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VENTURE CAPITAL FINANCING IN INDIA: AN OVERVIEW

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ABSTRACT

In India, the venture capital industry is still at a nascent stage. With a view to promote innovation, enterprise, knowledge based ideas into commercial production and conversion of scientific technology, it is very important to promote venture capital activity in India. Venture capital companies will fill the gap between the knowledge based startup enterprises and capital requirements of technology and funding available from traditional institutional lenders such as banks. This gap exists due to new startups companies which are totally based on intangible assets such as human capital and on a technology-enabled mission, often with the hope of changing the world. In this paper an effort is being made to study the various methods of venture capital financing and to analyze the growth of total cumulative investment and the total number of intermediaries of venture capital financing in India.

KEYWORDS: *Venture capital, Problems, Financial Assistance, Investments, Intermediaries.*

Introduction

In India the venture capital plays important role in the development and growth of innovative entrepreneurship. It is a specialized financial intermediary which combines the technological competence and financial skills, to provide both financial and managerial assist for entrepreneurs in innovative ventures. It can be visualized as —"your ideas and our money" concept of developing business. A growing venture capital companies will fill the gap between the knowledge based startup enterprises and capital requirements of technology and funding available from traditional institutional lenders such as banks. This gap exists due to new startups companies that are totally based on intangible assets like human capital and on a technology-enabled mission, often with the hope of changing the world. However, from the traditional banker point of view, they have neither physical assets nor a low-risk business plan. Not surprisingly, companies such as Apple, Yahoo, Hotmail and Exodus, to mention a few of the successful multinational venture-capital funded companies, initially failed to get capital as startups when they approached traditional lenders like banks. However, they will ready to get finance from several managed venture capital funds that specialize in equity or equity-linked investments in privately held, high-growth companies. Along with this finance came hand-on management assist, smart advice and other skills that helped the entrepreneurial vision to be converted to marketable products.

Venture Capital Financing

Venture capital financing is a type of financing by venture capital. It is private equity capital provided as seed funding to early-stage, high-potential, growth companies (start-up) or more often it is after the seed funding round as a growth funding round. It is provided with the interest of generating high rate of return on investment through an eventual realization event such as trade sale of the company. The features of venture capital investments are as follows:

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- It is a high risk investment made with an intention of creating high returns.
- The investments made in venture capital are based on long term goals.
- The investments are made in a start-up which is potential to grow enough.
- Investments are generally done in innovative projects like in the fields of technology and biotechnology.
- A supplier of venture capital participates in the management of the company also and provides managerial and technical support.

Review of Literature

- **V. Mahesh (2019),** studied the "Challenges of Venture Capital Financing in India" and concluded that the world markets are becoming more and more competitive. Companies are required to be well structured with respect to cost, productivity, technical skills, labour efficiency, changing consumer demand, adaptability and foresightedness to get competitive environment edge over the rival firms. There is an imminent demand for highly cost effective, quality products and so, the need for right access to valuable human capital to guide and monitor along with the necessary funds for financing the new projects. Today India is promoting venture capital financing to new projects, innovative ideas, liberalizing taxation regulations providing tax benefits to venture capitalist.
- **Kishan Kumar Shetty (2017),** studied "A Comparative Study on Impact of Venture Capital Financing on Startups in India" and concluded that the venture capital financing has shown a proliferating growth and has successfully helped young business with high risk and growth potential with financial stability. It bridges the gap where other sources of funds are not capable of funding ventures with high risk. By comparing venture capital financing from USA and China, they analysed that Indian venture capital sector performance is less but taking Indian economy as a whole, there is substantial growth and rapid investment momentum mainly in the consumer technology sector making it one of the most attractive markets for venture capital investments.
- **Viren Chavda (2014),** studied "The overview on Venture Capital Financing in India" and its main aim is to highlights the procedures of financing, issues and challenges faced by Indian venture capital companies. From the study they conclude that markets are becoming more and more competitive. Companies are required to be super efficient with respect to cost, productivity, technical skills, adaptability and foresightedness to get competitive edge over the rival firms. There is a need to support venture capital financing in India, as this would expand the industrial base of high tech industries and promote the growth of technology.

