# CHAPTER 4

## REVIEW OF LITERATURE

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CHAPTER 4
REVIEW OF LITERATURE

4.1 INTRODUCTION:
The research on Venture Capital has been done by the researcher through primary data as well as secondary data. Some of the research review is presented by the researcher which is relevant to the topic of research.

4.2 REVIEW:
Some of the key aspects of research under the review of literature are as follows:

Source: SEBI (Venture Capital funds) Regulations
Source: National venture capital Association

A substantial number of technocrats have worked out strategies to set up shop on their own and capitalize on opportunities.

Venture capitalist mitigate the risk of investing by developing portfolio of young companies in single venture fund. Many times they co invest with other professional venture capital firms. In addition many venture capitalist manage multiple funds simultaneously. For so many years it is noticed that they nurture the growth of high technology and entrepreneurial communities resulting in significant job creation, economic growth and international competitiveness. Companies such as Digital equipment corporation, Apple, Compaq, Intel are some of the famous example which receive venture capital early in their development.

In India venture capital funds are governed by Securities Exchange board of India (SEBI). As per theses guide lines venture capital fund means a fund established in the form of a company or trust, which raises money through loans, donations, and issue of securities or units as the case may be and makes or proposes to make an investment in accordance with these regulations.
4.3 BOOK REVIEW


If we look at entrepreneurs viewpoint one needs to do thorough homework on the profile of funds before approaching venture capitalist. One must also identify projects in which venture capitalist has already invested. It is a matter of concern that entrepreneur must know what are the aspects venture capitalist is looking forward. Going to a venture capitalist is like taking a final exam. Entrepreneurs should be fully prepared. Entrepreneurs should looked at the proposition of scaling the business from day one. If entrepreneur need to scale business from day one and require large money they should head for venture fund but if they need to structure idea into viable financial and marketing plan, then they should look for an angel to help.

Expectations of Venture Capitalist from entrepreneurs- Passion, commitment, multifunctional team, vision, transparency, well researched business plan, energy to turn idea into business. All this is true but focus is more on entrepreneur whereas market product and returns are equally important.

It is also not unusual for venture capital funds to set up an investment screen. The screen is a set of qualitative (sometimes quantitative criterion) criteria that helps venture capital funds companies to quickly decide on whether an investment opportunity warrants further diligence.

Venture capitalist tries to maximize the upside potential of any project. He tries to structure his investment in such manner that he can get benefits of upside potential and he would like to exit at the time when he can get maximum returns on his investment in the project.

4.4 RESEARCH PAPER REVIEW


It’s been observed in India that entrepreneurs are sometimes apprehensive in seeking venture capital funding. It is important to know the role that venture capitalist play. In order to examine this a research was conducted by Graduate school of business faculty members Thomas Hellmann and Manju Pari on a relationship between venture capitalist and internal organization of firms, particularly the building of management team. In the traditional financial relationship investors are involved on the financial side of the business but not on the human resource side. It is the general thinking in the Silicon valley that venture capital makes difference that is more than money. The researchers quantified for the first time that founders are more likely to be replaced by an outsider CEO if they obtain venture capital and that venture backed companies make leadership changes faster than other companies. Even its found that venture capital is particularly important in for attracting CEO to the companies that has no sign of success.

4.5 ARTICLE REVIEW

Source: Evalueserve, IVCA and Venture Intelligence India

The venture capital market in India seems to be getting hot. Research already is showing an interesting phenomenon emerging: most of the US based venture capital firms are investing in start ups and early stage companies in India. Earlier it was difficult for the finance companies to receive private equity or venture capital funding. The scenario began to change after 1990s with the growth of IT companies in India. Indian entrepreneurs, consultants and experts within this ecosystem and based on the analysis of the data from IVCA and venture Intelligence India whether this large investment can actually be absorbed by startup companies and early stage companies.

Trend of venture capitalist

2001-2003 - Venture Capitalist/Private equity becomes risk averse and activity declines:

India came “crashing down” when NASDAQ lost 60% of its value during the second quarter of 2000 and other public markets (including those in India) also declined substantially. During 2001-2003, the Venture Capitalists and Private
equities started investing less money and in more mature companies in an effort to minimize the risks. For example:
(a) The average deal size more than doubled from $4.14 million in 2000 to $8.52 million in 2001
(b) The number of early-stage deals fell sharply from 142 in 2000 to 36 in 2001
(c) Late-stage deals and Private Investments in Public Equity (PIPEquities) declined from 138 in 2000 to 74 in 2001
(d) Investments in Internet-related companies fell from $576 million in 2000 to $49 million in 2001.
This decline broadly continued until 2003.

