CAIA Insights

The Rise of India's Private Equity Market

CAIA ASSOCIATION®

Executive Summary

Capital formation across the globe is shifting away from traditional public equity and debt and into private markets. As a result, alternative investments—particularly private equity and venture capital (PEVC) investments—are more accessible than ever and are now recognized as the ideal vehicles for growth-minded investors to gain exposure to the world's most promising and innovative companies.

As CAIA Association highlighted in our 2020 report, The Next Decade of Alternative Investments, CAIA Members surveyed worldwide predict that by 2025 alternatives will constitute between 18-24% of the global investible market.

It's no surprise, then, that the conditions supporting this worldwide transition have made a bold mark in India, where private sector growth and innovation are reaching new heights.

CAIA Association, together with our data partner, Venture Intelligence, India's leading private markets data provider, invite the local investment community, along with investors across the world, to use this report to better understand the current state of the PEVC industry in India.

As data throughout this report reveals, India has reached a pivotal arc in its economic growth story, now offering private markets investors—general partners and limited partners alike—genuine opportunities to achieve both alpha and impact in the world's fastest growing major economy.

We hope that the research included here helps to spark greater interest and conversation around India's bright future and the role that our global industry can play in supporting its continued progress.

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Introduction
The CAIA View: Alpha, Beta, India

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The CAIA View: Alpha, Beta, India

Nothing in India happens on a small scale. A population of 1.4 billion people holds the promise of scale, but the real story is a rising middle class of consumers and one of the world's youngest populations, with almost 30% of citizenry under the age of 14.

Government-led investment in infrastructure has provided a downpayment on what is expected to be urbanization on a grand scale. The scene on the ground in India can sometimes be seen as chaotic, but there is a cadence and direction to this giant nation that is too big to ignore.

As most of the world emerges from the aftermath of COVID-19, supply chains are fitfully lurching back into action, and we are reminded that the good old-fashioned bull market has never seen a crisis that it didn't love. The depths of Q1 2020 are now being followed by record public equity market gains, extraordinary YoY growth in GDP, and impressive job growth across almost every sector of the economy. For the moment, central bankers remain accommodative to this risk-on trade.

"Price discovery is a bit more art than science, and arguably less subject to the volatility that is driven by the emotion of the public investor."

Ben Graham talked about the public equity markets being a voting machine in the short-term and more of a weighing machine over time, when the latter is able to fully calibrate the market value of a public company. If he were alive today, he might have to append that analysis with an 'except for' qualifier: except for when the central banker places a fat thumb on said weighing machine. The same is certainly true in the private markets where price discovery is a bit more art than science, and arguably less subject to the volatility that is driven by the emotion of the public investor.

All of Which Brings Us Back to India

Alpha is sometimes described as undiscovered beta, to be found in pockets where inefficiency reigns. That certainly applies to the private market in India today. The local opportunities remain largely undiscovered as the technology revolution advances, with the potential to deliver high returns to the diligent and patient investor.

In the coming pages, the investor will learn about the opportunities in India for participating in value creation from venture to growth capital, and the even more patient expectations in the buy-out space. From evolution to modern day, CAIA's in-depth study will give the astute investor the knowledge to make decisions in accordance with their investment horizon and risk tolerance. The role of sustainability, the use of leverage, and the importance of benchmarking are all critical ingredients for measurable and attributable outcomes; you will find those chapters of great interest too.

The very essence of any investment decision stems from informed consent. Understanding the risks, including those not immediately apparent, will always separate the informed investor from the absolute return seeking market participant. Let education and due diligence always be your guide, knowing that wealth is built around a long-term plan based on a diverse set of market exposures to match the duration of your liabilities and your risk tolerance.

I hope you enjoy the report and gain some actionable intelligence as you learn about the investment opportunities in India; a country of huge contrasts that is too big to ignore.

AUTHOR'S BIOGRAPHY

William Kelly
CEO, CAIA Association

William (Bill) Kelly is the CEO of CAIA Association. Bill has been a frequent industry speaker, writer, and commentator on alternative investment topics around the world since taking the leadership role at CAIA Association in 2014. Previously, Bill was the CEO of Boston Partners and one of seven founding partners of the predecessor firm, Boston Partners Asset Management which, prior to a majority interest being sold to Robeco Group in Rotterdam in 2002, was an employee-owned firm. Bill's career in the institutional asset management space spans over 30 years where he gained extensive managerial experience through successive CFO, COO and CEO roles.

India: A Hot Spot for Foreign and Domestic Capital

Takeaway: India's emergence as one of the world's most entrepreneurial and technology-oriented nations presents a massive opportunity for PEVC investors. As the alternative investment funds industry becomes larger and more sophisticated, it is vitally important that local industry personnel have the appropriate levels of professionalism.

India: A Hot Spot for Foreign and Domestic Capital

In the wake of the COVID-19 pandemic, India's economy has continued its growth trajectory. The country's GDP is expected to reach 9.5% in 2021-22, making it the fastest-growing major economy in the world and the third-largest contributor to global GDP. In the next six years, India is expected to contribute more to global GDP than Japan, Germany, Russia, Indonesia, Brazil and France combined in real purchasing power parity (PPP) terms.

Net average annual foreign direct investment (FDI) inflows into India measured approximately $38 billion between 2016 and 2020, making it the fourth leading destination for FDI worldwide.

India's relatively high domestic savings rate is perhaps the most significant statistic to note for those gauging the potential of the domestic investment industry. In 2019-2020, the country's savings-to-GDP ratio was second highest among top global economies, at 291 basis points (bps) ahead of the median rate of 27.3%.

Looking forward, we expect India to sustain this momentum, especially relative to other major economies on global investors' radar, like the United States and China. The Indian government's investment in physical and digital infrastructure - and improved business practices - will likely act as force multipliers for the country's key growth drivers in the coming decade: a younger population, a growing middle class, and the rise of urbanization across the country.

A Maturing Investment Environment

From increases in deal size, deal activity and fundraising, to improvements in term sheets and benchmarking practices, India's PEVC investment environment is reaching new levels of sophistication. According to Venture Intelligence, private equity firms (including VC) invested $39.5 billion in India-based companies during 2020, 4.6x (17% CAGR) the capital invested in 2010.

During the same period, deal volume increased from 454 deals annually in 2010 to a high of 1,037 in 2019; meanwhile, average deal size has more than doubled from $19.6 million in 2010 to $47.8 million in 2020.

At the end of FY2021, the average private equity fund size was $94 million and the average VC fund size was $35 million. CAIA expects these averages will keep growing as India continues to attract larger, more established fund houses, which currently dominate the country's PEVC landscape.

Indeed, the top five PE firms by fundraising accounted for 37% of total PE capital raised in the last five years. The top five VC firms accounted for 50% of total VC capital raised. Larger funds especially see India as a prime location for their investment operations given that the country's large consumer base allows for greater scale and better absorption of big ticket investments. In addition, the remaining funding gaps in sectors like healthcare, finance and infrastructure leave plenty of potential for future investment.

"While much of the global investment community was focused on the recent SPAC (special purpose acquisition company) trend during the last couple years, India's focus was on the promise of its unicorns."

India's VC-to-PE pipeline, as well as ample support for early-stage businesses, are also promising signs of a maturing industry. In the last 25 quarters, new investments (versus follow-on investments) accounted for at least half of VC transactions on average each quarter.

Additionally, an emerging venture debt market now offers investors alternative exposure to India's startup ecosystem, as well as a helpful pathway for these businesses to advance to their next milestones without losing control. Technology-focused startups especially benefitted from this increase in the availability of venture debt, as they were forced to react to the pandemic.