In previous studies the researcher focused on overview of venture capital financing in India and discussed the various challenges faced by venture capital financing in India and also compare the venture financing with USA and China and conclude that India is promoting venture capital financing to new projects and innovative ideas, which helped the young businesses to grow and become more and more competitive. The present study is focus on overview of venture capital financing in India and discuss the growth and trend of Total Cumulative Investment and Total Number of Intermediaries of Venture Capital Financing in India from 2013-14 to 2018-19.

Objectives of the Study

The objectives of the study are as follows:

- To study the various methods of venture capital financing.
- To analysis the growth of Total Cumulative Investment and Total Number of Intermediaries of Venture Capital Financing in India.
- To discuss the trend of Total Cumulative Investment and Total Number of Intermediaries of Venture Capital Financing in India.
- To know the various problems faced by Venture Capital Industry.

Research Methodology

Data used for the study is secondary data. All the relevant information has been collected through official website of SEBI in reference to study the significant growth of Total Cumulative Investment and Total Number of Intermediaries of Venture Capital Financing in India. To analyze the data percentage analysis and trend analysis method is used.

Limitation of the Study

- The data used for the study is secondary data. Hence, the limitation of secondary data are expected which influence the result of the study.
- The study is confined to know the concept of venture capital financing in India only from 2013-14 to 2018-19.
- The study does not focus on one particular sector of venture capital financing.

Methods of Venture Capital Financing

When the companies need money to finance the start-ups which needs immense capital requirements with a powerful business plan and has the capability to grow into a highly profitable venture, the company makes use of the following methods of venture capital financing are:

- **Equity Financing:** All the venture capital companies provide equity financing and the investors who buy the share of any company have a voting right and its contribution is not more than 49% of the entire stake and the ultimately power remains in the hands of entrepreneur.
- **Conditional Loan:** In the case of conditional loans, an entrepreneur needs to pay the lender in the form of royalty, when the company is able to generate revenue or profit. The royalty rate varies between 2% and 15% on the basis of revenue, profit percentage, cash flow of the venture, etc.
- **Conventional Loan:** In conventional loans an entrepreneur has to pay low rate of interest on the borrowed capital and such rate of interest will increase as per the increase in profit. Along with the interest on the borrowed capital an entrepreneur needs to pay a royalty in accordance with the sales/profit.
- **Income Note:** It is a form of hybrid financing on which entrepreneurs needs to repay the principal amount along with the interest within the predetermined stipulated period and need to pay a royalty on sale or profit.
- **Debentures:** The start-up companies raise funds by issuing debenture with a guarantee to repay the amount of the invested money when the security is matured.

Analysis of Data

To analyze the significant growth of Total Cumulative Investment (i.e. investment by Venture Capital Funds and Foreign Venture Capital Investors) and Total Number of Intermediaries of Venture Capital Financing in India, the percentage analysis and trend analysis method is used.

- In table-1 and graph -1 the growth of Total Cumulative Investment and Total number of Intermediaries of venture capital financing in India is shown from the financial year 2013-14 to 2018-19 which is collected through the official website of SEBI:

