

How to Find a Liu Qiangdong-like Blue Chip



An interview with Xu Xin (also known as Kathy Xu), Founding Partner of Capital Today

May 22, New York, US. The damp and cold weather does not undermine the passion and happiness at the Time Square. NASDAQ embraces its 118th IPO – JD.com, Inc., which has also been the biggest one among all the IPOs of Chinese companies in the US.

This morning, a figure dressed in purple with a pearl necklace looks outstanding among the crowd of black suits. She is no other than Kathy Xu, founder of Capital Today and the first investor in JD.com.

On the IPO day, JD.com closes at USD 20.90, up by 10% from the issue price and equivalent to a market value of USD 28.6 billion. Holding 7.8% of the total shares in JD.com, Kathy has made a profit of USD 2.2 billion out of the IPO of JD.com for Capital Today. And plus the profits made by Capital Today out of JD.com's Round C and Round D financings, Kathy has received more than a hundredfold return on her investment in JD.com, which has been her most successful case over her 20 years of investment career.

After the IPO of JD.com, Kathy accepted an interview by the journalist of *China Business Journal*, in which she told about how she had discovered a Killer entrepreneur like Liu Qiangdong.

Looking for a Blue Chip

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for a Killer entrepreneur.

China Business Journal: you invested USD 30 million in the JD.com project and has received a return of over USD 2 billion based on its market value on the IPO day. How did you feel with such an investment return?

Kathy Xu: JD.com has so far been the most successful case of mine with more than a hundredfold return. I felt glad that I had invested in the right person.

We were waiting for the opening at NASDAQ with Liu Qiangdong that day. I asked him how he felt when the share price flashed out, and he answered me he was rather delighted but not gloating over. He said although JD.com has been the biggest Chinese company listed at NASDAQ, he would not be really delighted until it becomes the most profitable company some day. I could feel his calmness from his words.

We have invested in JD.com for eight years and my sense of success originates from not only the profits made but also the fact that I have witnessed Liu Qiangdong and his team growing from a 50-personnel company up to a 50,000-personnel listed corporation.

China Business Journal: it was quite early when you invested in JD.com. There were a number of similar companies and the B2C industry had not met its boom. So why did you choose JD.com?

Kathy Xu: investing in a project is primarily investing in a person, and I have spent a lot of time looking for a Killer entrepreneur. For my first meeting with Liu Qiangdong I noticed his computer whereon he had wrote “The Best or Nothing”, which convinced me that he was just the person I had been looking for.

Liu Qiangdong started up his business ever since his campus life. In my eyes, one that starts up business on campus is rarely driven by his own desire for fame or money but by his born nature of entrepreneurship. Furthermore, an entrepreneur on campus must be brave and good at personnel management.

Liu Qiangdong was a social science major and taught himself programming. Having no computers of his own at that time, he had to take a bus for one or two hours to a relative and waited for an opportunity of doing programming exercises on computer until the evening when the workers came off duty. After he learnt it he programmed for others and made profits thereby. Later he opened a shop at Zhongguancun where he sold more CD writers than any other peer, and the situation was likewise good for his CD business later.

His experiences impress me with his cleverness and entrepreneurship. In addition, he is also an honest man who tells you everything instead of the flattering remarks only, which pleases me a lot.

China Business Journal: around 2011, e-commerce was a hot subject among investors and the valuations of many e-commerce enterprises were immensely exaggerated, which intensified the competition. However, you had locked on JD.com before the competition commenced. What is your secret of success?

Kathy Xu: I made up my mind after a 4-hour talk with Liu Qiangdong. I asked him how much

he would need, and he answered me USD 2 million. I said, “That’s far to enough. I will give you USD10 million.”

Given the decision made, I had to push it quickly worrying that he might meet with other investors. I bought him a flight ticket and brought him to Shanghai to meet with my partners the next day. That day we signed a framework agreement after which I provided him with a bridge loan of USD 2 million. Generally money would not be offered until the signing of the formal agreement, but we did so for the purpose of binding him as well as redeeming him from a Renminbi fund, with whom he had signed a contract before. That fund had promised a 5-million-Renminbi investment but refused to go on after an investment of RMB 1 million for such reason that JD.com was suffering a continuous loss.

I was afraid that there had hidden any time bomb in the previous investment contract so I asked Liu Qiangdong for a look at it, but he rejected my request stoutly saying the contract had been attached with a non-disclosure agreement. Despite being severely short of money, he was very stubborn then and would never compromise in anything that he thought was right, which was nothing else but the entrepreneurship we highly appreciated. So at last we made concession and just had the contract reviewed by our attorney to make sure there was no time bomb, and I pledged the same terms and conditions for our cooperation as we had agreed before.

China Business Journal: JD.com was holding a staff of only 50 people at the moment. How did you judge the prospect of the team and the company?

Kathy Xu: Liu Qiangdong showed me the backstage ERP system which had displayed a sales volume as much as RMB 50 million with a monthly growth of 10%. The key point is, he made not the least advertisement but many regular customers still come three times a year. That meant users liked this website.

Besides, Liu Qiangdong was then the No. 1 customer service staff and was replying users’ bulletins online everyday, which reflected his focus on the user experience.

In the communication with his senior management team, I was told that a regular conference was held every day, which was not easy for such a small company.