Finally, given the abundance of capital now available and the changing perceptions of risk in the country, term sheets are now evolving from a previous focus on downside protection to tools that guarantee upside participation. In addition, benchmarking practices for Alternative Investment Funds (AIFs) in India have led to improvements in transparency and thus better terms for investors.

The Ascent of the Indian Unicorn

While much of the global investment community was focused on the recent SPAC (special purpose acquisition company) trend during the last couple years, India's focus was on the promise of its unicorns - the startups that have, or are on track to achieve, a valuation of $1 billion.

In 2020, India had the third highest number of unicorns, led only by the United States and China. According to Venture Intelligence, by the end of 2020, India was home to 32 unicorns; by mid-August 2021 that number had already jumped to 55. To put that in context, the equity value of these 55 unicorns is nearly as much as the AUM of India's entire domestic equity mutual fund industry.

CAIA believes that, at the current pace, India could have more than 100 unicorns by 2025. This is based on the pipeline of startups closing on $500 million+ valuation, the current business environment, private markets activity and the increased pace of growth among these larger privately-held companies.

Looking Toward the Exits

Though COVID-19 forced a lull in exit activity in 2020, 2021 saw the largest harvest ever for PEVC investors in India, with roughly $19 billion in exits in the first half alone. As in 2020, 2019 and 2017, the greatest number of exits came from public market sales. With the $12 billion sale of Flipkart to Walmart in 2018 skewing averages, strategic sales have been the next most popular exit strategy in recent years, followed by secondary sales.

"An emerging venture debt market now offers investors alternative exposure to India's startup eco-system."

Relatively recent 'mega-exits' like the Flipkart-Walmart deal, Carlyle's partial exit from SBI Cards, Bain Capital and GIC's exit from GENPACT and the more recent IPO of Zomato - as well as the secondary sales of GlobalLogic and Star Health Insurance - have built confidence around India's PEVC landscape.

Larger multiple exits (10x +) seemed to be less affected by the pandemic than smaller or quicker turnaround exit deals, which were especially slow in 2020. Nevertheless, previous trends for these smaller exits may indicate a positive trajectory ahead, post-Covid.

Regional and Sector Trends in PEVC

The information technology (IT) and IT enabled services (ITES) sector accounted for roughly three-fifths of aggregate PEVC transactions in India in 2020. Deal sizes in this sector are generally smaller than the cross-industry average.

Banking, financial services and insurance (BFSI) was the second most active sector in 2020. Thanks in part to Carlyle Group's partial exit from SBI Cards and Payment Services, the sector generated the most exit value. IT, BFSI and healthcare, the third most active sector for

PEVC, contribute roughly 25% each to India's pipeline of potential unicorns.

Seemingly in line with sectoral numbers, we see a split between the regional leaders for deal value and deal volume in the country. Cities in southern India, most notably Bangalore, are known as hubs for the IT and ITES sector, and as a result, have been home to a higher number of PEVC deals in recent years. Nevertheless, in terms of deal value, western India, which includes Mumbai, is in the lead. Approximately 85% of India's startups funded by an institutional investor are located in Bangalore, Mumbai, or in India's National Capital Region, which encompasses Delhi. Other upcoming regional ecosystems include Chennai, Pune and Hyderabad.

AUTHOR'S BIOGRAPHY

Jo Murphy
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Jo has been in Asia for 25 years and has held several senior Asia Pacific wide management positions, successfully leading sales, business development, marketing and client relationship management divisions, and has both built and managed effective teams.

Expatriated to Hong Kong with Morgan Stanley Jo has also worked for HSBC, Deutsche Bank and Triple A Partners. Jo's roles have covered intermediary, buy and sell side as well as entrepreneurial groups, and now is Managing Director, Asia Pacific for the CAIA Association.

Jo enjoys the reputation of being hard-working, capable, committed, commercial, is a seasoned presenter and sought out moderator, regularly contributing to leading forums addressing topical aspects of the financial services sector, with a particular focus on the Asia Pacific private markets landscape. Jo was a founder and executive committee member of AIMA Hong Kong and now sits on its Education Committee. She holds corporate and NFP advisory board positions, is a Fellow of Singapore University of Social Sciences (SUSS) and is an advisory council member of UPACA Gurukul (India).

India Business and Investment Landscape

Takeaway: India's strong economic growth and political stability gives local and foreign capital the confidence in the country's new age business opportunities. As urbanization proceeds apace, an emerging middle class will be a key factor in the growth of wealth management. The local asset management industry will need properly qualified investment professionals to serve this new market.

India Business and Investment Landscape

More than 60% of global GDP is contributed by the top 10 largest nations. Close to 35% of the total is contributed by China and the United States together. Close to 7% is contributed by India and this share is expected to increase steadily on the back of strong and sustained economic activity in the foreseeable future.

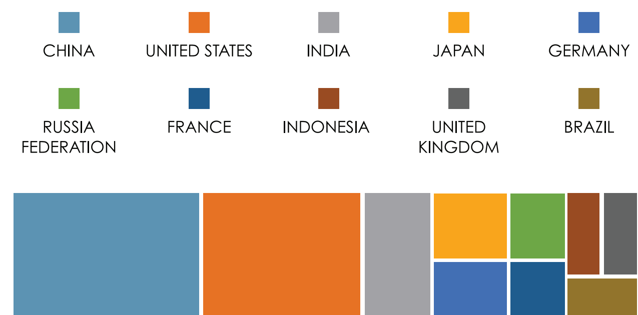
The economic prospects for India have rarely looked as bright. 2020 onwards, over the next six years, India is expected to add more to the global GDP than Japan, Germany, Russia, Indonesia, Brazil and France combined in real PPP terms. In other words, India is expected to add as much as the United States over the same period in real PPP terms.

In 2012, McKinsey Global Institute illustrated a change to the "world's economic centre of gravity" in the following 10 years.

As they predicted, the GDP-weighted centre of the world has moved closer to India and China, at a velocity not seen since the westward movement in the 1800s and early 1900s. This has resulted in a much greater focus on Asian trade routes.

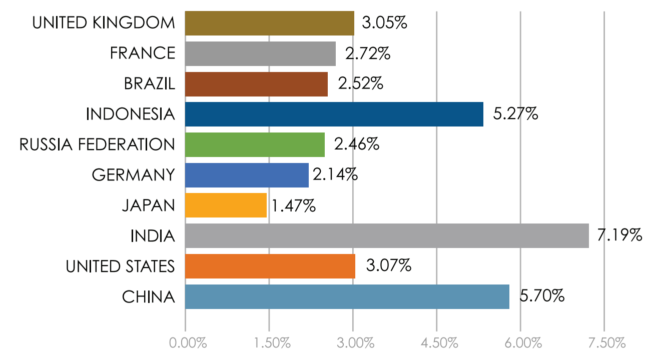
McKinsey noted that the economic growth was spurred on by the rapid expansion of cities as a result of mass migration from the poorer rural areas. According to World Bank estimates, 42% of India's population will be urbanized by 2030 up from 31% in 2011. To put that shift in perspective, the urbanization predicted is more than half the current population of the European Union.

