

Insights into the Funding Landscape of Indian Startups

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ABSTRACT

Startups are growing rapidly in almost all the sectors worldwide and are contributing to the economic growth of all the nations. Startups are innovative ventures and funding is very crucial for their growth. The government of various countries are providing the initial funding support to the startups in the form of seed funds. In addition to this, various private sector investors like angel investors, venture capitalists, different financial institutions etc. invest into the different growth stages of these startups and are mainly focused to earn profits with the expansion of these startups. The main aim of this research paper is to explore the various sources of funds available to the startups in their different growth stages. The paper is based on the secondary data sources. The paper elaborates the total funds raised by Indian startups. Split of funds invested by different investors is also given. Major Indian cities and sectors which are attracting more funds also highlighted. Therefore, this is a comprehensive study providing an overview of financial landscape of the Indian startups.

Keywords: Funds, Startups, Bootstrapping, Sources, Venture Capital.

Introduction

Countries all over the world are emerging as hubs of technological innovations. This is characterized by a transition from technology parks to entrepreneurial activities like startups. The rise of innovation-based startups is leading to new sources of employment and economic growth. Technological startups have become new sources of direct and indirect employment. Whereas, innovation and entrepreneurship are not growing smoothly around the world. Some countries are experiencing faster and more sustainable growth whereas others are very slow in startup development. Startups are supporting economic growth and development, reducing economic disparities and ensure the growth of sustainable development goals, especially in the case of developing nations. Even, governments all over the world are making policies to nurture the innovative startups, are identifying the supporting factors for growth, development, and sustainability of the startups.

Opportunities for entrepreneurship are increasing in developing nations like India because of the availability of large working population. India would add 183 million people to the working age group in the period of 2020-2050. These young people are reservoirs of energy and have new ideas, enthusiasm, and spirit to work. This energy can be utilized intelligently by developing a strong entrepreneurial system in the country.

The government of India has introduced many schemes for promoting self-employment through entrepreneurship like Startup-India, Standup-India, and Skill India. Startup India is a major initiative to

generate employment by encouraging the innovative and entrepreneurial spirit in the country, especially among youth. This scheme was started by the government of India on January 16, 2016. The basic idea of the Startup India scheme is to provide employment and promote innovations among the young generation of the country. A startup is a company that provides a unique or innovative solution to previously existing problems. According to the government of India, the definition of a startup is:

- Incorporated as a private limited company or registered as a partnership firm in India.
- Such an entity would be considered a startup only up to 10 years from the date of its incorporation.
- Its turnover for any of the financial years since incorporation should not exceed Rs 100 crores.
- It should be working towards innovation, development, or improvement of the product or process, or services.
- The entity should not be formed by splitting up or reconstructing a business already in existence.

The total number of startups registered with the government of India is increasing over a period of time. Up to the year 2023, 98000 startups were registered in India. The main purpose of this paper is to explore the various sources of funding according to the different growth stages of the startups and also to highlight the funds raised by the Indian startup ecosystem during 2014 to 2021 time period.

Review of Literature

For the growth of a company, funds are very important. Various primary and secondary data-based studies are available to explain the financing sources of the startups. Some of the studies have been reviewed below:

Andaleeb & Singh (2016) had given a conceptual study highlighting the various phases of startup funding from the investor's point of view. The study was based on the secondary data sources. According to investors' point of view, there are six phases of funds available namely bootstrapping, friends and family, seed, growth and early stage, and expansion phases. **Cotei & Farhat (2017)** examined the finances of startup companies over a period of time in the US. The study was based on the primary data sources. The study found that at the initial stages of business growth businessmen use inside capital such as personal savings, borrowing from friends and family, personal debt, and quasi-equity. But as businesses grow, the share of business debt and trade credit financing in the total capital injection volume increases significantly. **Garg & Shivam (2017)** highlighted the various important methods of raising finance for startups. The study found that bootstrapping, crowd-funding, angel investment, venture capital, bank loans, winning contests, getting business loans, and government support are the main sources of startup funding. **Varghese (2019)** explained the different sources of funds according to the different growth stages of the startups. The paper explains that in the initial stage, the founder invests his funds and takes help from his family and friends. In the seed stage of the startup development angel investors are the main sources of funding. At the growth or early stage of the startup development startup takes help from the venture capitalist. In the expansion stage, the company becomes a unicorn and the founder sells his company to earn profit. **Reserve Bank of India (2019)** highlighted a glimpse of the startup ecosystem of India. The study was based on primary data sources and found that bootstrapping was the main source of funding for the startups. **Sharma (2021)** explored the role, significance, and principles of entrepreneurial finance along with different sources of funds at various stages of enterprise development. The study highlighted that anticipating and avoiding financial stress is the main role of entrepreneurial finance. It explained seven principles of entrepreneurial finance. The study revealed that debt financing and equity financing are the main sources finance.