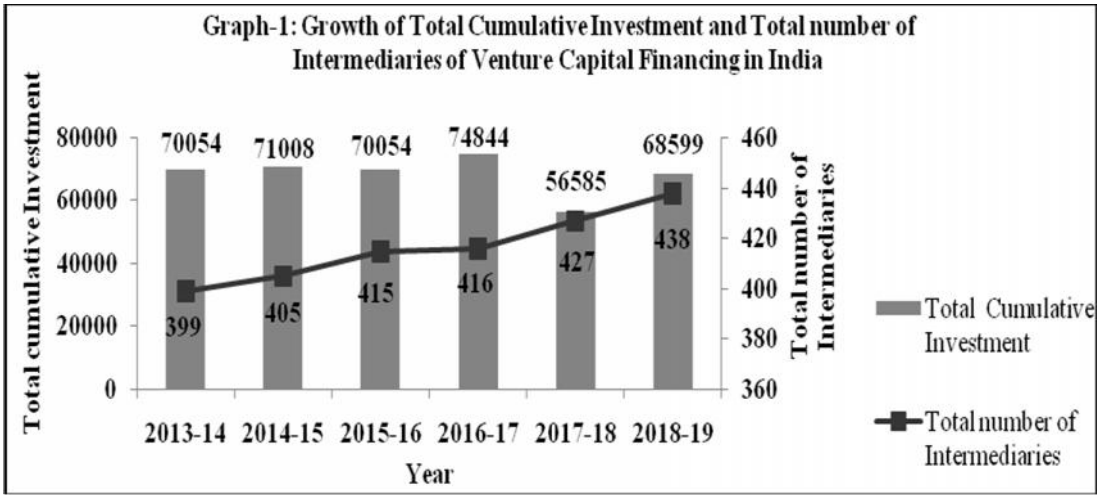
Table 1: Growth of Total Cumulative Investment and Total number of Intermediaries of Venture Capital Financing in India

Years	Total Cumulative Investment	Total number of Intermediaries
2013-14	70054	399
2014-15	71008	405
2015-16	70054	415
2016-17	74844	416
2017-18	56585	427
2018-19	68599	438

Source: SEBI Handbook, 2019 (Monthly)

Note: *Total Cumulative Investment= Venture Capital Funds (VCF's) + Foreign Venture Capital Investors (FVCI's).

*Total number of Intermediary= Intermediaries of Venture Capital Funds (VCF's) + Intermediaries of Foreign Venture Capital Investors (FVCI's)



Interpretation

From table1 and graph-1 it has been observed that the total cumulative investment of venture capital financing (i.e. investment by Venture Capital Funds and Foreign Venture Capital Investors) is increasing year to year except 2017-18. In this year the amount of investment is very less i.e. 56585 crores as compare to other financial years, because of lack of new technologies and unique business models. On the other hand the total number of intermediaries is increasing continuously. In the financial year 2018-19 total 438 intermediaries registered with SEBI for Venture Capital Funds and Foreign Venture Capital Investors.

Percentage and Trend Analysis

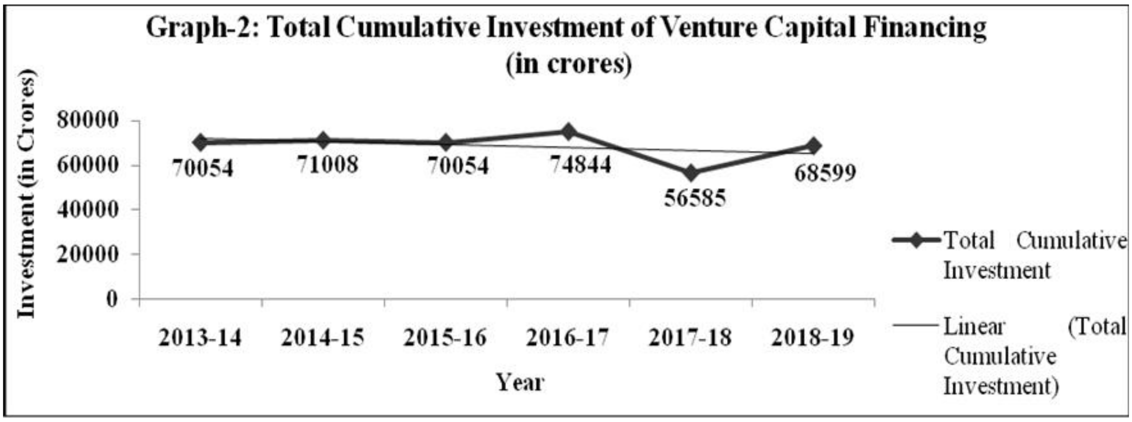
- In table-2 and graph-2 the growth of percentage and trend of Total Cumulative Investment of Venture Capital Financing in India is shown from the financial year 2013-14 to 2018-19:

