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RESEARCH ARTICLE

VENTURE CAPITAL IN INDIAN ECONOMY

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Abstract

The Venture Capital Industry in India has grown significantly since last few years. The Venture capital sector is the most vibrant industry in the financial market today. Venture capitalists are professional investors who specialize in funding to companies and building young, innovative enterprises to support business expansion with strategically. Venture capitalists are long-term investors who take a hands-on approach with all of their investments and actively work with entrepreneurial management teams in order to build great companies which will have the potential to develop into significant economic contributors. The duration for entry and exit such venture capitalist for 5-7 years to maximize their profit and return back. Venture capital is an important source of equity for start-up companies. Venture capitalists are people or companies who pool financial resources from high net worth individuals, pension funds, corporate insurance companies, etc. to invest in high risk - high return ventures that are unable to source funds from regular channels like banks and capital markets. The venture capital industry in India has really taken off in and it unbelievable role in Indian Economy. Venture capitalists not only provide monetary resources but also help the entrepreneur with guidance in formalizing his ideas into a viable business venture with existing resources or import new technology.

Introduction:-

With technology and knowledge based ideas set to drive the global economy in the coming millennium, and given the inherent strength by way of its human capital resources development, technical skills enhancement , cost competitive workforce, research and entrepreneurship, India can unleash a revolution of wealth creation and rapid economic growth in a sustainable manner. However, for this to happen, there is a need for risk finance and venture capital environment which can leverage innovation, promote technology and harness knowledge based ideas.

Types of Venture Capital Funds:-

There are different types of Venture Capitalist & Investors , development finance institutions such as Andhra Pradesh Venture Capital Limited (APVCL) by Andhra Pradesh State Finance Corporation (APSFC) and Gujarat Venture Finance Company Limited (GVCFL) by Gujarat Industrial Investment Corporation (GIIC). • VCFs promoted by Public Sector banks such as Canfina by Canara Bank and SBI-Cap by State Bank of India. • VCFs

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promoted by the foreign banks or private sector companies and financial institutions such as Grindlay's India Development Fund, Credit Capital Venture Fund and Indus Venture Fund.

Venture capital at a take-off stage in India;-

The venture capital industry in India is still at a growing stage today and there are tremendous changes seen since 1993 when VCAI formulated. With a view to promote innovation, enterprise and conversion of scientific technology and knowledge based ideas into commercial production, it is very important to promote venture capital activity in India. India‘s recent success story in the area of information technology has shown that there is a tremendous potential for growth of knowledge based industries. This potential is not only confined to information technology but is equally relevant in several areas such as other sectors eg. Bio-technology, pharmaceuticals and drugs, agriculture, food processing, telecommunications, service industry, Information Technology etc. Given the inherent strength by way of its skilled and cost competitive manpower, technology, research and entrepreneurship, with proper environment and policy support, India can achieve rapid economic growth and competitive global strength in a sustainable manner.

A flourishing venture capital industry in India will fill the gap between the capital requirements of Manufacture and Service based startup enterprises and funding available from traditional institutional lenders such as banks. The gap exists because such startups are necessarily based on intangible assets such as human capital and on a technology-enabled mission, often with the hope of changing the world. Very often, they use technology developed in university and government research laboratories that would otherwise not be converted to commercial use. However, from the viewpoint of a traditional banker, they have neither physical assets nor a low-risk business plan. Not surprisingly, companies such as Apple, Hotmail and Yahoo, to mention a few of the many successful multinational venture-capital funded companies, initially failed to get capital as startups when they approached traditional lenders. However, they were able to obtain finance from independently managed venture capital funds that focus on equity or equity-linked investments in privately held, high-growth companies. Along with this finance came smart advice, hand-on management support and other skills that helped the entrepreneurial vision to be converted to marketable products.

A similar investor preference for start-up companies eg. IT companies is being seen, though not of the same magnitude. Yet, it is apparent that investors are willing to take higher risks for a potentially higher reward by investing in start-up companies.