Global GDP, PPP Current, 2020

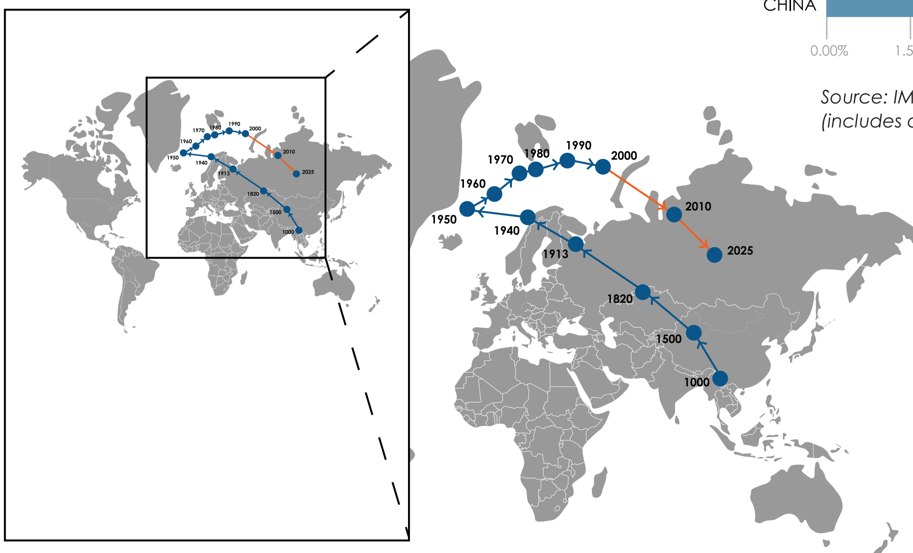


Source: World Bank

2021- 26 Average Real GDP Growth Projection (%pa)



Source: IMF, October 2021 series (includes actuals for India for 2021)



Capital Flows and Capital Formation

Historically, the United States has acted as the global capital for FDI, both inward and outward. Now, however, it receives more investments than it makes. Meanwhile, FDI into India has continued to accelerate in the last decade, with an average annual inflow of $48 billion between 2016 and 2020.

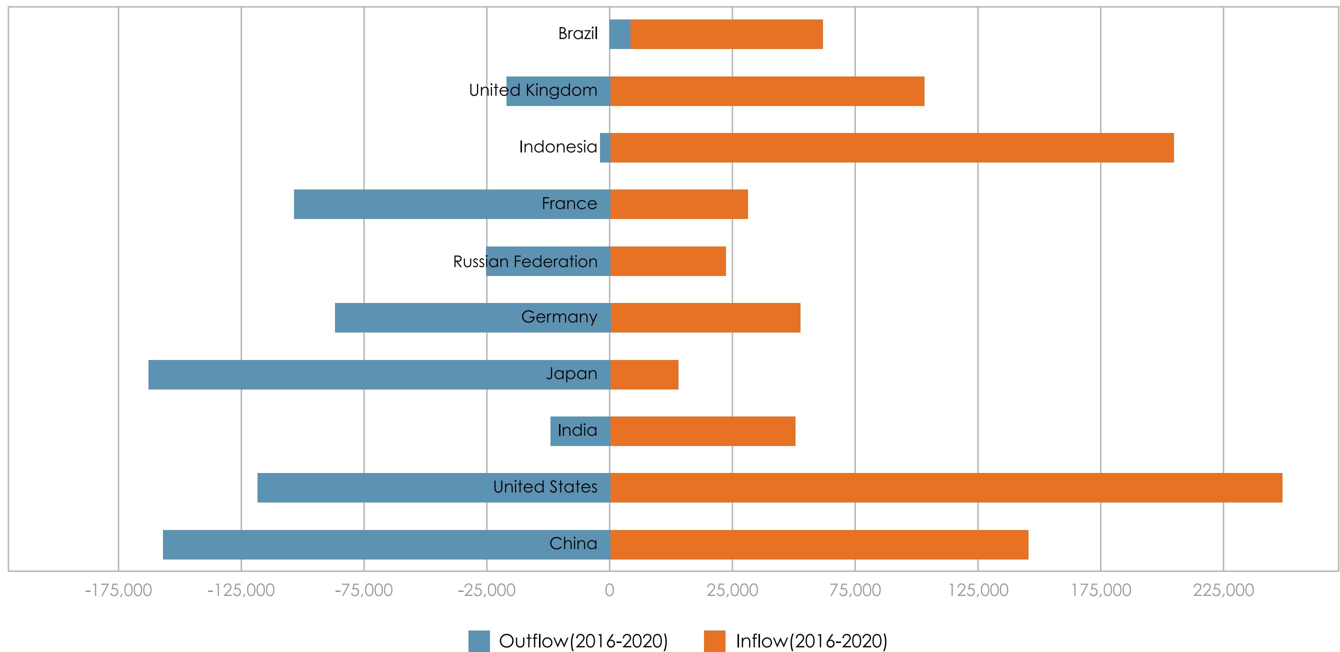
FDI Stock - Country Wise	Billions of USD			
	Inward		Outward	
Country	2010	2020	2010	2020
China	587	1,919	317	2,352
United States	3,422	10,308	4,810	8,128
India	206	408	97	191
Japan	215	243	831	1,982
Germany	956	1,059	340	1,207
Russian Federation	464	447	336	380
France	631	968	1,173	1,722
Indonesia	161	240	7	88
United Kingdom	1,068	2,206	1,686	2,055
Brazil	640	608	149	277

Source: United Nations Conference on Trade and Development

Domestic capital formation in India has been a steady growth trend in recent years. The median savings as a percentage of GDP for the top 10 largest economies (PPP) is 27.3%. The United States, United Kingdom and Brazil, which have had higher net FDI inflow as compared to India as mentioned above, have domestic savings of 857bps, 1,343bps and 1,224bps below the median of the peer group, respectively. India has a savings rate of 291bps above the peer group.

The capital requirements of India to fuel its growth are currently being met with an above average savings rate along with an increasing flow of foreign capital into the country.

Average Annual FDI in USD Millions



Source: United Nations Conference on Trade and Development

Demographic Dividend: Infrastructure and Technology to Remain Key

The India growth opportunity rests largely on a handful of key aspects; notably a relatively young population that is growing as a proportion of working age people. Similar to the other two largest global economies, China and the US, India has 67% of its population between the ages of 15 and 64. What is interesting is that this percentage is expected to improve over the next 20 years which is the opposite for China and the US.

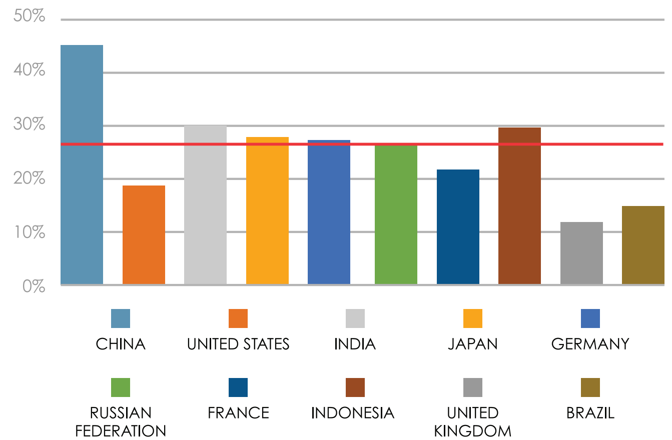
This positive demographic combined with increasing urbanization and the country's growth as a technology hub will, in time, expand the middle class. Many of these factors are still at a sunrise phase, which provides a strong growth opportunity for long-term investors.

As happened in China, mass migration from rural villages to the cities is driving the need for greater infrastructure investment and improved connectivity between the different regions of India.

India already has the second largest road and third largest rail connectivity in the world. Continued upgrading of these networks is necessary to ensure the economy can fulfil its potential over the long term.