Table 2: Growth of Total Cumulative Investment (in crore) of Venture Capital in India

Years	Total Cumulative Investment (in crore)	Percentage
2013-14	70054	17.03
2014-15	71008	17.27
2015-16	70054	17.03
2016-17	74844	18.20
2017-18	56585	13.76
2018-19	68599	16.68
Total	**411144**	**100**

Source: SEBI Handbook, 2019 (Monthly)

Note: Total Cumulative Investment= Venture Capital Funds (VCF's) + Foreign Venture Capital Investors (FVCI's)



Interpretation

From table-2 and graph-2 it has been observed that the total cumulative investment of venture capital financing has followed a moderate pattern of investment. But in the financial year 2017-18 the amount of investment is very less as compare to other financial years, it is just because of lack of new technologies and unique business models, but from the year 2018-19 it again started recovering.

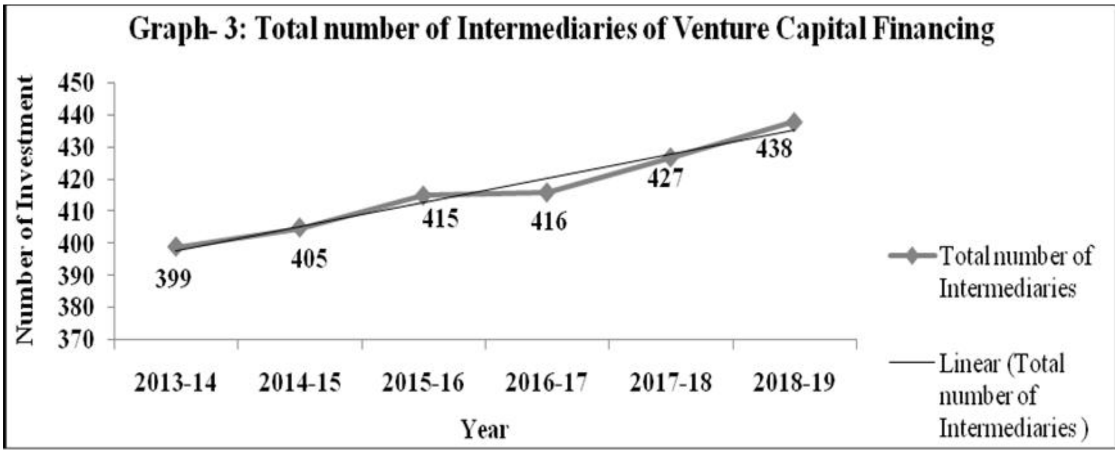
- In table-3 and graph-3 the growth of percentage and trend of Total number of Intermediaries of Venture Capital Financing in India is shown from the financial year 2013-14 to 2018-19:

Table 3: Growth of Total number of Intermediaries of Venture Capital Financing in India

Years	Total number of Intermediaries	Percentage
2013-14	399	15.96
2014-15	405	16.2
2015-16	415	16.6
2016-17	416	16.64
2017-18	427	17.08
2018-19	438	17.52
Total	**2500**	**100**

Source: SEBI Handbook, 2019 (Monthly)

Note: Total number of Intermediary= Intermediaries of Venture Capital Funds (VCF's) + Intermediaries of Foreign Venture Capital Investors (FVCI's)



Interpretation

From table-3 and graph-3 it has been observed that the total number of intermediaries of venture capital financing has followed a linear pattern and the number of intermediaries of Venture Capital Funds and Foreign Venture Capital Investors is increasing year after year. In the financial year 2018-19 total 438 Intermediaries registered with SEBI for Venture Capital Funds (VCF's) and Foreign Venture Capital Investors (FVCI's).

