Chapter

RESEARCH DESIGN
&
METHODOLOGY
2.0 INTRODUCTION

Starting an enterprise and making it successful is never easy. There are a number of parameters that contribute to its promotion, success or downfall. Product knowledge, risk-taking, experience, integrity, prudence and a clear understanding of the market are among the most sought after qualities of a promoter. However, there are other factors which lie beyond the control of the entrepreneur. Prominent among them is the timely infusion of funds. This is where the venture capitalist comes in with money, business sense and a lot more.

'Venture Capital' is a child of the modern era, but has its fundamentals in the oldest of drives, the entrepreneurial skill. For decades, new ideas and capital remained on a parallel track, discouraging
many entrepreneurs and killed thousands of potentially great business ideas. Then, had come the concept of venture capital which a fund-based financial service, had emerged the world over to fill gaps in the conventional financial system, focusing on new technologies and support to small, and medium-sized enterprises in the manufacturing and service sectors.

'Venture Capital' is long-term risk capital to finance high technology projects involves high risk but at the same time has strong growth potential. Venture capitalists (VCs) pool their resources as well as to assist new entrepreneurs in the early stages of the project. Once the project reaches the stage of profitability, they sell their equity holdings at high premium to yield maximum capital gains as a reward for taking higher risks for supplying seed capital.

2.1 SELECT REVIEW OF THEORETICAL AND EMPIRICAL LITERATURE

'Venture Capital' has become the major topic of discussion and is attracting more attention at present than ever before due to fast changing technology, emergence of new technology industries highly competitive global markets. There is a plethora of literature on venture capital, since many studies have been undertaken in the past to assess the role of venture capital financing in industrial development. Hence, in this section, an attempt is made to review the existing literature with a view to formulating the problem and meaningfully setting objectives and hypotheses for the present study.
The first study on 'venture capital' was in the works of Huntsman and Hoban (1980) who examined 110 investments by three venture capital firms over the period 1960-75. But, the study did not provide formal tests of superiority or inferiority of their returns. The study concluded that venture capital success was highly dependent on diversified investments.

In a comparative study between venture capital funds and mutual funds, Martin and Petty (1983) found that on average venture capital funds were more riskier than their mutual fund counterparts, and were not dominated on an average higher returns.

Tyebjee and Bruno (1984) conducted a study to ascertain the factors that influenced the investment evaluation of venture capital funds in the U.S. by analyzing rating of 90 deals by venture capital funds. They concluded the perceived risk was influenced by managerial capabilities and the resistance to environmental threat, while the expected return was strongly influenced by market attractiveness, followed by a highly differentiated product whereas cash-out potential was observed as not having any impact on the perceived risk and the expected return of a venture.

Ian Macmillan, et.al. (1985) provided the most important criteria that the venture capitalist would use while screening new venture proposals. The study enriched the mutual fund knowledge in the areas of risk assessment and management of venture capital fund. Since the study identified categories of venture capitalists that emphasize certain
criteria, entrepreneurs could choose the best category which goes with their idea.

Ronstadt (1986) examined the reasons why entrepreneurs exit early from their careers and provided evidence which suggests that at least some may have the potential for undertaking further ventures. Whilst this provides general evidence of the reasons for entrepreneurial exit, there is a need to examine more directly the implications for venture capitalists.

Ian Macmillan, et al. (1987) studied patterns within successful and unsuccessful ventures, scoring a point in highlighting how successful ventures are distinguished from unsuccessful ventures. The difference between earlier study and this study is that this study requested a posteriori ratings and not a priori.

Robinson Jr. (1987) examined the venture capital industry in the U.S. with the intention to help compare the orientation of individual venture capital firms on four strategic dimensions with that of the industry as a whole. While studying the goals and priorities of the venture capital firms, they identified three goals and priorities which did not show any difference or change over a period of time.

Chiampou and Kallett, (1988) in their study examined private venture capital funds, classifying them into two groups - one group consisted of more than 6-year old funds and the other newer funds. They found that the investment returns of the 35 mature funds over the period
1978-87 averaged 24.4 per cent per annum with a standard deviation of 51.2 per cent, whereas the younger firms performed much more poorly with the return averaging only 5.4 per cent over their shorter lives. However, the results for the younger funds probably reflect two biases in the sample. First, venture capital returns for the broad sample were lower in the middle years of the 1980s than in the earlier part of the sample, and the newer firms' returns heavily reflected that period. Second, it is difficult to measure the value of relatively recent investments since their values are unlikely to have been realized through merger or public offering or other events. Their values are often being reflected at cost rather than at market value. In contrast the older firms have more investments whose values are marked to market.

