FUNDING TRENDS FOR STARTUPS IN INDIA

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Abstract

Startups are keys for entrepreneurial growth in the country. They are germinating seeds on which the foundation of business pyramid is laid. It is true that all the seeds that we sow do not grow to trees that give sheds and lives to millions of creatures. Similarly, all the startups which germinate with some or more innovative ideas do not grow to big businesses, some die out but many of them travel through difficult phases and become vast business houses to give impetus to economic development and job creation for millions of people. The startups which survive business turbulences and become big business are well known to all like TATA, Reliance, Infosys, Wipro, HCL groups HDFC bank, ICICI bank etc., and the latest origins of Unicorns like e-retailer **Flipkart**, mobile wallet company **Paytm,** hotel aggregator **OYO rooms**, ride sharer **Ola cabs**, learning apps company **Byju,** and food deliverers **Swiggy**. However, the startups which failed to take off or die in the business turbulence are quickly forgotten and buried. Many of the startups fail due to poor managerial and marketing strategies, inadequacy of cash to run the show indicating thereby that funding is one of the key issues to set ideas into growth and become business ventures. In this paper the numbers of startups growing in India and their funding pattern have been studied for internet apps or technology based companies. From the study it is seen that India is becoming a start hub with a number of startups growing during 2015-18 and there is constant flow of money for funding the new businesses with successful new ideas backed with documented business plan.

Keywords: Bootstrapping, break even, business turbulence, crowd funding, debt finance, equity funding, SEBI, SEC, seed funding.

Introduction

Startups are basically the new business entities or companies that evolve out of innovative technology and business ideas that develop new utility in products and services to meet market needs. They are the young companies in the first stage of operation with nascent business model disrupting the existing market. These new companies are usually financed by individuals or small group of individuals. Graham (2012) says in his essays on entrepreneurship "Startup equals growth" that startup companies need not necessarily work on technology or take venture funding but they must be designed to grow fast and everything else we associate with startup follows from growth. As per government notification (Ministry of Commerce and Industry, 2015, Government of India) an entity is identified as a startup upto five years of its incorporation if its turnover does

not exceed Rs. 25 crores in the last five financial years, and it is working towards innovation, development, deployment, and commercialization of new products, processes or services driven by technology or intellectual property. The startups conceptualize ideas, ascertain marketability, allocate resources, establish products, scale up, and grow from small companies to scalable business models. More and more capital is needed from the conception of novel innovative ideas till the scaling up of business model. Raising capital is both necessity as well as difficult for all entrepreneurs, especially first time entrepreneurs. Several rounds of financing are required as a firm starts and grows (Bruno & Tayebjee, 1985). Since high costs are involved in the develompent of technology, technlogy startups need more funds than what can be arranged from personal saving or loan from close friends and families. Further, there is no contract, assets, receibale, and collateral to obtain bank debt for such entrepreneurs. Tapping the required amount from external sources is always a greater challenge for first time business venturers. Fisman and Love (2003) described that the startup firms struggle to overcome the weakness in financial development while established firms are able to use trade credit as a substitute of firm financing. Comin (2014) also stated that the difficulty faced by startups in raising capital adversely impacts commercialization of new technology. Arranging finance is one of the key areas for the startups to stand and establish in markets. Many such new ventures fail due to lack of capital to run business, scale up, and grow to mature businesses. Crowne (2002) also stated that most of the startup companies fail before realizing any significant achievements.

At the initial stage, entrepreneurs are more committed and try to manage fund from internal sources as well as by incurring personal debt rather than sourcing from external financers. Though this gives more freedom to develop the company, it lands entrepreneurs into a risky zone. This is also called bootstrapping. This has been defined as “A collection of method used to minimize the amount of outside debt and equity financing needed from bank and investors” (Alec, 2006). This internal source of finance includes owner financing, sweat equity, minimizing inventory and debtors, increasing creditors by delaying payments, incurring personal debt, managing subsidy finance etc. Many successful companies like Dell Computer and Facebook etc. have also managed their internal sources of finance at early entrprenerial stages.

Many startup ventures need more money than what the owner or entrepreneurs manage from the internal sources. For obtaining external finance a well documented business plan containing background information about the business, promoters, organizational goals, and the plans for reaching them are submitted to financiers and investors. The investors after evaluation of business plan and potential of growth invest in such projects. The external financiers and investors not only invest for returns but also provide guidance and support through review and monitoring of business ventures. The external sources of funding may take any combination of the angel/seed funding, private equity funding, debt funding, and crowd funding etc.

