very positive on.

**>>> You are sitting here in Silicon Valley, and you don't have any investment in the technology space. Why?**

**“ When things get hot we start exiting, if things get cold we buy a lot. That is how we manage risk**



The technology sector is rapidly changing. It makes it hard to invest in the sector. Our current fund has very little tech for that reason. It is the reason a lot of public investors shy away from technology because they say, “Look, there is a lot of money to be made but it is also very risky.” A company can suddenly lose its edge very fast. But plumbers will not forget the Astral brand very easily. Success can be quite short-lived in technology. But when it creates value it is incredible.

**>>> Besides Astral, which are the other companies in your portfolio that you are most excited about?**

There are quite a few. We have a lovely little company called V-Mart, which is a fantastic retailer in India serving tier 2 and 3 towns selling low-cost apparel. I was in Haridwar last summer for personal reasons. Then I went to visit the V-Mart store there. The store was packed. It was a better shopping

experience than other stores. They have air conditioning. They have prices on everything, so no negotiating. They have changing rooms for women. If you are buying on the street, you can't try something on. They have very low prices. Literally, their prices will compete with the street vendor because they cut out a lot of the middlemen in the distribution chain. We own a big chunk of the company. Another lovely company we own is La Opala, India's leading crockeryware maker. But we love that market because what is happening is that in India we are shifting from steel to opalware because now we have microwaves. La Opala has built a fantastic brand in that segment. It's a beautiful consumer company. We bought it at a very low valuation a few years ago.

Many of the companies that we invest in, no one finds them interesting. The nice thing about Mayur is that the money we put into the company is going to result in a new polyurethane (PU) plant. Today, India imports PU from China. We have this very good promoter in Jaipur who needed our money to build a PU plant. We gave him \$12 million and now next year the spanking new plant will be ready. It is pretty exciting. Similarly, Kajaria Ceramics, the country's largest ceramics player, is building a massive tile plant — the biggest that India has ever seen. The power of capital is that it helps transform a company. We like being in the public market and investing in these companies because they do wonderful things with our capital such as entering new markets, creating new products, and expanding. That is what the country needs.

**>>> Which are your biggest wins and what made them happen?**

There have been many. But it is never about me. It is we. We operate one firm. Everything is team work. We have team-oriented process. Hence, we have had many successes. But the one that I am proud of, even though it is an industry that went through a pincer, is SKS Microfinance. We bought a huge chunk in SKS very early on — a 25% stake

for \$8 million in 2006. The company went public at a huge valuation. We were the biggest sellers in the IPO and took out \$100 million. Subsequently, a crisis hit the company and the stock tanked 90%. Most investors sold and ran for cover. We hung on. The company was about to go under, it needed capital. It raised money through a preferential allotment and we were the only existing shareholder to buy the shares. So, we supported the company in its tough times and we got well rewarded for that support. The company is making a massive difference and is scaling up very nicely. It has gone through a very lean period and has emerged incredibly strong over the past three years. That is a company that today lends to about five million women across India. One very simple way to look at it is that SKS lends to about 2% of Indian households. Just one single entity does that

and that has a phenomenal impact. I think it's a great company and will turnaround very nicely.

**“ We like being in the public market because these companies do wonderful things with our capital such as entering new markets, creating new products, and expanding**

**>>> Given that you have worked with several entrepreneurs in India, do you see any commonality? Any common risk factors, that you perceive, in particular?** Indian entrepreneurs are among the best globally because the truth is that it is so difficult to build a company in India. Being an Indian entrepreneur is like being an Ethiopian runner. The

Ethiopian runners are really fast as their countries are very high above sea level, so there is very low oxygen. They are used to running on very low oxygen. That is one of the reasons Ethiopians are one of the world's best runners. When they come to sea level and they are running they are killing everyone else because suddenly for them it is like running down. It is easy. In the same way, Indian entrepreneurs are used to such tough conditions in running a business. Every distributor is trying to squeeze you, everyone is negotiating with you. They all make it through that. I would say the good ones stay grounded, though there are the stereotypical flashy entrepreneurs as well. But we like entrepreneurs who are down-to-earth, stable and uphold middle class values. That is, sort of, what we find works in the long term. 