Finally, exit options were considered to be few, with the general feeling that entrepreneurs were unwilling to sell their start-ups even if it was feasible. As a result, much of the risk capital available was not quickly deployed. However, since March 1999, things have been changing dramatically for the better in this concern.

Financing stages:-

There are typically six stages of venture round financing offered by Venture Capitalist, that roughly correspond to these stages of a company's development & funding .

- **Seed Money**:Lowlevel financing needed to prove a new idea, often provided by angel investors. Crowd funding is also emerging as an option for seed funding which help to startup the company.
- **Start-up**: Early stage firms that need funding for expenses associated with marketing and productdevelopment
- **Growth (Series A round)**:Early sales and manufacturing funds it is series a round and funds required various times as need in business.
- **Second-Round**: Working capital forearly stage companies that are selling product, but not yet turning aprofit
- **Expansion:** Also called Mezzanine financing, thisis expansion money for a newly profitable company **.**
- **Exit of venture capitalist** : Also called bridge financing, 4th round is intended to finance the "goingpublic" process between the first round and the fourth round, venture-backed companies may also seek to take venture debt

Role of Venture Capital in Funding Various Startups Companies:-

Venture Capital financing has seen a sea change over the past few years. Venture funding initially started with the aim of supporting talented entrepreneurs and assisting them in strengthening their growing business and providing them with the much needed financing which otherwise was not available to them.

Venture capitalists:-
A venture capitalist is a person Institute or investment firm that makes venture investments, and these venture capitalists are expected to bring managerial and technical expertise as well as capital to their investments. A venture capital fund refers to a pooled investment vehicle that primarily invests the financial capital of third-party investors in enterprises that are too risky for the standard capital markets or bank loans. Venture capital firms typically comprise small teams with technology backgrounds (scientists, researchers) or those with business training or deep industry experience.

A core skill within VC is the ability to identify novel technologies, Concept of Business idea that have the potential to generate high commercial returns at an early stage from the stage start up to maturity level . By definition, VCs also take a role in managing entrepreneurial companies at an early stage, thus adding skills as well as capital, thereby differentiating VC from buy-out private equity, which typically invests in companies with proven revenue, and thereby potentially realizing much higher rates of returns. Inherent in realizing abnormally high rates of returns is the risk of losing all of one's investment in a given startup company. As a consequence, most venture capital investments are done in a pool format, where several investors combine their investments into one large fund that invests in many different startup companies. By investing in the pool format, the investors are spreading out their risk to many different investments versus taking the chance of putting all of their money in one start up firm.

Structure:-
Venture capital firms are typically structured as partnerships, the general partners of which serve as the managers of the firm and will serve as investment advisors to the venture capital funds raised. Venture capital firms in the United States may also be structured as limited liability companies, in which case the firm's managers are known as managing members. Investors in venture capital funds are known as limited partners. This constituency comprises both high net worth individuals and institutions with large amounts of available capital, such private pension funds, university financial endowments, insurance companies ,foundations, , and pooled investment vehicles, called funds of funds .In Indian various institution and financial houses which regulate and govern by Government of India and VCAI Those are SIDBI, ICFAI, ICICI Bank Ltd. , SBI Venture Capital etc.

Types:-
Venture Capitalist firms differ in their approaches. There are multiple factors, and each firm is different. Some of the factors that influence VC decisions includes:

- Business situation: Some VCs tend to invest in new ideas, or fledgling companies. Others prefer investing in established companies that need support to go public or grow.
- Some Venture Capitalist invest solely in certain industries or sectors.
- Some prefer operating locally while others will operate nationwide or even globally.
- VC expectations often vary. Some may want a quicker public sale of the company or expect fast growth. The amount of help a VC provides can vary from one firm to the next.