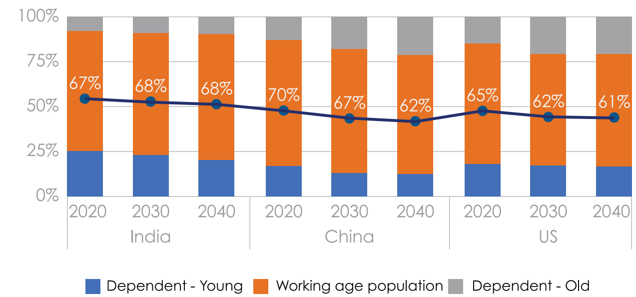
The digital economy is shaping up largely in urban areas, where there is sufficient scale and the skill base to allow commercial ventures to flourish . As India gets younger and Tier II cities gain greater attention from developers and investors, a technology-driven digital eco-system will be one of the most exciting growth areas of the Indian economy.

Savings to GDP Ratio - 2019/2020



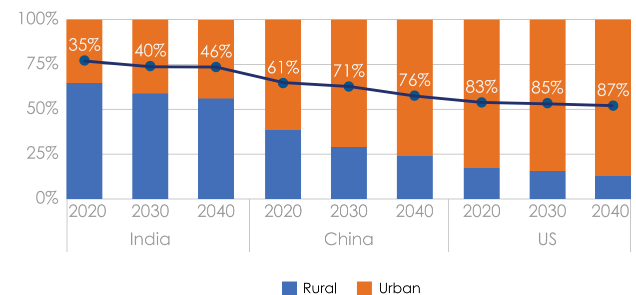
Source: World Bank

India Continues to Stay Young Over the Decades



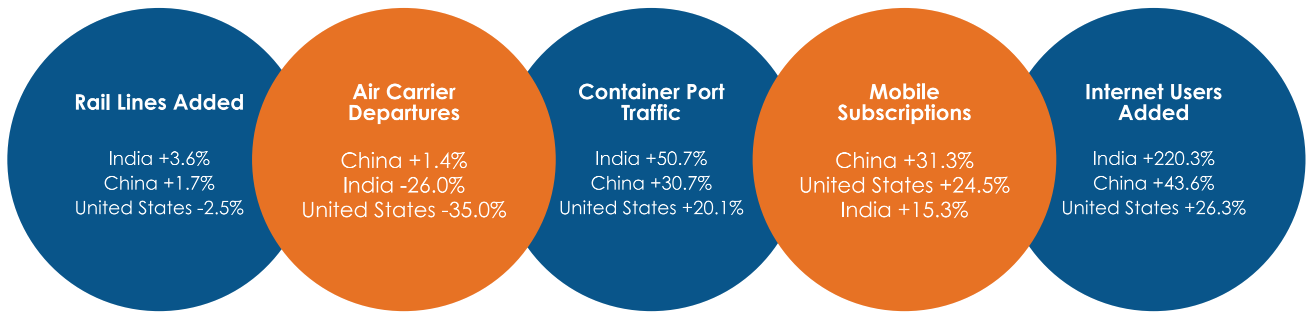
Source: World Bank

India Gathers Pace to Urbanization with an Increasing Population



Source: World Bank

Infrastructure and Technology Changes in Last 5 Years (Latest Available)



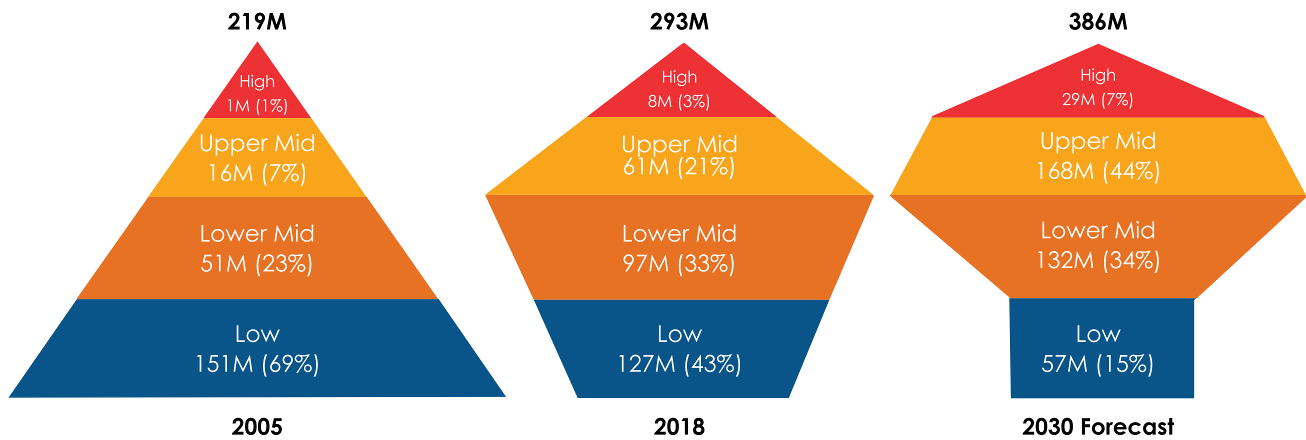
Source: World Bank

The key to increasing prosperity in India is the middle of the pyramid, where wealth management firms are already serving increasingly middle class households. The pyramid is expected to change shape as incomes rise. The growth of the alternative investment market in India is just one pointer to the rise of the middle class.

"The digital economy is shaping up largely in urban areas, where there is sufficient scale and the skill base to allow commercial ventures to flourish."

Political stability and continued commitment to reform by India's government are crucial to the country's success. There is a realistic assumption, in this report and elsewhere, that reforms will continue with the same momentum as we have seen in recent years and make India an attractive investment destination. There have already been massive improvements on several fronts, including the ease of doing business in India and the removal or reduction in procedural days. As we have said, this is just the beginning of a long road.

Households



Source: WEF

AUTHOR'S BIOGRAPHY

Shreekant Daga
Associate Director, CAIA Association

Shreekant is a CAIA, CFA and FRM charter holder. Shreekant pursued Bachelor's in Management from Narsee Monjee College and later did his Master's in Management from Jamnalal Bajaj Institute of Management Studies (JBIMS). He also holds a Master's in Commerce from Mumbai University. He is an alumnus of BSE Training Institute. He has also acquired several certificates from the NSE.

Shreekant has more than 5 years of experience in Structured Finance. His experience encompasses investment banking, handling recovery in stressed assets, ABS deal and rating evaluation, stressed assets and mutual fund rating. In mid-2018, he joined the Chartered Alternative Investment Analyst (CAIA) Association, India liaison office as Associate Director, Business Development.

Shreekant has been a visiting faculty at JBIMS and is also involved in mentoring and evaluating year-long projects for Mumbai University. He is a contributor to academic research and has 4 research papers presented and published at international forums and journals respectively.

Current State of Private Equity and Venture Capital in India

Takeaway: Solid economic progress and regulatory enhancement is supporting the growth of a knowledge-based and digital India. Crucially, this has resulted in favourable support for India's burgeoning alternative investments market, at a time when there is a marked increase in investor appetite.

Current State of Private Equity and Venture Capital in India

Domestic and international investors have demonstrated their confidence in India as one of the most promising growth economies of the 21st century. World Bank estimates value India's economy at around $3 trillion today, with projections for this to increase to $5 trillion in the next 10 years.

This growth path is underpinned by the Indian Government's dedicated efforts, along with agencies like Invest India, to enable a more robust and self-reliant country. The promotion of India as a knowledge-based and digital hub is a central plank of this strategy.