Objective

Before on set of papers a number of research questions hunted like, are we able to develop startups in India? Whether the startup ventures are evenly growing on pan India basis or concentric to certain region? Do the new innovative ideas get support and backing? Do the small and young entrepreneurs get enough funding to convert their ideas into viable project? What is the funding pattern like whether the young entrepreneurs are getting enough seed funding to culminate and validate the innovative ideas into products and services, whether they are getting enough equity funding to launch and scale up successfully the commercial operations for the products validated? Considering the above questions in mind, the following hypotheses emerge.

(a) The new startups are growing on pan India basis.
(b) The new startups are co-centered in certain region.
(c) The new startup companies are getting enough funding for seed stage.
(d) The new startup companies are getting enough funding at growth stage.

Methods

The research is exploratory where empirical study has been made about the growing startups in India and its comparison with other country of world, the existing funding tools available for the starts ups. Funding pattern of internet app and technology based startups during Jan'2015 to December'2018 were studied. The researcher relied on the data obtained through secondary source for internet / technology based starts ups funding deals. The date on which the funding deal is announced has been taken into cognizance for analysis of the startups name or products normally referred in the deals. For uniformity and analysis, all the funding deal amount has been converted to USD on the prevailing exchange rate at the time of the deal.

Analysis and Discussion

India has moved to 3rd position in technology based startups after USA with more than 47,000 and UK over 4500 during 2015. This has also been revealed in the study done by Assocham in association with Thought Arbitrage Research Institute that India is leading to 3rd largest technology based startups spreading mainly in Delhi NCR, Banglore ,Mumbai and thereafter Hyderabad, Ahmedabad, Kolkata, and Chennai etc. (PTI, 2016). In a report on startups, Indian an overview by Assocham and Grand Thornton India LLP, the comparison of Indian startups during 2015 has been made with other countries, the details of which are appended in **Table I** given below (Assocham and Grand Thornton, 2016).

Table 1.

Details	India	China	Israel	USA
Total number of startups	10000	10000	4750	83000
Tech based startups	4300	3400	4000	48500
Non Tech startups	5700	6600	750	34500
New Set up in days	30-60	30	13	4
Corporate tax rate	34%	25%	26%	39%
Bank lending rate	10.30%	5.60%	3.90%	3.30%
R&D spending % of GDP (Est.2014)	0.85%	1.90%	4.20%	2.80%

Source: World Bank News articles, Govt. sites.

From Table 1 it is noticed that in setting up startups ventures, we are at par with China while on technology based startups we are leading after USA. However, the compliance for setting up new businesses and bank lending rates needed to be reduced to boost more startups in India. The R&D spending may also increase considerably with more opportunities and avenues, lesser startup cost due to reduction in bank lending rates, and fewer legal compliances for startups.

Geographical Distribution of Startups (2015-2018)

Historically the manufacturing industries were being set up and growing where they can easily source raw materials and supply to markets. However, in the present information age the technology based startups companies are growing in the areas where the entrepreneurial eco system is better suited for technical and financial support. The data on geographical distribution of internet app / technology based startups in India are tabulated hereunder.

Table 2
Distribution of Technology Startups

	2015		2016		2017		2018		Total (2015-18)	
Region	No	%	No	%	No	%	Nos	%	Nos	%
Delhi NCR	260	27.7	335	32.91	199	28.97	83	26.62	877	29.72
Bangalore	205	21.93	297	29.17	226	32.9	101	32.79	829	28.12
Mumbai	168	17.97	188	18.47	141	20.52	62	20.13	559	18.96
Others*	302	32.41	198	19.45	121	17.61	63	20.46	684	23.20
Total	935	100	1018	100	687	100	309	100	2948	100

*Delhi NCR- National Capital Region include Delhi, Gurugram, Faridabad, NOIDA and Ghaziabad

* Others include major cities like Ahmedbad, Hyderbad, Chennai, Pune and Kolkata Jaipur, Indore etc. where number of startups <50

From Table 2 it is seen that around 70% to 80% of technology based startups are concentrated in 3 regions like NCR, Banglore and Mumbai, while the balance are spread in rest of India like Ahmedabad, Hyderaba,Chennai, Pune, Kolkota, Jaipur, Indore, and other places.