Iyer, K\(^9\) (1989) in his study underlined the tremendous potential of the Indian venture capital industry, suggested that the country very badly needs such capital in adequate measure to nourish its substantial pool of potential technocratic entrepreneurs. However, it was rightly stressed that venture capital industry in India could be built-up only on the basis of sound expertise, knowledge and track record so as to be able to attract investment funds from the general public as in the U.S. and Europe.

Barney, et.al.,\(^10\) (1989) examined the influences on the degree to which elaborate governance mechanisms were used by venture capitalists and found that high agency-risks and business-risks were associated with more elaborate governance structures.
Ramesh, S. (1989) reviewed the existing venture capital industry in India and brought out that structural changes presently taking place in Indian economy which in turn are making the environment more conducive for venture capital investment across sectors of economy. Enterprising people from the northern states of India have to exploit these opportunities to their best advantage. Innovative and dynamic people working in fast growing medium, and large-scale enterprises are more suitable for taking-up such projects.

Bhattacharya, S. (1989) research work formulated the requirements of successful venture capital financing in India in the light of experience in the U.S. and some of the South-east Asian countries, and identified that the origin of venture capital activity could be traced to the rise of merchant banks in the U.K.

Sahlinan (1990) examined the nature of the principal-agent relationship between mutual-fund providers and venture-capitalists. He visualized why conflicts exist and discussed the mechanisms to deal with the same. There are conflicts between the investors and the venture capitalists as well as between managers of portfolio firms and venture capitalists. He demonstrated that there is a similarity in the mechanisms for addressing such conflicts and relates agency-costs in a venture capital context to agency issues in other settings.

Amit, et.al. (1990) developed a model which examines the nature of the adverse selection problem for venture capitalists. The general
assumption is made that the entrepreneur knows his own ability level, whereas the venture capitalist does not. In an initial case it is assumed that the entrepreneur is risk-neutral and no new investment is needed.

Cottrell, R.L., 16 (1990) in his article stressed that India could not hope to develop a private sector venture capital industry in isolation from the evolution of wider, liberated equity markets. India's attempts to create a private sector venture capital capability 'within a vacuum' have a limited chance of success. Only as part of the development of more far-reaching policies could it evolve.

Eldrige, W.D18 (1991) in their report, identified various external factors that affect the prospering of venture capital subsidiary in the short-term as fiscal regime, increasing ability of the investing public to rely on financial statements, the growing or existing stock market as economic policy matter. They suggested that government should pay attention to financial gain tax, financial statement reliability, improving/tightening the regulatory framework and a growing stock market as measures for attracting development financial institutions in India.

Meggisson and Weiss17 (1991) acknowledged the importance of reputation and certification of venture capitalist role for the success or otherwise of initial public offerings. They found significantly less under-pricing in issues with venture capital banking which, in keeping with other studies, emphasized that the quality of the underwriter or auditor could influence pricing of initial public offerings.
Sagari and Guidotti,\textsuperscript{18} (1991) listed four exit routes available with the venture capitalists as initial public offerings, acquisition by another company, re-purchase of the venture capitalist's shares by the investee company, and secondary purchase of venture inventor's shares by a third party.

Ruhnka, et al.,\textsuperscript{18} (1992) investigated the strategies employed by 80 venture capital firms to deal with the 'living dead' investments in their portfolios — ventures that were self-sustaining but failed to achieve levels of growth or profitability necessary for attractive exists such as IPO or acquisition. Venture managers were able to achieve a successful turnaround or exit in 55.9 per cent of living dead situations, regardless of the age of the venture capital firms, their size or the relative availability of investor personnel for monitoring investees. From the influence of this result, they concluded that causal factors were outside venture capital control.