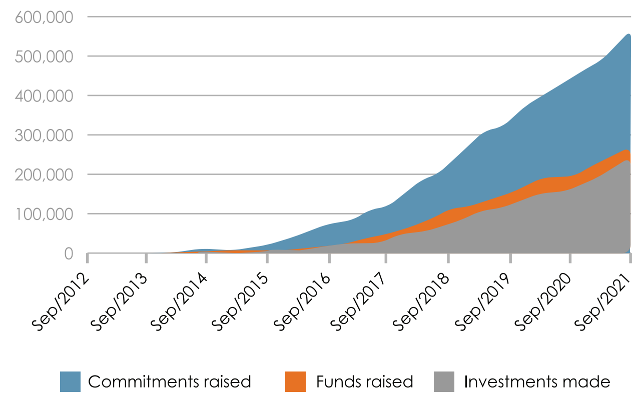
The key to India's emergence as a credible and vibrant investment destination is undoubtedly a reform-minded and anchored government, leading to India now regularly sitting among the top 10 economies showing the most notable improvement in the World Bank's 'Ease of Doing Business' rankings.

Prime Minister Narendra Modi's reform agenda is showcasing opportunities and gradually eradicating the structural inefficiencies that held India back for so long. By doing so, the government has created a robust launchpad for accelerated economic growth.

These regulatory enhancements, especially those introduced to bolster the local financial markets, are not just underpinning the traditional public markets but, just as importantly, are extending solid and favorable support to India's burgeoning alternative investment funds (AIF) Industry, and in particular its PEVC sector.

India's attraction is also being soundly aided by geopolitical tailwinds, stemming from nervousness about the impact of China's attempts to rein-in capitalism and the economy's debt dependence. President Xi Jinping's crackdowns have certainly resulted in an increase in foreign institutional investors (FIIs) investigating Indian PEVC opportunities as a viable alternative.

Total AIF in 10 Million INR



Source: SEBI

Further, multinationals have largely been overdependent on Chinese manufacturers. In a time of political tension and supply chain pressure, they're looking to diversify their partners. India is proving a popular choice, offering up a cost effective, reliable and English-speaking alternative.

For FIIs, those actively seeking an alternative for their emerging market allocations, alongside direct investment opportunities, India ticks all the boxes.

The rapid pace of growth is further demonstrated by the sustained optimism being shown in India's stock markets. With public market valuations sitting at lifetime highs – for example, the average price/earnings ratio across the Sensex is currently around 27x - the market boom is drawing in new retail investors. The Sensex has more than doubled from its March 2020 low and was the best performing market in the world in 2021.

Two other factors of note and acting as further

accelerants are the Central Bank of India's liquidity high surplus levels and declining interest rates.

These factors in aggregate have drawn the attention of India's local investor community to a wider range of investment options, leading to a marked increase in private markets activity. This greater diversification is particularly notable in the manner of its increasing momentum over the past 12-18 months.

Resilient, Raging & Raring To Go: PEVC

PEVC has been a solidly resilient sector within India's growing private market, in spite of COVID-19's outbreak. Deal activity is raging and 2021 was a landmark year for the industry. The sector is benefiting from sooner-than-expected business recovery, alongside solid investment inflows from both domestic sources and FIIs.

One of the most encouraging aspects for India is that new investments are larger. During the first half of 2021, investments grew 33% year-on-year, with investment flows of $27.1 billion across 442 deals, compared to $20.4 billion, across 433 deals during the same period in 2020 (Venture Intelligence Data).

The past decade has certainly seen a coming of age for India's PEVC sector. We've seen the number of fund managers swell from around 350 in 2017 to over 500 in 2021. Capital flows have been equally buoyant with a pool of over $10 billion back in 2010 rising to over $30 billion in 2020. Noteworthy is the mix of both interest from FIIs - finding India's allure too good to miss – alongside home-grown investors diversifying their portfolios.

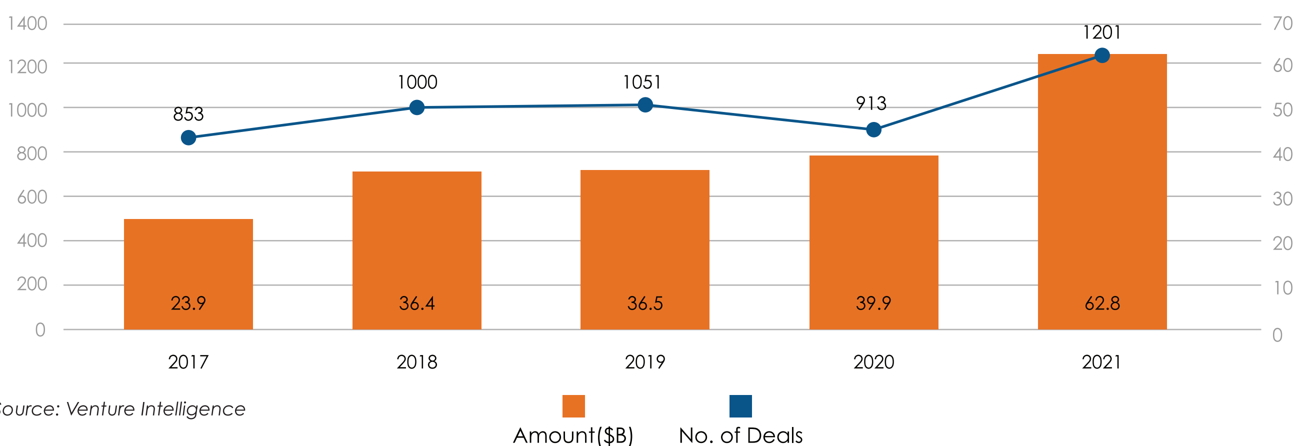
With many sectors flagged for growth, PEVC LPs and GPs are increasingly eager to assess opportunities early, seek solid partnership actively, and allocate investment quickly.

Change of Approach

Fuelling this activity is a significant change in the approach target companies are taking during the formation stages of partnerships, and their engagement with PEVC partners. There's now an increasing willingness to provide control to PEVC firms, sturdily assisting with the acceleration and growth within the sector. This approach was previously absent, leading to often thwarted and stalled transaction negotiations, muddled engagement and, ultimately, compromised returns. The old guard wanted to hold on too tightly to the reins.

The large pool of young Indian entrepreneurs is spearheading this change. Globally exposed as well as professionally trained, they are unencumbered by the conservatism of the previous generations. This cohort of entrepreneurs are eager to embrace the opportunity to partner. Indeed they are actively

Private Equity and Venture Capital Investments by Year



Source: Venture Intelligence

seeking out potential opportunities, whether via domestic or international channel sources. This certainly bodes well for the sector; for engagement, for opportunities and for returns ahead.

Sectors of Note

The Information Technology (IT), Information Technology Enabled Services (ITeS), Software as a Service (SaaS), Healthcare and Pharmaceutical sectors, each saw a significant portion of new investment flow in 2021. IT, ITeS and SaaS have benefitted strongly from the growth of digital adoption, as well as a greater need for digitization on the back of strong consumer shifts during COVID-19. In the wake of the pandemic, India has emerged as the fastest-growing and third-largest fintech ecosystem in the world. This led to a spike in deal volume, where the number of transactions was greater than $100 million, to 73 in the first half of 2021 compared to 28 during the same period of 2020.

The Banking, Financial Services and Insurance (BFSI) sector has seen a contraction of interest in non-banking financial companies to an increased focus towards insurance – focused on the insurer and insurtech segments. This focus has been enhanced by the Insurance Regulator and Development Authority of India (IRDAI) permitting insurance companies to invest in Fund of Funds, in April 2021, providing a further and significant boost.

For at-home services – consisting of consumer technology, vertical e-commerce, edtech, fintech and foodtech – each attracted significant interest during 2021. With the rise of disposable incomes, focus is increasing on businesses who serve the Indian consumer, both offline and online. As a result, the logistics sector is anticipating exponential growth, with many new investment targets emerging.