The geographical distribution of startups has been shown in Fig. 1.

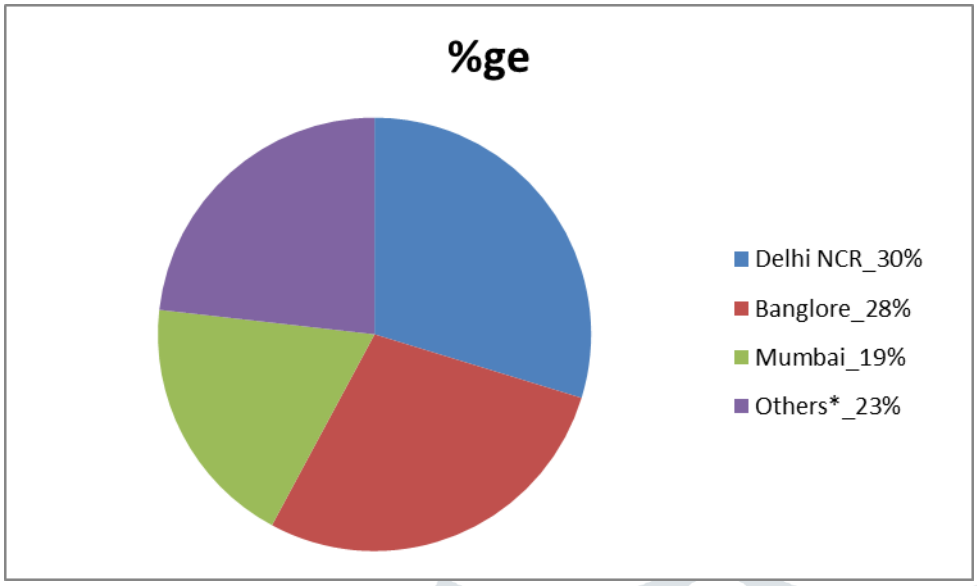

Fig. 1. Geographical Distribution of Startups

Funding Stages

The initial funding in almost all startups originates from the entrepreneur himself for investing in business ideas. As the idea shapes into a business venture, more and more funds are needed to galvanize innovative ideas into business process, business development, and growth. The fund requirement increases with increase in activity of shaping ideas into business processes, conceptualizing the innovative ideas into products and services, and adding utilities through product development, thereafter marketing and establishing the products and services in the market, and scaling up the business development. The funding need of business ventures at different stage of time is depicted through the diagram FR on startups funding, and revenue growth in figure-2.

In the diagram it is depicted that the funding stages can be divided in two time zone, that is, initial stage (seed) funding, and the second stage (growth) funding where the revenue starts to flow in the business depicted through revenue curve. Then a time comes in the activity where the revenue flow matches the funding costs (breakeven). Thereafter, any incremental revenue yields to profit or internal accrual.