Problems of Venture Capital Industry

In India, the venture capital financing companies is still at a nascent stage. Every entrepreneur knows from the beginning that they are going to face some problems/hurdles at the time of financing the business. These problems/hurdles are:

- **Strong Team Members:** Startups usually start with a team consisting of trusted members with complementary skill sets and these skills are crucial not only for the business to survive, but also for its growth and development. Usually, each member is specialized in a particular area of operations. Assembling a good team is the first major requirement, failure to have one sometimes could break the startup.
- **Raising Funds:** Availability of funds is a major challenge for the startups companies because there is large expectation of the investors and they want to invest in those companies were the risk factor is less and rate of return is fixed.

- **Proper Business Plan:** The business plan should concisely describe the nature of the business. There are number of startup companies who falter because they forgot to plan or maybe they plan but did not cover all the areas like marketing, sales, advertisement, development, staffing, skills shortage, and funding etc.
- **Project Cost and Returns:** Investors would like to invest in those ventures were the future cash inflows are likely to be more than the present cash outflows. While calculating the Internal Rate of Return (IRR) the risk related with the business proposal and the length of time his money will be tied up are taken into consideration.
- **Competitors:** No matter how great your products or services are, it is a crowded market and there are number of products and services are available. So, you have to put yourself in a potential customer's place and see which type of product makes you different.
- **Availability of good Deals:** In India, the availability of "good deals" is a major challenge for venture capitalists. There are number of venture capital players who are facing scalability issue because of the infrastructure limitations like plant location, accessibility, relationship with the suppliers and creditors, transportation facilities, labour availability etc.
- **Future Market Prospects:** There are number of problems related to market which affect the decision of the investors like marketing policies adopted, marketing strategies in relation to the competitors, market research undertaken, future market prospects and market size etc.

Results of the Study

- Equity financing method is mostly used for financing the new start-ups or businesses, because with financial support investors also provide technical and managerial supports which help the business to grow.
- The total cumulative investment of venture capital financing is followed a moderate pattern of investment and the amount of investments is increasing all the financial years except 2017-18.
- The total intermediaries of venture capital financing is followed a linear pattern. The number of venture capital intermediaries is increasing continuously all the financial years because today India is promoting venture capital financing to new projects, innovative ideas, liberalizing taxation regulations providing tax benefits to venture capitalist.
- In India, venture capital industry facing many problems/hurdles related to business plan, strong team members, availability of funds, project cost and competitors etc, which directly affect its growth.

Suggestions

- Indian government continues to introduce several regulatory programmes like Digital India, Startup India which boost the environment for start-ups and investors and helps in the growth and development of venture capital financing in India.
- Developing good infrastructure and use of new and innovative technologies help to attract more Foreign Venture Capital Investors (FVCI).
- Proper scalable business model should be created because investors want to invest in those businesses were they have higher profit margin and lower infrastructure and marketing investment with minimal expenditure.
- Many new startup funding options are available today. So, to increase your chances of getting the funds, you need to choose the most suitable funding alternative. Sometimes, you may also need to use more than one option to fund your startup.
- A specific and realistic business plan should be chalk out because when investors pay you, they expect to see how you spend their money to grow your business to its next milestone.

Conclusion

The venture capital investment assists in nurturing innovative entrepreneurship in India. It is a risk financing generally available in the form of equity or quasi-equity like convertible loan instruments. It gives the business fund based on their potential and their interest as perceived by the investors.

India is promoting the venture capital financing to new tasks, innovative ideas, liberalising taxation guidelines providing tax advantages to venture capitalist. But still there is a need to create awareness and to build an entrepreneurial environment; a lot of emphasis should now be given to creating infrastructure for mentoring startups. Various contributors such as Government, corporate and funding institutions should join hands to provide better ecosystem to start up companies. The country waits for the rapid project capital investment commercial enterprise in India regardless of the present problems in the Indian industrial infrastructure.

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