Global institutional investors are increasing their real estate allocations and are looking at opportunistic real estate investment strategies in India. PE real estate in India has significant momentum, led by the aggressive investments of Blackstone and Brookfield. According to Jones Lang LaSalle, more than $14 billion was invested by private equity in Indian property since 2006. Approximately 10 new PERE funds are being launched annually.

"This cohort of entrepreneurs are eager to embrace the opportunity to partner. Indeed they are actively seeking out potential opportunities, whether via domestic or international channel sources."

India's collapsing and aged infrastructure offers endless creative development opportunity between public and private interests, particularly in roadways, electrical grids, renewable energy and telecommunications.

Tech in Focus: (R)Evolution

As noted, the appetite for tech-related investment is substantial, which is probably not surprising given India's domestic demographics and such a large pool of the 'online first' digital generation. With almost 30% of India's citizens under the age of 14, there is undoubtedly a demographic dividend that works to the advantage of the technology sector.

India has a strong heritage in IT services stemming back to the 1980s when India provided agile and robust SaaS solutions to global markets. India's strong links with its colonial past mean English is widely spoken. Officially there are over 130 million English speakers across the country, the second highest in the world after the US. There are over 1.5 million new engineering graduates entering India's job market each year, making it the second highest talent hub in the world, after mainland China.

With this backdrop, India's burgeoning technological

evolution - indeed, revolution – has become a reality and, given it was a core pillar of PM Modi's move to a more robust and self-reliant India, the country is well on the way to achieving that goal.

India's digital generation are early adopters, enjoying the warm embrace of the world's largest 4G network, low-cost data accessibility and widespread smartphone use - India has more than 1.1 billion smartphone users. Naturally, eCommerce and digital banking services have accelerated at a speed that reflects this classic technology leap, experienced by all emerging markets.

It is also instructive to factor in India's sizeable pool of increasingly affluent workers, consumers and investors – expected to comprise of 1 billion people by 2030 (World Economic Forum) - around 70% of the population. Digitization has transformed life in India's vast expanse, creating a mass of consumers from city to hinterland and promising a tremendous pool of opportunity now and in the future.

A recent paper 'Digital India : The $1 trillion Opportunity' [Source: Ninety One] positions India as the world's fastest growing digital economy. It notes that India is well on the way to unlocking $1 trillion in value (from ~$250 billion in 2020) and will account for over 25% of India's overall GDP by 2025. The PEVC sector is eager to participate in this opportunity, so India's digital economy is definitely one to watch.

Access for all? …. Caveat Emptor

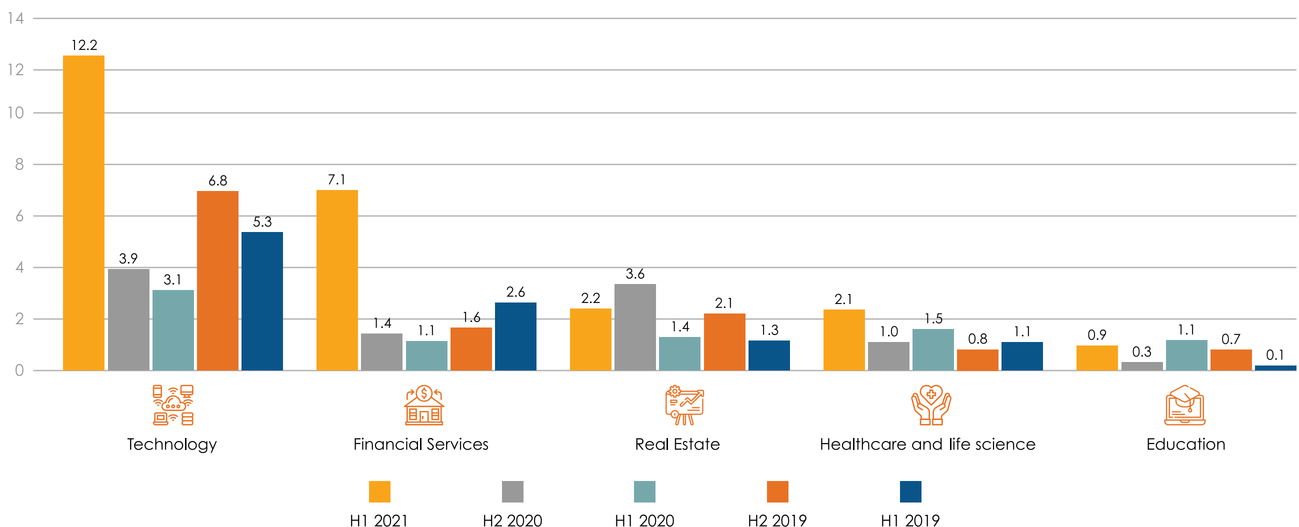
In common with any new investment growth market, as confidence rises and demand grows for access to India's PEVC story, it is important to note the attendant risks. There are liquidity, valuation and exit terms to be considered, each providing a long list of due diligence to complete and monitor. The particularly porous nature of PEVC target firms also need close attention. Deep research, checks and balances within any investment, operation or monitoring procedure is absolutely key.

Given that PEVC target firms are often working with third parties, this does also require caution. Fraudulent activities – and not just from within – but by and on portfolio companies invested in and third parties being dealt with are certainly more possible. In particularly challenging moments, when economic survival is threatened, a blurring between what's acceptable

Technology in the Lead

The technology sector dominated the PE investments space with 16 start-ups entering the unicorn club in 2021 compared to 9 in 2020. Edtech is the emergent sector as major players like Byju's and UpGrand continue to raise funds.

Top Five Sectors Attracting PE Investments (in USD billion) Raise Funds



Source: Venture Intelligence

and unacceptable behaviour can occur. Fraud does occur, in all markets, like in the cases of TAL Education Group and Luckin Coffee (Source: KPMG).

"The checks and balances call for careful, robust monitoring and clear preventative protocols to be firmly in place."

The checks and balances call for careful, robust monitoring and clear preventative protocols to be firmly in place. With distressed deals in particular, manager selection, KYC and deep (even forensic) levels of pre-investment due diligence are required. Experienced PEVC investors know this, but window dressing is a real risk too. Operations may present healthy profits but upon further investigation, accompanying financial reports do not tally up. WeWork's infamous 'Community Adjusted EBIDTA' is an example of how a company can manipulate and misrepresent financials. As with any PEVC investment, caution is encouraged.

With engagement, review and investment in target firms happening at an increasingly speedy pace, cybercrime also needs solid consideration, as do data breach and IP theft. India's regulatory landscape – whilst certainly having been adapted and refined of late – remains complex in many parts. This is particularly so when the threads of central, state and local municipal authorities each need to be understood and stitched into a transaction. Wishing to transact speedily within such a framework certainly calls for caution.

Additionally, both governance and sustainability factors are being more deeply reviewed. For many PEVC funds - particularly the global heavyweight firms who are already in or are entering the market - investing in certain portfolio targets will require substantive change so that their own internal protocols and investment-ready permits are met.

Where target companies do not exhibit the same robustness around their governance and ethics framework that foreign investors in particular are used to, there will be pressure for change in the sector. Funds are now addressing these areas actively with target portfolio companies; imposing change requirements on each company and closely monitoring for implementation.