Diagram-FR

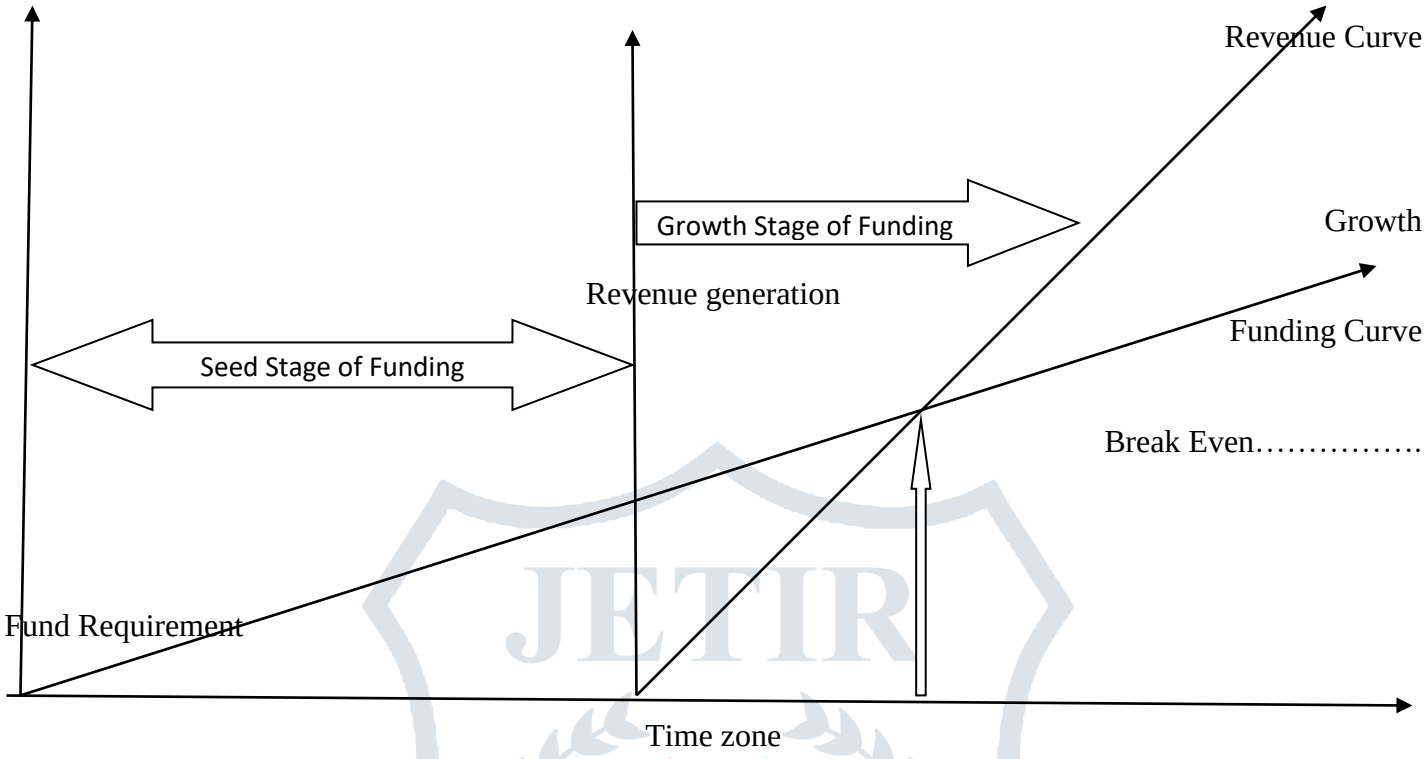

Fig.2. Funding Stages

Funding Deals

The funding deals for startups often come in newspapers. The funding deals during the period January 2015 to December 2018 has been captured by Trak.in for all investment deals in internet app and technology based startups. The actual numbers of startups and their funding deals may be more but the analysis has been made based on data taken from the records of funding and investment deals in internet app & technology based startups by trak.in. The amount of fund commitment has been converted in equivalent USD based on the exchange rate prevailing on the date of deals. In the following table the total no of deals in different type of funds with or without fund commitments has been disclosed.

Table III.

					Amount not disclosed
Year	Period	Types of Funding	Total number of deals	Amount (Million USD)	Number of deals
2015	Jan-Dec	Seed Funding	498	164.95	199
		Private Equity Funding	435	8435.77	83
		Crowd Funding	2	0.16	0
		Total	935	8600.88	282

2016	Jan-Dec	Seed Funding	605	124.12	299
		Private Equity Funding	413	3781.73	113
		Total	1018	3905.85	412
2017	Jan-Dec	Seed Funding	310	73.93	145
		Private Equity Funding	366	10277.47	69
		Debt Funding	11	45.48	1
		Total	687	10396.88	215
2018	Jan-Dec	Seed Funding	126	204.90	29
		Private Equity Funding	172	3523.53	16
		Debt Funding	11	51.48	0
		Total	309	3779.91	45

*Crowd Funding in Jan 2015 by Seeds Crowd Funding Platform for 0.13 Million USD to Nurturey, and by Kikstarter for 0.03 Million USD to Stridalyzer.

**Debt Funding started in June 2017 by Yes Bank to Lendingkart. There are 11 number of deals for debt financing of startups in each year, that is, 2017 and 2018.

Table IV shows the number of funding deals. The mean and standard deviation of the total numbers of deals for the calendar year 15 to 17 has been shown in the given below table. Higher standard deviation indicates that there is more fluctuation in year wise number of deals. The crowd funding was only in 2015 while the debt funding started in 2017 only.