The main findings of the studies show that at the initial level, bootstrapping is the main source of funding whereas in the later stage of the startup's growth angel investors and venture capitalists are the main sources of the funding.

Research Methodology and Objectives

The study is based on secondary data sources. For getting insights into the Indian startup ecosystem, various research papers, reports, government websites, startup India portal, newspaper articles, etc. are analyzed in detail. To elaborate the funding growth of startups, the paper uses the reports "The State of Indian Startup Ecosystem (2021)" and "The State of Indian Startup Ecosystem (2022)" for the period 2014-2022. These reports are published by Inc42, a private media leading

company established in the year 2015 in India, and known for its end-to-end coverage of the Indian startup ecosystem. This company has produced more than 50 research reports which offer detailed insights into companies, people, and market trends shaping the startup ecosystem.

The main objectives of the study are:

- To know the various sources of funds according to the different growth stages of the startups.
- To highlight the total funding raised by Indian startups in the period 2014-2021.
- For getting an overview of the funding of startups working in different sectors of the economy.
- To highlight the funds raised by the major Indian cities and the split of funds invested by different investors.

Sources of Funds

Funds play a pivotal role in the development of any business. A startup uses various sources of funds in different stages of its growth namely Pre-seed stage, Seed stage, Early growth stage and Expansion.

- **Pre-Seed Stage**

This stage is the starting point of any company. In this stage, the initial idea is converted into a business opportunity. This stage requires a small amount of funds. These funds are necessary for converting the idea into a prototype. In this stage, the viability of an idea conversion into the business model, the cost of the business plan, and the innovative aspect of the idea are assessed. This stage of product development is generally financed by the owner himself known as bootstrapping, because at this stage the business failure rate is high. In this stage, the main sources of funds are family and friends, relatives, accelerators and incubators.

- **Seed Stage**

In this stage of company development, market trials are conducted for product acceptance by the customers. The product is re-defined according to the tastes of the customers and the main target of the entrepreneur is to achieve product market fit. The logo of the product, infrastructure, and long-term planning for the business execution is done in this stage. Companies generally find necessary partners for product development like designer companies, potentially public relations and market research firms. In this stage, most of the funds are invested by the entrepreneur himself because of business immaturity. But angel investors, crowd funding, micro venture capital firms, and investment syndicates are also good sources of startup financing at this stage.

- **Angel Investors:** These are individuals who provide their capital to the startups in exchange for equity in the company or convertible debt.
- **Crowd-Funding:** It means raising small amounts of funds from large number of individuals to finance a new business company. This money is raised from investors through the socialization of the project online. Around 600 crowd-funding platforms are raising billions of dollars in the world (Anand & Raj, 2019).
- **Micro Venture Capital Firms:** These companies reinvest small amounts of funds from various sources.
- **Seed Fund Scheme:** Only DPIIT-recognized or registered startups can take benefits under this scheme. Under the Startup India seed fund scheme government of India is providing finance up to Rs. 20 lakhs to startups through DPIIT recognized incubators for proof of concept, prototype development, product trials, market entry, and commercialization.
- **Credit Guarantee Funds for Startups:** To ease access to early-stage debt to finance the capital requirement for startups a credit guarantee scheme with a corpus of 500 crores per year for the period of four years has been established. Under this scheme, the government guarantee to banks and alternate investment funds for funding collateral-free credit of up to Rs. 10 crores (Government of India, 2021).