Hustedde and Pulver\textsuperscript{20} (1992) examined the role of different types of intermediaries in securing venture funds for their entrepreneurial clients. Their results showed that entrepreneurs who failed to seek advice were more likely to be less successful in acquiring equity finance, but those using bankers or public agencies were likely to increase their chances of failure. While providing interesting insights, the study focused primarily on entrepreneurs seeking finance for early stage projects.
Landstrom\textsuperscript{21}(1992) found that the involvement of business angels in monitoring their investments would vary according to the level of agency-risk and suggests that the agency framework is inappropriate. He argued that the assumptions applicable in agency theory, which is concerned with rational economic maximizing behaviour, asymmetric information, and conflicting objectives, are not valid in the case of informal investors since they are more motivated by non-economic factors, have a desire to make a value-added contribution, and are able to mitigate asymmetric information problems through prior relationships and close involvement in the business.

Joseph Rosenstein, et.al.\textsuperscript{22} (1992) examined the board size and how the size varied in different categories of venture capitalists after the first investment. It also studied the board composition and control. Finally, the overall value-added was inferred based on how much time was spent by the venture capitalist and usefulness of such time.

Norten and Tennebaum,\textsuperscript{23} (1993) examined the link between financing structures, financing stages and venture capitalists characteristics. They found that smaller, less-diversified venture capitalists made greater use of ordinary equity instruments, but the use of preference shares did not increase in higher risk (early) stage investments nor did investors who were subject to greater amounts of unsystematic-risk make greater use of preferred instruments.
Ray and Turpin's, 24 (1993) empirical study was a landmark in analyzing the investment evaluation criteria used by venture capital funds. The entrepreneur's personality and experience were found to be the most important aspects of evaluation and financial considerations as the least important in venture investment evaluation.

Mohinder, K and Chandra, S., 25 (1993) in their research endeavour to deal with the development of venture capital financing, discussed the role of venture capital in financing high-tech projects. The paper attempted to trace the development of its growth in India and abroad. It also described the features of some leading venture capital funds and suggested ways for the healthy growth of the venture capital financing industry in India.

Gupta, S.L., 26 (1993) conducted a research with an eye to explore the need and vast scope for venture capital financing in order to augment India's technical progress. The paper also examined the improper application of the concept of venture capital in India. It made suggestions for tapping the full potential of venture capital financing in India after highlighting the existing fiscal and institutional limitations on the promotion of venture capital.

Fried, V.H. and Hisrich, R.D., 27 (1994) directed their research efforts towards developing a model of the venture capital investment decision-making process. They suggested that venture capitalists use three generic criterion for screening investments – the viability and novelty
of the project; its integrity, track-record and leadership skills of management; and its possibility for high returns and an exist-before proceeding to detailed evaluation.

Mc Nally,^2^ (1994) provided an analysis of the role of corporations both as direct (i.e. through corporate venturing) and indirect (i.e. through funds) investors in venture capital, and suggested that problems relating to mis-matches in expectations between corporations and other parties in relation to investment time, scale, and control mechanisms in particular, had resulted in major difficulties in the development of this source of finance.

Lerner^2^ (1994) identified the alternative ways in which venture capitalists reduce the problems of adverse selection bought-out when they tend to invest with other venture capitalists. He investigated more than 600 rounds of investment in bio-technology firms. He found that syndication is common from the first investment round of investing, a fact he argued, is a part of the screening process. He commented that venture capitalists are more comfortable with a deal when other venture capitalists of similar experience are willing to invest as well.

Fiet^3^ (1995) found that formal venture capitalists attach more importance to market-risk than agency-risk and vice-versa and argues that formal venture capitalists are less concerned about agency-risk because they protect themselves from it through stringent contracting which enables them to replace under-performing entrepreneurs. Informal
venture capitalists that screen very few deals per year have access to comparatively limited information and place more emphasis on agency-risk that is finding the 'right' entrepreneurs who will be able to address market-risk.

Kumar, N. (1995) in his study observed that venture capital industry in India is a fast emerging financial services industry. It is long-term risk capital meant to finance high technology projects involving high risk. The government has allowed overseas venture capital investments in India. The ministry of finance in 1995 allowed off-shore investors who may invest in approved domestic venture capital funds.

Mukhopadhayay, D. (1995) acknowledged the venture capital industry in India at the take-off stage. The study covered the history, operation and management of venture capital funds, and suggested a set of policy measures required for their effective functioning in India.