	Number of funding deals for start-ups					
Types of Funding	**2015**	**2016**	**2017**	**2018**	**Mean**	**Standard Deviation**
Seed Funding	498	605	310	126	384.75	182.94
Private Equity Funding	435	413	366	172	346.50	103.78
Crowd Funding	2	0	0	0	0.50	0.86
Debt Funding	0	0	11	11	5.50	5.50
Total	935	1018	687	880.00	737.00	276.00

Table IV. Funding deals

Table V shows funding commitments. The funding commitments in different source as disclosed is summarized in the given table with their mean and standard deviation for the period calendar years 2015-2018. Higher standard deviation indicates that there is more fluctuation in the year wise funding commitments. Crowd funding was only in 2015 while the debt funding started in 2017 only.

	Funds commitment in million USD					
Types of funding	**2015**	**2016**	**2017**	**2018**	**Mean**	**S. Deviation**
Seed funding	164.95	124.12	73.93	204.90	141.98	48.57
Private equity funding	8435.77	3781.73	10277.47	3523.53	6405.63	2926.80
Crowd funding	0.16	0	0	0	0.04	0.07
Debt funding	0	0	45.48	51.48	24.24	24.33
Total	8600.88	3905.85	10396.876	3779.21	6670.70	2898.93

Table V. Funding commitments

In the calendar year 2015 the total number of deals for financing startups were 935 (498 for seed funding, 435 for private equity funding, and 2 were for crowd funding) with total funding commitment of 8600.88 million USD ($164.95 million for seed funding, $ 8435.77 million for private equity placement, and $ 0.16 million out of crowd funding) clocking an average amount of 13.17 million USD per deal ($0.55 million in case of seed funding, $ 23.97 million in case of private equity placement, and $ 0.08 million in case of crowd funding) except the 282 number of deals in which the amount of funding has not been disclosed (for 199 deals in case of seed funding and 83 in case of private equity funding).

Similarly, during the calendar year 2016, 1018 deals were there for financing startups (605 for seed funding, 413 for private equity) with a total funding commitment of 3905.85 million USD ($124.12 million for seed funding, $ 3781.73 million for private equity placement) clocking an average amount of 6.45 million USD per deal ($ 0.41 million in case of seed funding, $ 12.61 million in case of private equity placement) except the 412 number of deals that were there where the amount of funding has not been disclosed (for 299 deals in case of seed funding and 113 in case of private equity funding).

In the calendar year 2017 also 687 deals took place for financing startups (309 for seed funding, 366 for private equity funding and 11 by debt financing) with total funding commitment of 10396.88 million USD ($ 73.93 million for seed funding, $ 10277.47 million for private equity placement, and $ 45.48 million from debt financing) clocking an average amount of 22.22 million USD per deal ($ 0.24 million in case of seed funding, $ 28.08 million in case of private equity placement, and $ 4.83 million by debt funding) except the 232 deals in which the amount of funding has not been disclosed (for 156 deals in case of seed funding, 74 in case of private equity funding, 2 for debt funding).

During the current calendar year 2018 309, a number of deals took place for financing startups (126 for seed funding, 172 for private equity funding, and 11 by debt financing) with total funding commitment of 3379.2 million USD ($ 204.90 million for seed funding, $ 3523.53 million for private equity placement, and $ 51.48 million from debt financing) clocking an average amount of 29.38 million USD per deal ($ 2.11 million in case of seed funding, $ 22.59 million per deal in case of private equity placement, and $ 4.68 million by debt

funding) except the 45 deals in which the amount of funding has not been disclosed (for 29 deals in case of seed funding and 16 deals in case of private equity funding).

The comparative year wise analysis for the total number of deals in different type of funds is depicted in Fig. 3.