- **Early-growth Stage**

It is the stage when startup products or services are entirely launched in the market. The primary sources of funds in this stage are:

- **Venture Capital Funds:** These are professionally managed investment funds that are invested in high-growth startups. Venture capital is formed by collecting money from wealthy investors, large institutions, and significant financial organizations. After collecting money, venture capital firms choose a company carefully for investing funds, especially high-growth companies that have boosted innovation and abilities to gain attractive profits (Hoang, 2015).
- **Banks/NBFCs:** These are traditional sources through which startups raise funds.
- **Venture Debt Funds:** Private investment funds are invested into startups on loan basis.
- **Fund of Funds:** The government of India has established a fund of funds of Rs 10,000 crore for capital access to small businesses. The government provides this capital to the SEBI-registered Alternative Investment Funds (AIFs) which are called daughter funds. These alternate investment funds invest money into growing Indian startups through equity and equity-linked instruments. Table 1 shows the sector-wise distribution of fund of funds during 2015-2020.

Table 1: Sector-wise distribution of funds under fund of funds scheme 2015-2020

Name of Sector	Funds Allocation (in crores)
IT, ITES	900 (20%)
Healthcare & Life sciences	495 (11%)
Finance & Technology	405 (9%)
E-commerce	207(6%)
Logistics	180(4%)
Education & Edtech	180(4%)
Artificial Intelligence	135(3%)
Consumer	135(3%)
Food and Beverage	135(3%)
Others	1665(37%)
Total Funds	4500

Source: Government of India, 2020

Table 1, shows that startups in IT and ITES sectors are getting more funds in comparison to other sectors. A total of 4500 crore rupees are invested in 384 startups through this fund.

- **Bridge Financing:** Bridge loans are short-term loans that are given to startups to reach the next round of funding. It generally bridges the gap between the investment level to keep a startup company afloat (Anand & Raj, 2019).
 - **Mezzanine Financing:** It is offered to those startup firms that are growing and gaining profits. It is provided quickly to the firms on the high-interest rate. But, if a firm fail to repay loans on time, venture capitalists can convert the debt into ownership of a company.
- **Expansion Stage**

In this stage, the startup experiences a fast rate of market growth and increases revenue. The company approaches to becomes a unicorn, and a venture capitalist generally invests funds to earn profits. In this stage, a startup company becomes public by selling its shares on a stock exchange. It provides the company access to the public market and also increases its credibility and exposure.

In addition to promote innovations Startup India Scheme is providing incentives like incubation help, seed funding, tax rebate, relaxation in labor and environment laws, and India-foreign tie-ups for the growth of startups. The government of India is also promoting startups by providing financial help through different sector-specific schemes like the Rashtriya Krishi Vikas Yojna (RKVY), Raftar scheme for agricultural startups, ignite scheme for biotech startups, and venture capital assistance for startups in the defense sector. The dairy entrepreneurship development scheme is promoting small entrepreneurs in the animal husbandry sector. Startup entrepreneurs are also taking financial help through Mudra Yojana.

The study provides an overview of total funding in Indian startups through the total amount of investment and total deal counts during 2014-2021. Deals counts may be composed of different kinds of funding which include venture funding, private funding, syndication, initial public offering, and merger and acquisitions. Table 2 represents the funding amount in Indian Startups shown for the period 2014 to

2021. For analyzing the overall funding, compound annual growth rate (CAGR) of funding is calculated for the period of 8 years by using the Eq. (1).

$$\text{CAGR} = \left(\frac{\text{Current Value}}{\text{Initial Value}} \right)^{1/n} * 100 \quad \dots(1)$$

Where

n= time (number of years)

* = multiplication

Table 2: Total Funding in Indian startups (2014-2021)

Year	Amount (in \$ Bn)	Deal Counts	Mega Funding Rounds
2014	5.3	379	12
2015	9.3	987	18
2016	5.7	1050	13
2017	13.7	1000	21
2018	11.9	833	28
2019	12.8	812	33
2020	11.5	924	30
2021	13.7	1044	109
CAGR (%)	12.60%	13.50%	31.76%

Source: Inc42 (2022)

Table 2 shows that startup funding has increased over a period of time. In the year 2014, only \$5.3 bn was invested which has increased to \$13.7 bn in 2021. Any funding round which is equal to or greater than \$ 100 mn is known as Mega Funding Round. In all the consecutive years mega funding was rising in Indian Startups. The funds raised by the startups grew at the rate of 12.60% in the period of 8 years from 2014-2021. Whereas deal counts and mega funding rounds grew by 13.50% and 31.76% during this period. Table 3 shows the sectors-wise funding analysis of startups in the Indian economy for the period 2014-2021.