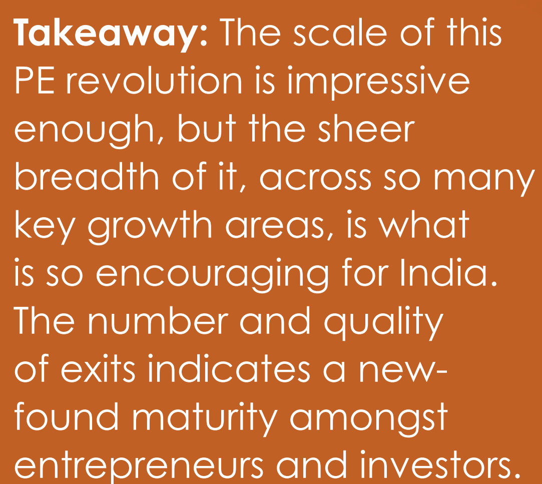
Some of these differences in business culture will likely cause tension and perhaps a delay in engagement but, most importantly, we will ultimately see best practice across the board and a stronger and more robust Indian PEVC sector.

Conclusion

Being or investing in a unicorn is a rather tantalising proposition. India's PEVC sector has laid the foundations for local and global investors to fully engage. With India's strong economy, an evolving and progressive regulatory framework, combined with a highly entrepreneurial landscape, there will undoubtedly be great opportunities ahead.

Jo Murphy
Managing Director, CAIA Association

How PE Investing in India Has Evolved

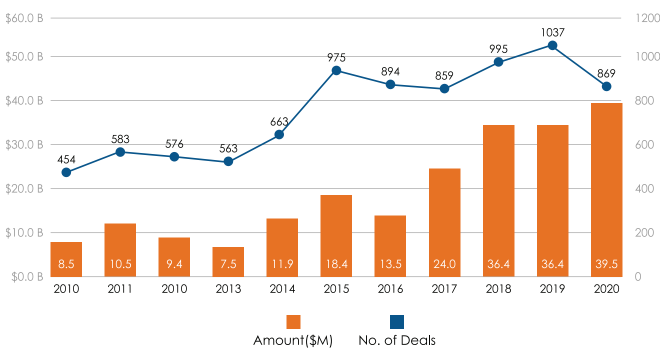


Takeaway: The scale of this PE revolution is impressive enough, but the sheer breadth of it, across so many key growth areas, is what is so encouraging for India. The number and quality of exits indicates a new-found maturity amongst entrepreneurs and investors.

How PE Investing in India Has Evolved

The PEVC industry has emerged as a significant shaper of trends in the Indian economy during the last decade. Today, the largest Indian corporate houses - including Reliance Industries and the Tata Group - have loosened their purse strings to acquire innovative PEVC-backed companies. The public markets are welcoming rapidly scaling startups, and venture-backed startups are making audacious acquisitions of companies that are much older and better established than themselves.

Private Equity in India: 2010-2020



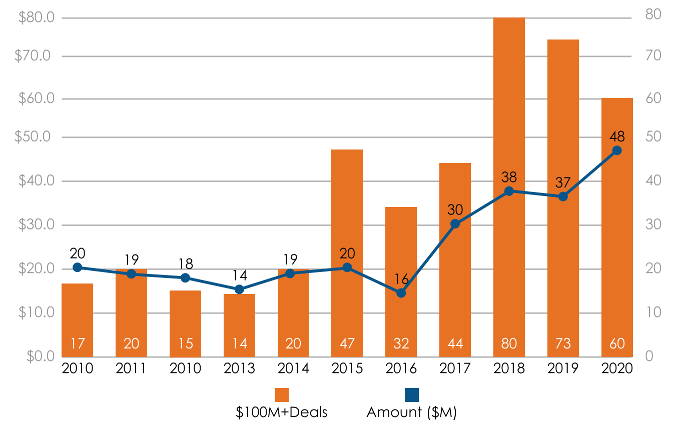
Source: Venture Intelligence

The value of PEVC investments in India more than quadrupled during the decade spanning 2010-2020. PEVC firms invested $39.5 billion in India-based companies (across 869 deals) during the pandemic-impacted 2020 - which was 4.6x (17% CAGR) the capital invested in 2010.

The deal volume had also grown by 7% (CAGR) over the same period - starting off 2010 at 454 deals and hitting an all-time-high of 1,037 in 2019. The average deal size has witnessed a steady rise over the decade, from $19.6 million in 2010 to $47.8 million in 2020, reflecting rapid maturing of both the startup ecosystem and the PEVC asset class.

The number of 'mega-deals' (of $100 million or more in value) has vaulted 3.5x - from 17 such deals in 2010 to 60 in 2020. While the onset of the pandemic in early 2020 had a chilling effect on investment activity, the Reliance Industries (RIL) Group stemmed the tide by raising massive amounts of capital across its Jio brand telecom and retail ventures over the next few months. The $9.9 billion raised by the Jio platforms in May 2020 - valuing it at $64.8 billion - catapulted it as the largest ever PE investment in the country.

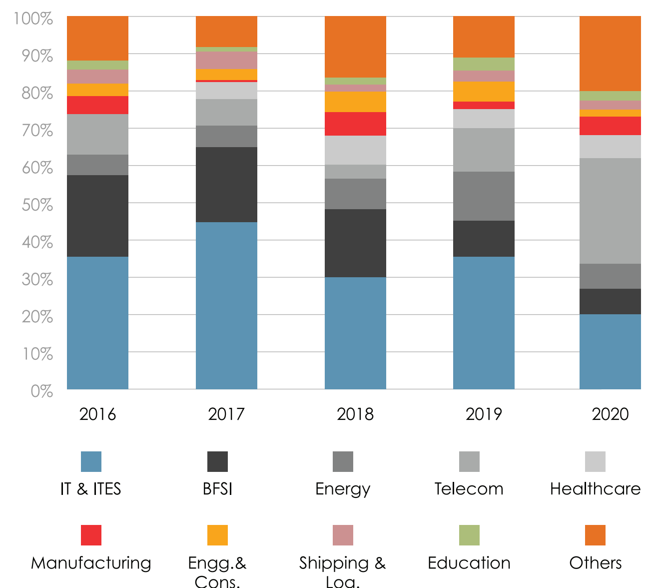
Average Cheque Size: 2010-2020



Source: Venture Intelligence

Private Equity Investments by Sector

Private Equity in Core Industries



Source: Venture Intelligence

IT and ITeS companies remained the favorite destination for PEVC investments during the decade - accounting for 30-45% of the pie. The IT and ITeS industry cumulatively attracted around $70 billion worth of PEVC funding,

growing at a 25% CAGR. While consumer-driven sectors like e-commerce and fintech saw the start of mega investments in these sectors starting around 2014.

The pandemic - by accelerating digital adoption - has led to a tidal wave of funding for a range of other tech sectors such as edtech as well as B2B sectors including enterprise software and SaaS.

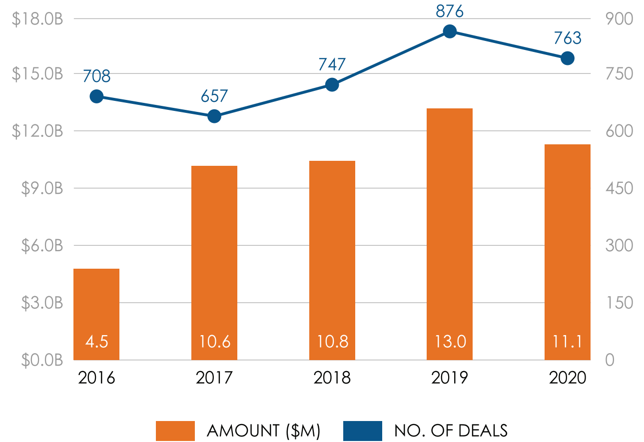
BFSI companies were the next favorite, raising around $28.4 billion during the decade. Investments in BFSI grew at 7% CAGR during the period and hit a peak in 2018, when the sector attracted $6.5 billion. PE investments in healthcare and life sciences companies grew at a 17% CAGR during 2010-2020, with the investment value rising 5x (from $548 million in 2010 to $2.5 billion in 2020). Other core industries that have seen a rise in PE interest over recent years include Energy, Telecom, Engineering & Construction and Logistics.