Deo, M. (1996) research efforts directed toward examination of importance of venture capital industry, bought out that venture capital is a long-term equity investment in business that displays potentials for significant growth and return. In a short span of less than a decade, venture capital financing has made considerable strides in the Indian business scenario. The basic features of venture capital financing, eligible activities, stages of financing and the problems and prospects in Indian scenario have all been discussed in his study.
Pandey, I.M., (1996) conducted a pioneering work in the Indian venture capital industry, aiming at ascertaining the investment evaluation criteria used by Indian venture capitalists. The study, giving a background of venture capital, highlighted its strategic role in the development of technology, innovative entrepreneurship and small enterprises in India. He also examined the practices and policies of the venture capital firms in India.

Sapienza and Korsgaard, (1996) examined the entrepreneur – investor relations. They carried out two studies: a simulation study using students, and a survey questionnaire study of venture capital partners. Their principle conclusion was that timely feedback promoted positive relations between entrepreneurs and investors. They suggested that entrepreneurs should yield a level of control and share information so that investors would eschew monitoring, and trust and support the entrepreneurs.

Sweeting, R.C. and Wang, C.F., (1997) focussed their work on handling of post-investment investor-investee relationships. Though their research was limited to only one large venture capital firm, they did observe that it was possible to run it profitable and successfully with a hands-off approach.

Gomper, et.al. (1998) studied the growth of venture capital funding in the U.S. between 1972-94. A list of industry-specific and macro-economic factors that had influenced both the demand and supply of
venture funds was outlined. An attempt was made to identify the importance of these factors using unique data on venture capital commitments in the United States. A series of reduced-form, regressions suggested that tax rates, rule changes in federal pension law and real growth in gross domestic product seemed particularly important predictors of commitments. The success of venture capital companies at raising funds was also examined.

Pramanik, A.K. (1998) in his study maintained that lack of financing was inhibiting the process of industrial development in India. So the Indian capital market emerged as a major source of finance – several new institutions have appeared on the financial scene and venture capital companies have joined to expand the range of financial services. He suggested that venture capital companies should try to popularize the concept of venture financing through publicity as there is poor awareness about the availability of venture capital financing. Further, he expressed his expectations that venture capital activity running at full stream could speed-up the process of industrial development in India.

Black and Gilson, (1998) examined the importance of well-developed stock markets and Initial Public Offerings (IPOs) for venture capital financing. The empirical study tested the significance of IPOs over time in the U.S.

Mike Wright and Ken Robbie, (1998) conducted a study to review and synthesise a wide body of research relating to venture capital
and thence to identify possible directions for future research. The study analysed the issues involved in venture capital at two inter-related levels i.e., from the industry/market level and the venture capital firm-level. They concluded that venture capital provided a potentially rich research agenda for researchers in the accounting and finance area.

Bernard’s, 41 (1998) research analysis evaluated the hows and the whys a software entrepreneur should keep in mind before approaching a venture capitalist. He suggested that the choice of the venture capital was right, but the time was not right. Timing is everything in this business that needs to be taken care of.

Pandey, I.M., 42 (1998) in another attempt investigated the process of developing venture capital in India. The detailed case analysis of TDICL revealed that the steps involved in the process of developing venture capital activity in India are impetus, internal context, external context and sustainability.

Gautam Vashisht, 43 (1999) in his study provided the structuring and launching venture capital funds. He concluded that a more efficient vehicle for structuring venture capital funds is limited liability partnership (LLP), which is both tax efficient and simple to operate. Enactment of LLP in India would also provide level playing field to domestic venture capital funds vis-a-vis off-shore/private equity funds.

Gompers and Lerner, 44 (1999) in their study provided excellent examples on the venture capitalist-entrepreneur relationship based on
agency theory. They argued that venture capitalists stage their investments in new ventures because of a concern that entrepreneurs with inside information will continue spending investor money even when faced with losing prospects because they stand personally to lose salary, perks and reputation. Further, the representation of venture capitalists, unlike outside board members, increases around the time of CEO turnover. They also find that geographic proximity is important for venture capital board members.

Mishra, R.K. (1999) in his paper dealt with the financial viability and performance of a venture capital limited of the pharmaceutical company, M/S Jayaprada Clonetech Private Limited in Andhra Pradesh. The study concluded that the demand for the product is quite good and the indigenous requirement is being met by imports.

Pandey, I.M and Shantanu Dutta, (1999) studied the development of venture capital in India. Their discussion comprising in-depth case studies covered several issues, such as initiation of venture capital activity, the sources of venture capital fund, the profile of funds, investment strategy and evaluation, and the value addition by venture capital firms. They concluded that in terms of sources of funds there is a difference between India and other developed countries.