Roles:-
Within the venture capital industry, the general partners and other investment professionals of the venture capital firm are often referred to as "Venture Capitalists" or "VCs". Typical career backgrounds vary, but, broadly speaking, venture capitalists come from either an operational or a finance background. Venture capitalists with an operational background tend to be former founders or executives of companies similar to those which the partnership finances or will have served as management consultants. Venture capitalists with finance backgrounds tend to have investment banking or other corporate finance experience.Although the titles are not entirely uniform from firm to firm, other positions at venture capital firms include:

Principal:-
This is a mid-level investment professional position, and often considered a "partner-track"position. Principals will have been promoted from a senior associate position or who have commensurate experience in another field, such as investment banking,

Entrepreneur-in-residence:-
(EIR)—EIRs are experts in a particular domain and perform due diligence onpotential deals. EIRs are engaged by venture capital firms temporarily (six to 18 months) and are expected to develop and pitch startup ideas to their host firm although neither party is bound to work with each other. Some EIRs move on to executive positions within a

portfolio company.

Venture partners:-
Venture partners are expected to source potential investment opportunities ("bring indeals") and typically are compensated only for those deals with which they are involved.

Management consulting, or a market of particular interest to the strategy of the venture capital firm.

Associate:-
This is typically the most junior apprentice position within a venture capital firm. After a fewsuccessful years, an associate may move up to the "senior associate" position and potentially principal and beyond. Associates will often have worked for 1–2 years in another field, such as investment banking or management consulting.

Need of Venture Capital:-
There are entrepreneurs and many other people who come up with bright ideas but lack the capital for the investment. What these venture capitals do is to facilitate and enable the start up phase companies.

When there is an owner relation between the venture capital providers and receivers, their mutual interest for returns will increase the firms motivation to increase profits.

Venture capitalists have invested in similar firms and projects before and, therefore, have more knowledge and experience. This knowledge and experience are the outcomes of the experiments through the successes and failures from previous ventures, so they know what works and what does not, and how it works. Therefore, through venture capital involvement, a portfolio firm can initiate growth, identify problems, and find recipes to overcome them.

Venture Finance Process &Features of Venture Capital investments
- High Risk
- Lack of Liquidity
- Long term horizon
- Equity participation and capital gains
- Venture capital investments are made in innovative projects
- Suppliers of venture capital participate in the management of the company

Methods of Venture capital financing:-
- Equity
- conditional loan
- participating debentures

The funding process: Approaching a Venture Capital for funding as a Company:-

The venture capital funding process typically involves four phases in the company's development:-

- Idea generation
- Start-up
- Ramp up
- Exit
- Following are brief discussion involve phase in VCs :

Step 1: Idea generation and submission of the Business Plan:-

The initial step in approaching a Venture Capital is to submit a business plan. The plan should include the below points:

- There should be an executive summary of the business proposal
- Description of the opportunity and the market potential and size
- Review on the existing and expected competitive scenario
- Detailed financial projections
- Details of the management of the company
- There is detailed analysis done of the submitted plan, by the Venture Capital to decide whether to take up the project or not.

Step 2: Introductory Meeting:-

Once the preliminary study is done on ideas of the businessby the VC and they find the project as per their preferences, there is a one-to-one meeting that is called for discussing the project in detail. After the meeting the VC finally decides whether or not to move forward to the due diligence stage of the process.

Step 3: Due Diligence:-

The due diligence phase varies depending upon the nature of the business proposal. This process involves solving of queries related to customer references, product and business strategy evaluations, management interviews, and other such exchanges of information during this time period.

Step 4: Term Sheets and Funding:-

If the due diligence phase is satisfactory, the VC offers a term sheet, which is a non-binding document explaining the basic terms and conditions of the investment agreement. The term sheet is generally negotiable and must be agreed upon by all parties, after which on completion of legal documents and legal due diligence, funds are made available.

Types of Venture Capital funding:-

The various types of venture capital are classified as per their applications at various stages of a business. The three principal types of venture capital are early stage financing, expansion financing and acquisition/buyout financing.