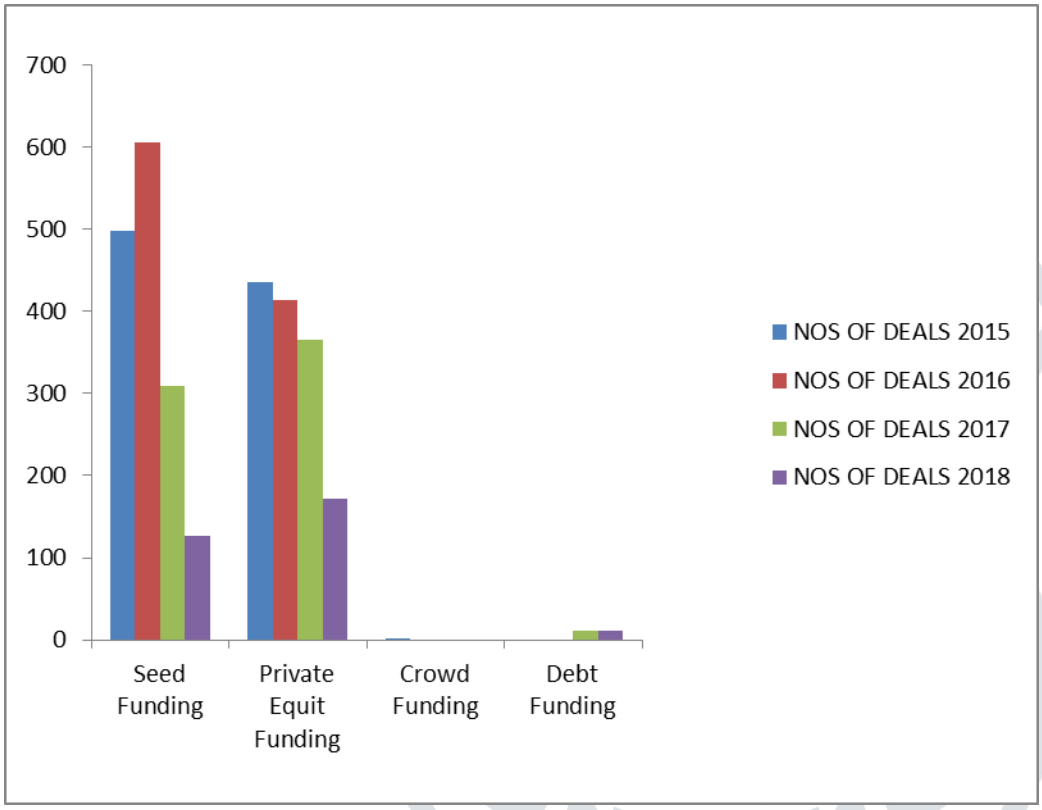

Fig. 3. Number of Deals for Different Types of Funds

The numbers of deals where fund commitment was not disclosed is depicted in Fig. 4.

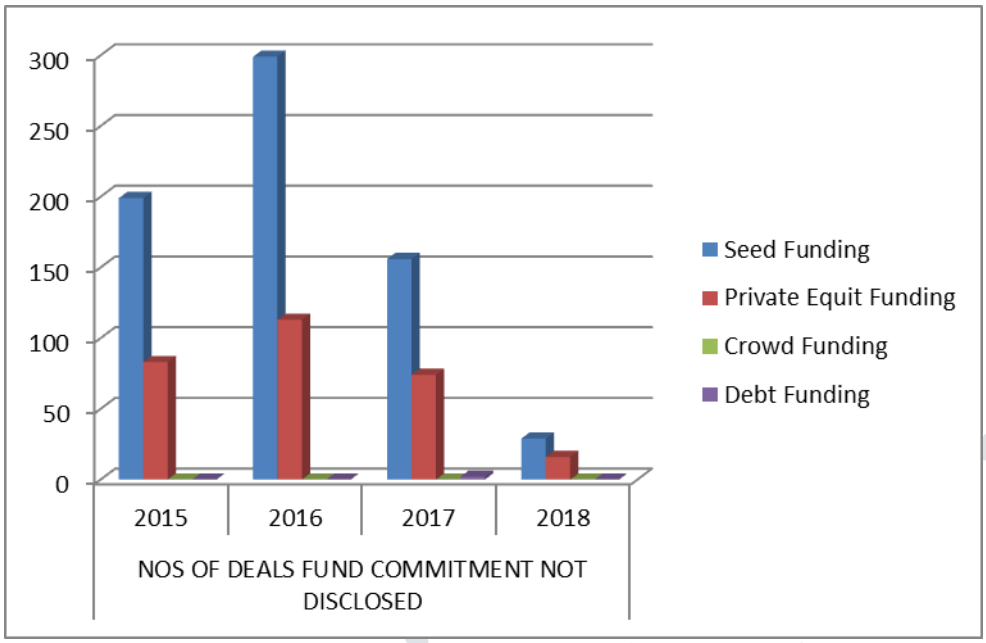

Fig. 4. Numbers of Deals Where Fund Commitment was not disclosed

The comparative analysis for the fund commitment is depicted in Fig. 5.