2004 onwards - Renewed investor interest and activity: As India’s economy started growing at 7%-8% a year, and some sectors, including the services sector and the high-end manufacturing sector, have been growing at 12%-14% a year, investors renewed their interest and started investing again in 2004. The number of deals and the total dollars invested in India started increasing substantially.

Source: Evalueserve

Private equity investment expands beyond IT and ITES: A very important feature of the resurgence in the Private equity activity in India since 2004 has been that the Private equities are no longer focusing only on the IT and the ITES (IT Enabled Services, commonly known as “Business Process Outsourcing” or BPO) sectors. This is partly because the growth in the Indian economy is no longer limited to the IT sector but is now spreading more evenly to sectors such as bio-technology and pharmaceuticals; healthcare and medical tourism; auto-components; travel and tourism; retail; textiles; real estate and infrastructure; entertainment and media; and gems and jewellery.

4.6 WEBSITES REVIEW
Source: www.evalueserve.com
www.venturewoods.org

Lack of Venture Capitalists who have cross-border experience: The real worrisome aspect is that many US-based Venture Capitalists believe they can help
the growth of Indian start-ups, and provide good returns to their own shareholders by:

1. Making decisions by periodically visiting India:
This usually requires conducting frequent conference calls and either the Venture Capitalists flying to India or the executive management of the startup flying to the US every two or three months (for a face-to-face meeting). Since the Indian start-ups require a lot of handholding in the areas mentioned above, this approach is unlikely to be very effective.

2. Sending one of the senior partners in the Venture Capitalist firm to India to set up a subsidiary that can help its portfolio companies:
Although this approach may work, it is likely to fail in instances where the partner has not lived and managed any organization in India for at least two to three years. This is because even Indians living in the US are usually not familiar with the typical business practices in India unless they have had 2-3 years of recent experience on the ground in India.

3. Hiring a junior partner in India:
This approach has three major disadvantages: First, the challenges required by Indian start-ups vary from hiring good talent inside and outside the country to setting up effective and efficient processes. Second, if the partner is fairly junior then this person may not have sufficient experience to advise this start-up effectively, and third, such a junior partner would have a ‘low standing’ within the Venture Capitalist firm and hence, both the junior partner and its portfolio companies in India would feel they are being dictated to by senior partners in the US (who may not understand the environment in India adequately).

4.7 REPORT REVIEW

Source: Indian Private Equity Report 2008
Private equity and venture capital impacted by global slowdown:
All private equity and venture capital investment witnessed a significant decline. It is basically due to absence of mega deals. As this was the time when US mortgage crisis had started taking a heavy toll on Indian and world markets.
The star sectors of 2007, apart from real estate, were unable to attract huge investments in 2008. However, in 2008, except real estate, every other sector faced a drop in investment value. Infrastructure sector received the second highest number of investments though it was lower than 2007. Telecom sector was the biggest loser where, as media and entertainment received almost the same investments in 2007 and 2008. This sector continues to attract Private equity attention, given the strong underlying growth opportunity.

4.8 OVERVIEW OF VARIOUS STUDIES

Source: Vikalpa: Venture capitalist screening criteria by Vinay Kumar and Mohinder N Kaura

Venture capital Industry by V Subbulakshmi

Various studies have traced the development of venture capital funds in India. The details are as follows:

1. Pandey, 1996 with a sample size of nine venture capital firms
   Findings: Identified criteria which are rated high by venture capitalists.

2. Kumar, Asim 1996 with a sample size of 10 venture capital firms.
   Findings: Present a perspective of Indian venture capital industry. Identified problems with regard to policy and taxation.

   Findings: Presents a perspective of venture capital firms from annual publication of IVCA and highlights the general practices as given in venture capital firms' official documents.

4. Pandey, 1998 with a sample size of one venture capital firm.
   Findings: Presents the experience of the largest venture capital firms (TDICI). Documents the problems companies faced in developing the business.

   Findings: Presents factors that restricted the growth of the industry: categories of venture capital companies in India; regulatory framework and tax environment for venture capital firms; features of India's venture capital companies and venture capital funds.

6. Kumar Vinay, 2002 with sample size of 12 venture capital firms
Findings: Studies investment preferences vis-à-vis venture stages and finds that location of the venture and ownership that a venture capitalist can buy are the preferences for later stage and early stage respectively.

Summary

Though various researches are done but working out the criteria from entrepreneurs and venture capitalist point of view over and above business plan is required. A proper action plan is required for entrepreneurs and venture capitalist before screening any project. Qualitative analysis and quantitative analysis both are equally important for venture capital funding. In India venture capital funds are governed by SEBI so even the Venture Capitalist from outside India need to know the entrepreneurs and the growing sectors in India as cross border difference make lot of impact on the funding. Certain specific parameters to be required for venture capitalist especially when there exist lot of apprehension.