The venture capital funding procedure gets complete in six stages of financing corresponding to the periods of a company's development

- ***Seed money:*** *Low level financing for proving and fructifying a new idea*
- ***Start-up:*** *New firms needing funds for expenses related with marketing and product development*
- ***First-Round:*** *Manufacturing and early sales funding*
- ***Second-Round:*** *Operational capital given for early stage companies which are selling products, but not returning a profit*
- ***Third-Round:*** *Also known as Mezzanine financing, this is the money for expanding a newly beneficial company*
- ***Fourth-Round:*** *Also called bridge financing, 4th round is proposed for financing the "going public" process*

Early Stage Financing:-

Early stage financing has three sub divisions seed financing, start up financing and first stage financing.

- Seed financing is defined as a small amount that an entrepreneur receives for the purpose of being eligible for a start up loan.
- Start up financing is given to companies for the purpose of finishing the development of products and services.
- First Stage financing: Companies that have spent all their starting capital and need finance for beginning business activities at the full-scale are the major beneficiaries of the First Stage Financing.

Expansion Financing:-

Expansion financing may be categorized into second-stage financing, bridge financing and third stage financing or mezzanine financing.

Second-stage financing is provided to companies for the purpose of beginning their expansion. It is also known as mezzanine financing. It is provided for the purpose of assisting a particular company to expand in a major way. Bridge financing may be provided as a short term interest only finance option as well as a form of monetary assistance to companies that employ the Initial Public Offers as a major business strategy.

Acquisition or Buyout Financing:-

Acquisition or buyout financing is categorized into acquisition finance and management or leveraged buyout financing. Acquisition financing assists a company to acquire certain parts or an entire company. Management or leveraged buyout financing helps a particular management group to obtain a particular product of another company.

Advantages of Venture Capital:-

- They bring wealth and expertise to the company
- The business does not stand the obligation to repay the money
- Large sum of equity finance can be provided
- In addition to capital, it provides valuable information, resources, technical assistance to make a business successful

Disadvantages of Venture Capital:-

- As the investors become part owners, the autonomy and control of the founder is lost
- It is a lengthy and complex process
- It is an uncertain form of financing
- Benefit from such financing can be realized in long run only

Exit route:-

There are various exit options for Venture Capital to cash out their investment:

- IPO
- Sale to other strategic investor
- Promoter buyback
- Mergers and Acquisitions

Examples of venture capital funding:-

- ✓ **Kohlberg Kravis & Roberts (KKR),** one of the top-tier alternative investment asset managers in the world, has entered into a definitive agreement to invest USD150 million (Rs 962crore) in Mumbai-based listed polyester maker JBF Industries Ltd. The firm will acquire 20% stake in JBF Industries and will also invest in zero-coupon compulsorily convertible preference shares with 14.5% voting rights in its Singapore-based wholly owned subsidiary JBF Global Pte Ltd. The funding provided by KKR will help JBF complete the ongoing projects.

- ✓ **Pepperfry.com**, India's largest furniture e-marketplace, has raised USD100 million in a fresh round of funding led by Goldman Sachs and Zodius Technology Fund. Pepperfry will use the fundsto expand its footprint in Tier III and Tier IV cities by adding to its growing fleet of delivery vehicles. It will also open new distribution centres and expand its carpenter and assembly service network. This is the largest quantum of investment raised by a sector focused e-commerce player in India.

Compensation:-

- ❖ Venture capitalists are compensated through a combination of management fees and carried interest .
- ❖ Management fees an annual payment made by the investors in the fund to the fund's manager to pay forthe private equity firm's investment operations. In a typical venture capital fund, the general partners receive an annual management fee equal to up to 2% of the committed capital.
- ❖ Carried interest a share of the profits of the fund (typically 20%), paid to the private equity fundsmanagement company as a performance incentive. The remaining 80% of the profits are paid to the fund's investors Strong limited partner interest in top-tier venture firms has led to a general trend toward terms more favorable to the venture partnership, and certain groups are able to command carried interest of 25– 30% on their funds.

