Forget valuation, often the business model itself is problematic, says MAPE Advisory's Jacob Mathew

By *Dearton Thomas Hector*, ET Bureau | 5 Jun, 2015, 05.15AM IST 2 comments | Post a Comment

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Just because somebody has downloaded your shopping app in his/her smart phone, you cannot start talking about the lifetime value of a customer, says MAPE Advisory's Jacob Mathew.

Jacob Mathew, *MD & co- founder, MAPE Advisory*

"Talking about valuation of online businesses is a bit like walking against a procession. We are investors in 4-5 such businesses and a few close friends and colleagues are part of the unicorn valuations. One such friend recently remarked: "Earlier, enterprises were about selling to consumers and giving dividend to shareholders; current mood is all about selling to shareholders and giving dividend to consumers"

How do you justify such skyhigh valuations? How are you selling below cost with a negative gross margin just because you have a lot of cash in your capital account? These are difficult questions with seemingly no answers other than talking about Uber's $50bn valuation or how Amazon's humungous market cap is still holding despite years of negligible profits.

Are they relevant or the right metrics in India? Take Ola Cabs' US$2.5 bn valuation in the last round (supposedly going up to US$4bn in the next few months), that is Rs 15000 crores of valuation. Assuming a cost of Rs 5 lakhs for a taxi, you can buy three lakh taxis, and India by various counts have about 3-5 lakh taxis. You ask this and you get to hear about how Uber's valuation is $50 bn though the relevant US market size is only $11 bn and how I am missing the value of disruptive technologies in expanding the market.

Is that the right argument? Uber seems to be making a 30 per cent gross margin on its rides after paying the cab while in India folks seems to be making a 30-35 per cent loss at gross margin levels. Today I took a Uber from home to Bangalore airport — a 33 km ride one way, for which Uber charged me Rs 405. Taking the same ride in my own car would have cost me around Rs 450, just for the fuel and the airport toll - forget the capital cost of the car and the driver's cost.

Valuations are too much into the future and are based on humungous assumptions. You can justify the Flipkart valuation if you assume that by 2020 the Indian online market will be $100 bn and they have 60 per cent market share and that they are making EBITDA margins. Will the current $5-6 bn market actually jump to $100 bn in 5 years? Will the leader have 60 per cent market share and that too in a market like India where not much consolidation is happening? Will the topline hold when you are charging all costs plus a small profit margin to the customers?

Forget valuation, at times the business model itself is problematic. Will buyers pay 2 per cent commission for buying/renting a house in India where the touch point is only online? How can you use a car to home deliver restaurant food with ticket sizes of less than Rs 500/order? Just because somebody has downloaded your shopping app in his/her smart phone, can you start talking about the lifetime value of a customer?

So, I will keep my car at home and get into an Uber/Ola. At an effective rate of Rs 6/km, forget auto rickshaw rates, this seems cheaper than India's Mars mission."

(MAPE Advisory Group advises on private equity funds and M&A deals.)