Rajeev Mukhija, (1999) in his paper outlined the policy and legal framework for venture capital industry in India. He examined two such policy instruments viz., 1987 Guidelines and the 1996 SEBI/CBDT
Compliance Rules for the operation of venture funds. Finally, the study concluded that the efficient exit mechanism is desirable to ensure that dis-investment by venture investors is carried out at a price matching the real net-worth of the investee company as per exit plan envisaged at the time of investment. This will increase the confidence level of the venture capitalist and other investors giving boost to the venture capital investment in India and making them an engine for growth of the economy.

Shashank Rajurkar, 48 (1999) made a study relating to the issues facing the Indian venture capital industry. The issues - fund limitations, lack of incentives, domestic versus overseas competitions on funds, anomalies in SEBI and CBDT Regulations, sweat equity and employee stock-option plans (ESOPs), absence of angel investors, limitations on exit mechanism - are discussed. Notwithstanding these issues faced by the Indian venture capital industry today, the industry are surging ahead. The study suggested the vibrancy of the Indian entrepreneurship, market opportunities for small, and medium-ventures and encouragement by the government, gave rise to optimism on the future of venture capital in India.

Singhvi, L.K 49 (1999), examined the growth of venture capital industry in India, observed that it is in its growth phase. Large number of domestic off-shore and private equity funds has been continuously increasing their activity in venture capital industry. The government of India and SEBI are seriously making attempts to facilitate more and more venture capital funds to flow into the country. Economic and securities
market reforms are ideally placed to attract new venture capitalists within the country and from abroad. Finally, the study concluded that the venture capital industry is poised for tremendous growth in the years to come.

Vishnu Varshney, 60 (1999) in his paper addressed the venture financing methodology, value addition and dis-investment mechanisms. The study concluded that the aspects of venture capital industry especially value addition and dis-investment mechanism, may have far-reaching implications for the development of the whole venture capital industry.

Hsu61 (2000) in his study compared a group of venture capital-backed start-ups with a control group of start-ups that obtained government funding through the United States Small Business Innovative Research (SBIR) programme, which does not impact ownership or governance. The study concluded that venture capital changed the path of funded projects by altering the commercialization strategy and making the firm more sensitive to the business environment.

Kortum and Lerner,62 (2000) investigated trends in patent rates as a measure of innovation. According to their paper on average each dollar invested by venture capitals contributed to the rate of patents 3 to 4 times more than corporate R&D. Statistical analysis revealed that the rate of U.S patent-filing was correlated with earlier-stage venture capital disbursements, when controlling for corporate research and development expenditures. Moreover, from the late 1970s to the mid – 1990s venture
capital represented only 3 per cent of corporate R&Ds, but responsible for 10 per cent to 12 per cent of privately-funded innovation.

Moon-Kyum Kim, 53 (2000) have examined the role of Korean venture capital industry in recent venture boom years. Specific issues covered by the study included the progress of the venture capital industry, government's support-system and future prospects. The study concluded that the institutional investors are still reluctant to make investments in venture capital funds because of the low rate of return and high-risk pertaining to the venture business.

Leslie A. Jeng, Philippe C. Wells, 54 (2000) in their study analysed the determinants of venture capital for a sample of 21 countries. In particular, they considered the importance of initial public offerings (IPOs), gross domestic product (GDP), and market capitalization growth, labour market rigidities, accounting standards, private pension funds and government programmes. They found that IPOs were the strongest driver of venture capital investing. Private pension fund levels were a significant determinant over time but not across countries. Surprisingly, GDP and market capitalization growth were not significant. Government policies could have a strong impact, both by setting the regulatory stage and by galvanizing investment during down-turns.

Shepherd and Zacharakis, 56 (2001) emphasized the necessity of a balance between trust and control in the venture capital–entrepreneur relationship. They proposed that the entrepreneur could "build trust with
the venture capital and vice-versa by signaling commitment and consistency, being fair and just, obtaining a good fit with one's partner, and with frequent and open communication". They regarded their study as a counter weight to economic approaches like agency theory in which control is emphasized.