Table 3: Sector-wise Funding of Startups

Years	Sectors (Funding in \$ bn)								
	Fintech	E-commerce	Consumer Services	Edtech	Media & Entertainment	Enterprise tech	Deeptech	Agritech	Logistics
2014	0.17	3.1	0.1	0.033	0.185	0.15	0.040	0.001	0.094
2015	1.56	2.6	0.9	0.096	0.310	0.79	0.083	0.032	0.396
2016	0.82	1.0	0.5	0.196	0.384	0.57	0.074	0.005	0.292
2017	3.12	3.9	0.7	0.210	0.260	0.69	0.090	0.057	0.279
2018	1.55	2.5	2.4	0.566	0.816	0.64	0.287	0.095	0.318
2019	2.78	2.4	0.9	0.445	0.564	1.09	0.117	0.252	0.907
2020	2.16	0.9	1.8	1.435	0.922	1.63	0.187	0.212	0.261
2021	7.97	10.7	3.0	4.732	3.652	3.21	0.451	0.684	1.462
Total Funding	20.13	27.1	10.3	7.713	7.093	8.77	1.329	1.338	3.707
CAGR calculated (%)	61.76	16.75	52.98	86.02	45.18	46.66	35.37	126.14	40.92

Source: Inc42(2022)

A perusal of Table 3 shows that funding raised by the startups in all sectors has increased manifolds since 2014. Startups in the E-commerce sector have raised the highest funding among all the sectors followed by Fintech sector. Whereas CAGR of funding is highest in agriculture and Edtech sectors respectively. Funding grew with the rate of 126.14% & 86.02% during the period 2014-2021 in startups in both the sectors. The study also highlights the funding of startups in major cities of India. Table 4, shows that high amount of funding is raised in major Indian cities.

Table 4: Funding to Startups in major cities of India

Cities	Funding Raised (in \$ bn)	Growing Sectors
Bangalore	31.5	Edtech, Deeptech
Delhi	24	Fintech, Edtech
Mumbai	7	Media, Entertainment
Pune	2	Fintech, Healthtech
Chennai	1.8	Zoho, Freshwork
Hyderabad	1.5	IT based work

Source: Inc42(2021)

Table 4 shows that Bengaluru has raised the highest amount of funding \$31.5 billion. Edtech and Deeptech sectors are the main growing sectors in Bangalore. Delhi is ranked second with Fintech and Edtech as the main growing sectors. Table 5, shows the split of funds invested by different investors in the time period 2014-2020.

Table 5: Split of funds according to the different investors

2014-2020 (Investors Split)	
Angel Investors	60.1%
Venture Capital	17.9%
Corporate	17.1%
Accelerator and Incubators	1.7%
Family Office	1.2%

Source: Inc42 (2021)

Table 5 shows the total investment done by the different investors. It is found that the majority of funds are invested by angel investors. Venture capitalist invested 17.9% of the funds. Accelerators and Incubators invested just 1.7 % of the total funds.

In the Indian economy, there is biasedness in female-led startups. In the year 2020, a total of \$11.5 billion funds were raised by the Indian Startups. Out of these total funds, the share of female entrepreneurs' funding was \$1.4 billion which is approximately 13% of the total investments (Inc42, 2021). This shows that investors have a low level of confidence and are reluctant to invest in female startups.

Main Findings of the Study

The main findings of the study are the following:

- In the initial stage of the idea execution bootstrapping is the main source of funding for the startups.
- The Government of India has launched mainly three schemes namely the Startup India seed fund scheme, Fund of Funds, and Credit Guarantee Fund for financing the Indian startups.
- The benefit of seed funding scheme is given to startups in their initial stages of establishment.
- The Government of India has invested more funds in IT & ITES sectors through Fund of Funds scheme.
- Indian Startups were raising \$5.3 bn in the year 2014 which has been raised to \$13.7 bn in the year 2021.
- Funds raised by the startups originated in Agritech, Edtech, and Fintech sectors and grew at a higher rate in comparison to startups working in other sectors.
- Bangalore City has raised the highest funding in India.
- The share of angel investors is highest followed by the venture capitalists in startups investment.

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