The success of a small company depends on its boss’ learning ability. At that time, JD.com even had no accountants of its own. After our investment, I suggested to employ an accountant. He agreed but was willing to offer a salary no more than that of his old staff, which was at most RMB 10,000 per month. I spent a lot of time only to find good CFOs rarely worth below RMB 20,000 per month. Later I found a CFO and shared his salary expenditure with JD.com half and half. Two months after the participation of the new CFO, Liu Qiangdong said to me, “a 20,000-Renminbi-salary person is really better than a 5,000-Renminbi-salary one. Please go on with such talent search.” Later many senior managers were introduced into JD.com, who made extremely important contributions towards the rapid growth of JD.com’s business.

Insistence is sometimes vital

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China Business Journal: someone says that in a financing, the entrepreneur will think not only how much money he can take from the investor but also what else the investor can benefit to his business. On what aspects will you usually help the entrepreneur's company?

Kathy Xu: we are good at building brands and can provide it with the experience of the other companies we have invested in. We pushed JD.com to pay over RMB 10 million for the advertisement in buses and the metro as well as the keyword optimization on the internet, which greatly improved the public awareness of JD.com. Secondly, the price war. I feel exceptionally lucky that I gave him USD 10 million for the first investment despite that he asked for only USD 2 million. That made him braver and faster, with the courage for loss-bearing development.

China Business Journal: in your opinion, in which affairs should and should not an investor interfere with regard to the investee? Wherein lies the boundary for an investor to participate in the investee's corporate governance?

Kathy Xu: according to my philosophy, the entrepreneur plays the leading role and makes decisions on whatever relates to the business while the investor only plays a supporting role. An entrepreneur deserves no investment if he is even inferior to us with regard to the decision-making for the business development. Believe the one you have funded. I don't agree with any investor who makes decisions for the investee. After all, an entrepreneur is fighting on the forefront and knows what to do; otherwise you should not have funded him. I think it's most important for an entrepreneur to be insightful and far-sighted, and to be able to see what others cannot see. He shall manage to make many hard decisions. Keep in mind that the truth is usually held by the minority. As an investor, you must always trust him since you have funded him.

China Business Journal: in the case of JD.com, have you survived any difficult time?

Kathy Xu: the entrepreneur I fund must have a killer's intuition for the industry, which Liu Qiangdong satisfies well. JD.com decided to increase its SKUs (Stock Keeping Units). I was afraid that the money might not be adequate and the capital chain might break, as a loss was to be suffered for each SKU. However, Liu Qiangdong insisted on his decision. It was eventually proved that it was a strategic decision of a critical sense. By increasing the SKUs, the ATV (Average Transaction Value) was reduced and users' costs of trial were cut down. The decision of SKU increase exposed to me Liu's excellent strategic insight.

Therefore, I back him when he proposed to build his own warehousing logistics system after our second round of financing. At that time, Ma Yun did not want to engage himself in capital-intensive asset business like warehousing logistics. As a result, JD.com embraced a three-year non-competition period.

We were under strong pressures at early times, since a delivery center is to be built for each city covered by our network, where the loss will not be made up until two thousand orders are received per day. It would cost half a year for some (cities), and two years for some others. A huge loss would be suffered during the process, which required a resolute belief.

Cultivation of Category Leader

We firstly select the person and category and then cultivate the company into a category leader

as soon as possible.

China Business Journal: someone says that for a VC, investment is somewhat like gambling and one success out of ten projects is well enough to make up the losses from all the investment failures. Regarding the case of JD.com, do you think it was as if you were gambling?

Kathy Xu: I can't agree with you. Our capital fund is featured by a style of focus. We have so far invested in 15 cases where 7 investee companies have become the No. 1 brand in their respective sectors, and JD.com is just the most successful one. Other investors invest three cases a year while we may invest in one case every three years. We highly focus on consumer goods brands, retail chains and B2C. We always spend much time in the selection of the course in the hope of identifying a category leader.

We have conducted a research into the US brands. There were 25 US brands ranking top worldwide in the 1920s, where 21 are still among the world's best brands nowadays after 60 to 80 years and three of the other four have become the second best brands. In other words, unless serious mistakes are made, you are difficult to be replaced by others once you are recognized by consumers. Take JD.com as an example. We firstly select the person and category and then cultivate the company into a category leader and root the brand in consumers' hearts as soon as possible. Therefore, it is very important for JD.com to grow fast.

China Business Journal: someone says that the bottleneck for a growing company often lies in its boss. JD.com takes 8 years to grow from a 50-personnel company to a 50,000-personnel one with its turnover increased from RMB 50 million to 100 billion. It is a challenge to the manager. Have you ever worried that such a company may run out of control?

Kathy Xu: efficiency and cost play key roles in retail. At the earliest time, JD.com employed a dozen of VPs and Liu Qiangdong also used to take everything in hand. He convened the regular conference everyday where all VPs had to report to him and all identified problems were promptly solved with a high efficiency. He worked until very late everyday during that period, even with not the least rest in three successive months. With expansion of the corporate size, however, the management mode gradually became less efficient.

Liu Qiangdong has extremely strong learning ability and soon delegates his authority to his subordinates. The senior managers invited to JD.com are offered not only high salaries but also stages and authorities.

We have told many companies about the management trainee plan but only Liu adopts it immediately in his company. Management trainees are recruited from colleges and universities and they are provided opportunities of cross-training in JD.com, where they are provided with large space for learning and development. The management trainees are eventually fixed in a specific position based on their respective preference and playing a pillar role in the development of JD.com.

JD.com has maintained a 200% growth for five or six successive years, wherein HR has been playing a key role. JD.com is where high-end talents (specialized in IT, data and internet) and blue collars (e.g. deliverymen) coexist. There must be something unique in Liu Qiangdong who can manage both the types of human resources concurrently.