Raul, R.K.* (2001) in his paper delineated the reasons of recent spurt in venture capital, types of venture capitalists, parameters of venture capital financing, present trends and stages of venture capital financing. At present listing guidelines provide that at least 60 per cent of issued capital, with exceptions, should be offered to the public. This rule should be relaxed for venture capital undertakings. Buy-back of shares under section—77A in the Companies Act, 1956 could facilitate the exit option of venture capitalists. These suggestions could help to build an extremely strong and vibrant venture capital industry in the country which could ultimately create generation of industries, new employment and wealth. The policy measures would be such that it would not kill the goose that is yet to lay the golden eggs.

Vinay Kumar, 57 (2002) in his study endeavored to highlight issues, practices and perspectives of Indian venture capital industry. The study aimed to understanding the practices followed by the industry for screening ventures. These screening criteria are generally used to identify the successful ventures. Finally, the study attempted to come-up with appropriate suggestions for venture capitalists, for entrepreneurs who
seek venture capital and public policy pertaining to venture capital for the development of Indian venture capital industry.

Shane and Stuart,\textsuperscript{68} (2002) studied the social capital of company founders. New ventures with founders having direct and indirect relationships with venture investors were more likely to receive venture funding and are less likely to fail. They concluded that founder social capital represents an important endowment for early-stage organization, either the decision criteria is partially subjective or they objectively place value on established relationship.

Nagendra V. Chowdary et.al.\textsuperscript{69}(2002) Studied the developments in the present venture capital industry in India. They dealt with various issues relating to venture capital and provided practical insights wherever relevant. They concluded how a venture capitalist works, how to prepare a business plan and how to approach a venture capitalist for assistance. They also examined a unique Indian flavor by tracking the evolution of the venture capital industry in India and the contemporary legal framework under which it operates.

Neel Kant Sharma\textsuperscript{60} (2002) studied venture capital as a catalyst in the growth of the Indian economy. He examined the development of venture capital industries in which investment had been made and also the reasons for the poor growth of venture capital industry in India. The study recommended alternative strategies to venture capitalists for
effective management of venture capital funds in India and suggested ways to develop venture capital market in India.

Pandey, I.M et al. (2003) examined the aspects relating to entrepreneurship development and venture capital. Entrepreneurship helps creating innovative enterprises which provide foundation for building a nation's competitiveness. Venture capitalists provide risk capital and facilitate the development of entrepreneurship. The study concluded that venture capital is capable of creating a facilitating environment to build entrepreneurship culture and help entrepreneurship develop as a preferred career option.

Mishra, A.K. (2004) in his study mentioned that the Indian venture capital industry has grown substantially over the years and acquired its own distinct character. Focusing on information technology sector in the early years, the venture capitalists have diversified into areas like call center, business process outsourcing (BPO) and commodity businesses. With the dotcom bust taking its toll, the current venture capital landscape is not very encouraging. However, Indian markets continued to be a hot destination and it is likely that venture capital investments would increase in the forthcoming years.

Sanjay Anandaram, (2004) was of the opinion that venture capital in India would have to become globalized. Local venture capital participants would have to forge links and relationships with international players and vice versa. He suggested that with the right mix of regulatory
changes, fund managers and local capital, it is possible to see a burgeoning venture capital business in India. In addition, over the next several years, he believed, a robust eco-system required to foster and engender entrepreneurship will emerge.

Nagayya D* (2005), in his article, reviewed the development of venture capital funds (VCFs) and venture capital investments (VCIs) in India. The Indian environment of VCFs, particularly through institutional sources like Industrial Development Bank of India (IDBI) and Small Industries Development Bank of India (SIDBI), had been presented in detail. To make the program dynamic, to meet the entrepreneurial interests in the small, and medium enterprises sector, changes taking place were covered in depth. The role of the nodal agency viz., Securities and Exchange Board of India (SEBI) in supervising and monitoring the functioning of venture capital funds was highlighted. The involvement of the Indian Venture Capital Association (IVCA) in pursuing with the government of India for a revision of guidelines for VCFs at different periods had been recapitulated.

Harini Mittal (2006) expressed that the Indian venture capital industry had grown over the years. The capital market and venture capital needs would to be harmonized. There are a few sectors, besides information technology, in which India is making rapid strides. The service sector, especially business process outsourcing (BPO), is seeking a lot of momentum. Semi-conductor business also is a field that holds a lot of
promise. Telecom sector is a burgeoning field with a sizeable market within the country itself. Other potential sectors are life sciences (pharmaceuticals and bio-technology), retailing, media and entertainment. Venture capitalists are expecting a lot of activity for themselves in these sectors. But much needs to be done on the exit mechanism front to encourage the flow of venture funds.