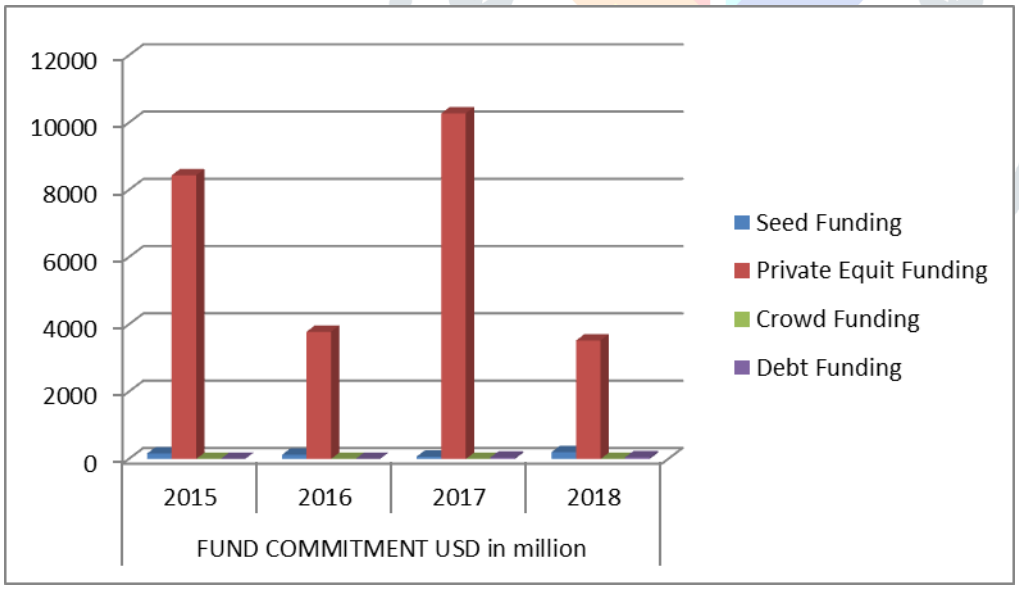

Fig. 5. Fund Commitment Comparison

Research Finding

Analysis of investment and funding deals of internet app and technology based startups reveals these are mostly concentrated in metros and A class cities (Table II and Fig. 1). As indicated in Table III and bar charts it is seen that there is also considerable backing and support with financial commitment deals for startups with

novel unique idea having growth potential, and commercial viability for seed stage as well as for growth stage funding. The funding commitment and the disclosure of amount of funding is more in case of private equity funding than that of seed funding. There is also considerable variation in number of funding deals and funding commitments as indicated with higher standard deviation in Table IV and Table V. The source of crowd funding which was just started in January 2015 soon dwindled in absence of legal and regulator's support while debt financing has just started since June 2017 and is picking up slowly for seed funding and private equity placements. Further, the financial deals without fund commitment have decreased over the years leading thereby synchronizing deals with fund commitment as the case may be.

Conclusion

India is fast becoming a startup hub with substantial young, educated, and working population, germinating new innovative ideas. The new startups in India are mostly centered in metros and "A" class cities need to spread to other parts of India as well. The backing and support of innovative idea having commercial viability with potential to grow is also increasing with pace of time through seed, and private equity mode of funding. SEBI has recognized crowd funding as an alternative source of funding for early stage of startups. If regulated properly however, the policy and guidelines need to be relooked to boost up the crowd funding and debt financing also in the country to scale up further in entrepreneurial development for startups. Furthermore, it is needed to relook and review the compliance for setting up new businesses, the bank lending rates, and R&D spending as indicated in table I while comparing India with world to boost more startups in India.

Limitation and Scope for Further Research

The researcher has analyzed the funding deals and commitments for internet app and technology based startups only on the basis of data captured by Trac.in. The funding deals for other startups are not readily available. There is scope for analyzing funding deals in other startups as well for bringing broader pictures of funding deals for startups in India in other sectors and on overall basis.

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