Because a fund may be run out of capital prior to the end of its life, larger venture capital firms usually have several overlapping funds at the same time; doing so lets the larger firm keep specialists in all stages of the development of firms almost constantly engaged. Smaller firms tend to thrive or fail with their initial industry contacts; by the time the fund cashes out, an entirely-new generation of technologies and people is ascending, whom the general partners may not know well, and so it is prudent to reassess and shift industries or personnel rather than attempt to simply invest more in the industry or people the partners already know.

Venture capital firms and funds:-

A venture capitalist is a person or investment firm that makes investments in newly set-up ventures. These venture capitalists are expected to bring managerial and technical expertise as well as capital to their investments. A venture capital fund refers to a pooled investment vehicle which is also known as limited partners or Limited Liability Company. Limited Liability company primarily invests the financial capital of third-party investor in enterprises that are too risky for the standard capital markets or bank loans.

Top Most Active Venture Capital Firms In India for Startups:-

1. Helion Venture Partners
2. Blume Ventures
3. **Accel Partners**
4. Sequoia Capital India
5. Nexus Venture Partners
6. Inventus Capital Partners
7. IDG Ventures
8. Naspers
9. Zodius Capital
10. Warburg Pincus
11. Canaan Partners
12. Axon Partners Group
13. SIDBI Venture Capital Limited
14. ICICI Venture Capital Ltd.
15. Intel Capital

Role of Venture Capital in Indian Economy &Venture capital investments hit an all time high in 2015

For venture capital to progress in an economy, the concept of industrialist must become a part of the societal framework (Bygrave, 1989). Venture capitalists are opportunity seekers Bygrave,2001). Abundance and visibility of entrepreneurial activity are necessary to attract their attention (Guler and Gullien, 2004). This is particularly the case for venture capital firms engaging incross border activities, whose primary motivation and objectives are achieving high return on investment (ROI) figures (White, Gao, and Zhang, 2002). Therefore it is necessary to examine the number of opportunities offered to VC's, but even more importantly, the nature or type of theopportunities at hand.The Venture Capital industry has grown many folds over the last decade and a half. The number of venture capital funds increased in a significant manner the total corpus increased from Rs.200 crores in 1990 to Rs.5000 crores in 2000 and approximately 15,000 crore in 2010.

In India the venture capital plays a vital role in the development and growth of innovative entrepreneurs. Venture capital financing is in its early stage in India. The emerging scenario of global competitiveness has put an immense pressure on the industrial sector to improve the quality level with minimization of cost of products by making use of latest technology skills. Venture capital may take various forms at different stages of the projects. There are four successive stages of development of a project like development of a project idea, implementationof the idea, commercial production and marketing and finally large scale investment to exploit the economics of scale and achieve stability. Cumming and Macintosh have defined venturecapital as "Financial intermediaries who gets capital investment from various institutionalinvestors, high net worth people from the various economic sectors and make investment of these pooled deposits in small and private business which have high technology and have a lot of potential for high growth.

In general term we can say that venture capital means capital which is intended to invest into a highly risky firm with good growth potential. Venture capitalist is a person who works as an intermediary between investors who give their fund to invest and new companies which gets risk capital on another hand.

Conclusion:-

The venture capital industry is emerging in India it is very helpful to start business and entrepreneurs as a result of internal and external factors. The World Bank funded the creation of the first venture capital funds. These funds were the beginning of a process of legitimatizing venture investing and they were a training ground for venture capitalists who later established private venture capital funds. The world is becoming increasingly competitive. Companies are required to be more efficient in relation to cost, productivity, labour efficiency, technical know-how skills, adaptability and foresightedness. There are many sectors of the economy that are ready for venture capital investors like IT, Retailing, Manufacturing, Pharmacy, service along with Government sectors eg. Railway , Construction and Agriculture Sector getting benefits of Venture Capital and inherits new technology. The concept of Venture Capital Help Indian Economy and Growth of GDP.

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