2.3 STATEMENT OF THE PROBLEM

Technology and knowledge-based ideas like information technology, bio-technology, bio-informatics, electronics, medical, healthcare, media and entertainment and the like will be the growth drivers in the global economy in 21st Century. They require equity capital as well as managerial assistance to turn these ideas into viable enterprises. However, these ventures lack access to existing equity markets due to great uncertainty and long gestation periods. The only way to finance such ideas is ‘venture capital’. Thus, these sun-rise-industries supported by ‘venture capital’ can be propelled into a powerful engine of economic growth and wealth creation in sustainable manner.

Given the inherent strengths by way of its human capital, technical skills, cost competitive manpower, research and entrepreneurship, India can unleash a revolution of wealth creation leading to employment generation and rapid economic growth. What is needed is ‘venture capital’. It is already a decade-and-a-half since the venture capital industry started taking roots in India. Still we hear that the industry is
nascent and dormant to a great extent. But there are economies elsewhere in the world that have shown remarkable progress through venture capital in the same period.

Therefore, it becomes appropriate for any study to inquire into the experiences of venture capital firms. Which would enable them to reshape their goals and redesign strategies and evolve suitable criteria to identify successful investment opportunities? Further the success of an enterprise funded by venture capital is dependent on the relationship it enjoys with venture capitalist. The venture capitalist should, therefore involve himself continuously in venture capital-funded enterprises not only in the pre-investment but also in the post-investment period for mutual benefit.

2.4 NEED FOR THE STUDY

From the review of literature it can be observed that various studies have been carried-out by academicians, researchers, organizations and others both in India and abroad on venture capital financing and its ramifications. In the Indian context, these studies are either macro in nature covering the entire country or micro confined to a few areas of venture capital companies. Studies covering all dimensions of venture capital companies at regional level are very a few and far between as compared to studies at the national level. It is also understood that studies so far made have covered many venture capital companies lacking focus on specificity. Exclusive studies on specific venture capital
companies are scanty. Further, research studies made on venture capital finance confirming to State Level Venture Capital Companies are scanty.

Hence, there is a need to conduct an in-depth study to evaluate the performance of venture capital companies operating in different states of the country. Therefore, the present research study, "Venture Capital: A Study of Andhra Pradesh Industrial Development Corporation Venture Capital Limited (APIDC VCL)", a state level venture capital company in the state of Andhra Pradesh, is an attempt in this direction. It is hoped that the present study will be a gap-filling one and an useful addition to the existing literature on the subject.

2.5 OBJECTIVES OF THE STUDY

The study specially aims at realizing the following objectives:

- to review the origin, growth and development of venture capital industry in India;
- to evaluate the performance of APIDC VCL in venture capital financing;
- to study the venture capital process of APIDC VCL in portfolio enterprises;
- to appraise the financial performance of portfolio enterprises; and
- to offer suitable suggestions for the better performance of APIDC VCL and its portfolio enterprises.
2.6 HYPOTHESES

The following null hypotheses are posited for testing in the study:

- There is no gap between gross sanctions and disbursements to venture capital-funded enterprises across industrial categories.
- There is no significant difference in disbursements between stages of investments across industrial categories.
- There is no significant difference in disbursements through different instruments across sectors.
- There is no significant difference between portfolio enterprises across sectors as to magnitudes of current ratios.

2.7 SAMPLE DESIGN

APIDC VCL was promoted by Andhra Pradesh Industrial Development Corporation (APIDC), a government of Andhra Pradesh Enterprise, on 29th August, 1989 and it commenced operations from April, 1990. But in 1994, the company was taken over by Dynam Venture East Private Limited with majority shareholding of 51 per cent while the rest of 49 per cent held by APIDC. Since then, APIDC VCL became a joint venture of Dynam Venture East Private Limited and APIDC.

The present study aims at evaluating the performance of venture capital industry from two dimensions: firstly, evaluation of the performance of APIDC VCL which is a state level Venture Capital Funding Organization in Andhra Pradesh; and funded enterprises of APIDC VCL form the other dimension of the study.
To study the first dimension, sampling is not required as it relates to only one venture capital funding company in Andhra Pradesh i.e. APIDC VCL. In order to study the second dimension i.e. financial appraisal of select funded-companies of APIDC VCL operating in Andhra Pradesh, the list of funded-companies was obtained from the records of APIDC VCL. As on 31st March, 2006, the total number of units funded by APIDC VCL was 18, consisting 11 units operating in Andhra Pradesh, and the rest of 7 in other States, 4 in Tamil Nadu, 1 each in Karnataka, Maharastra and West Bengal.

Since the present study is confined to the State of Andhra Pradesh, the 7 venture capital-funded enterprises operating in other states are excluded from its purview. Hence, the universe for the study constitutes all the 11 venture capital-funded enterprises operating in the state of Andhra Pradesh. All these 11 venture capital-funded enterprises are categorized into 5 different industrial groups [See Table 2.1].

Table 2.1
SAMPLE DESIGN OF VENTURE CAPITAL-FUNDED ENTERPRISES OF APIDC VCL

<table>
<thead>
<tr>
<th>S. No.</th>
<th>Industry Group</th>
<th>Number of units in A.P.</th>
<th>Number of Sample units</th>
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</thead>
<tbody>
<tr>
<td>1</td>
<td>Information technology</td>
<td>04</td>
<td>02</td>
</tr>
<tr>
<td>2</td>
<td>Industrial products and electronics</td>
<td>02</td>
<td>00</td>
</tr>
<tr>
<td>3</td>
<td>Pharmaceuticals and chemicals</td>
<td>02</td>
<td>02</td>
</tr>
<tr>
<td>4.</td>
<td>Services</td>
<td>02</td>
<td>01</td>
</tr>
<tr>
<td>5.</td>
<td>Food processing</td>
<td>01</td>
<td>01</td>
</tr>
<tr>
<td>TOTAL</td>
<td></td>
<td>11</td>
<td>06</td>
</tr>
</tbody>
</table>

Source: Compiled from the records of APIDC VCL, Hyderabad.
Of these 11 venture capital-funded enterprises of APIDC VCL, 6 units have responded positively and others declined to part with the information despite the researcher's repeated attempts. The sample, therefore, represents 6 venture capital-funded enterprises across 5 industrial groups, forming more than 50 per cent of the universe.

2.8 PERIOD OF THE STUDY

APIDC VCL came into existence in 1989 as a state government enterprise in the field of venture capital financing. From 1994 onwards, it became a joint venture with Dynam Venture East Private Limited, which holds 51 per cent share capital in APIDC VCL. The present study relates to the post-privatization period operations of APIDC VCL i.e., a 12-year period from 1994-95 to 2005-2006.

2.9 SCOPE OF THE STUDY

The present study is a micro-level and area-specific study. The scope of the study is confined to the objectives of the study as outlined earlier. The present study is limited to the APIDC VCL's portfolio enterprises operating in Andhra Pradesh only and excludes enterprises outside the state.

2.10 DATA BASES

The data for the study have been collected both from primary and secondary sources. The primary data relating to venture capital finance have been collected through structured questionnaire canvassed among the executives of venture capital-funded enterprises of APIDC VCL. The
secondary data have been gathered from various sources such as official reports, various websites, brochures, annual reports, journals, and magazines, various published and unpublished studies.

2.11 TOOLS OF ANALYSIS

The collected data through the questionnaire are scrutinized so as to appraise the quantitative and qualitative aspects of the data before passing them for tabulation. After tabulation of data, the data are analyzed by using the appropriate statistical tools such as averages, percentages, linear growth rates and hypotheses formulated are tested using t-test and ANOVA test. Financial Management tools such as ratio analysis and capital budgeting techniques were also used.

2.12 CHAPTERISATION

The thesis is organized into eight chapters, the description of which is given in what follows

Chapter – 1 : Venture Capital - Theoretical Framework

Chapter – 2 : Research Design and Methodology

Chapter – 3 : Venture Capital Industry in India – An Overview

Chapter – 4 : APIDC Venture Capital Limited – A Profile

Chapter – 5 : Performance Evaluation of APIDC VCL

Chapter – 6 : Venture Capital Process of APIDC VCL in Portfolio Enterprises


Chapter – 8 : Summary of Findings, Conclusions, and Suggestions.
REFERENCES