Venture Capital

VC-type investments have also grown significantly over the decade with over $50 billion being invested in the segment over the last five years alone. Led by SoftBank's $2.5 billion investment in Flipkart in 2017, the period between 2016 and 2020 saw 129 mega-investments, representing close to 70% of the cumulative figure. The most active VC firms during the period have been Sequoia Capital India (across 175 companies) and Accel India (111 companies). Tiger Global, the New York-headquartered hedge fund investor, has been a key trendsetter in the segment, backing 40% of the more than 50 Unicorns in the country, starting with its 'make or break' bet on Flipkart.

E-Commerce has largely defined the success of VC in India over the last decade. Since the landmark year of 2018, which saw the $16 billion acquisition of Flipkart by US retail giant Walmart, the sector has attracted as much as $10 billion. Investor interest initially spread from horizontal e-commerce (like Flipkart and Snapdeal) to transportation and delivery tech startups like Ola, Swiggy and Zomato. The pandemic served to catapult e-commerce to the next orbit, with various flavors including Direct-to-Consumer brands and Social Commerce models attracting dollops of capital.

Venture Capital in India: 2016-2020



Note: Venture Capital includes i) Seed to series F investments in companies less than ten years old; ii) Late stage tech investments.

Source: Venture Intelligence

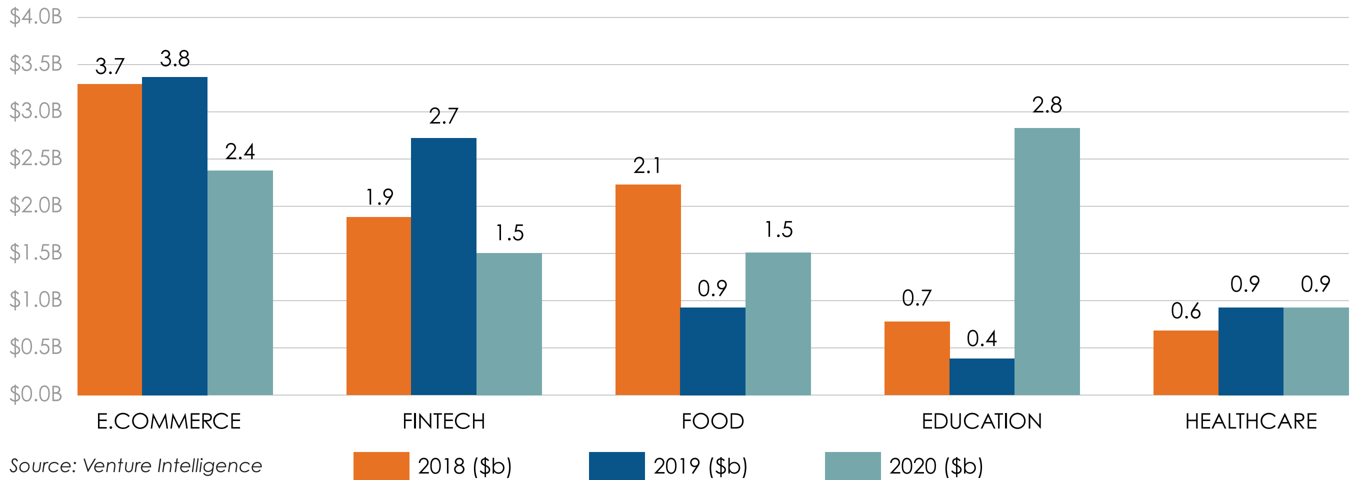
In the second half of the decade, Fintech startups began to find favor, attracting over $4 billion during 2019-2020. India's startup space saw the creation of 36 Unicorns during the 2010-2020 period, with most of them emerging from the E-Commerce and Fintech sectors. The pandemic changed the fortunes of the EdTech sector, helping it attract massive doses of funding for startups (apart from the already large Byjus) including Unacademy, which turned Unicorn.

"With a massive rise in the availability of capital, it is not surprising that fast growing private companies are seeing a steep elevation in their valuations."

Venture Debt Investments

Venture Debt - that is debt provided to venture-backed companies by specialized lenders - came into its own in the last decade, especially the latter half. Pioneered by Innoven Capital (which was spun out from Silicon Valley Bank's Indian unit) and joined by new firms like Trifecta

Venture Capital in Top Sectors



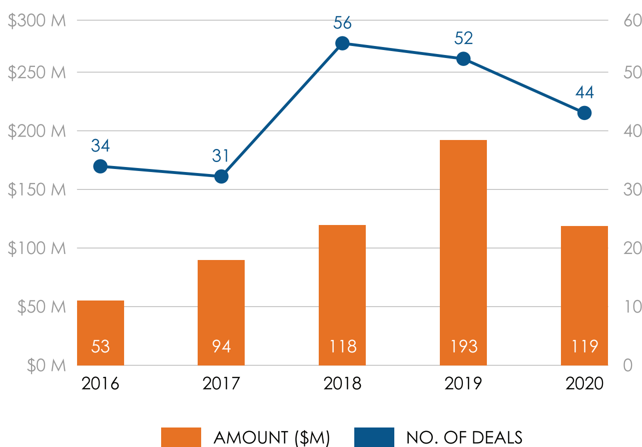
Source: Venture Intelligence

Note: (a) Venture Capital includes i) Seed to series F investment in companies less than ten years old; and ii) late stage invesments
(b) Companies are double counted if they fall in more than one sector. E.g. if a company is an AI based fintech company, it would be counted under both AI as well as fintech

Capital, Blacksoil and Alteria Capital, these investors lent almost $200 million to VC-backed startups in 2019.

Venture debt represents less than 5% of the VC market in India, but it has large headroom for growth, especially if the Indian ecosystem evolves similarly to the US, where the share of venture debt funding may be as high as 15%.

Venture Debt in India 2016- 2020



Source: Venture Intelligence

Valuations

With a massive rise in the availability of capital, it is not surprising that fast growing private companies are seeing a steep elevation in their valuations. Among the 'pure play' internet companies, Info Edge - which operates multiple online brands led by jobs listing service Naukri.com - chose to go public on the Indian stock market as early as 2006. The company's stock price, after staying in the INR 150-200 (USD 3.5- 4.5) zone until 2010, has rocketed over the last decade to over INR 5,000 (USD 67), providing it with a market capitalization of over INR 66,000 crore ~USD 9 billion.

Three of Naukri's peers from the 2000 era – marriage services-focused Matrimony.com and B2B listings-focused Justdial and IndiaMART - went public over the last decade, after demonstrating a track record of profitability. With Zomato successfully embarking upon an IPO in July 2021 and other startups set to follow, it will be interesting to see how the domestic markets treat these fast growing – but loss making - ventures. From a revenue multiple perspective, InfoEdge, Matrimony, IndiaMART and JustDial have tended to trade in the 10-15x range. The valuation of privately held B2B unicorns are also pegged in this range. Mature private companies in the B2C segment however seem to enjoy a premium, with their revenue multiples sitting in the 15-20x range.

Younger private companies, who have turned unicorns in less than 5 years (including Groww, Cred and Unacademy) are clearly not being valued on historic financial performance (which would put their multiples near 100x), but are based on tailwinds witnessed on the

back of the pandemic as well as their future growth potential.

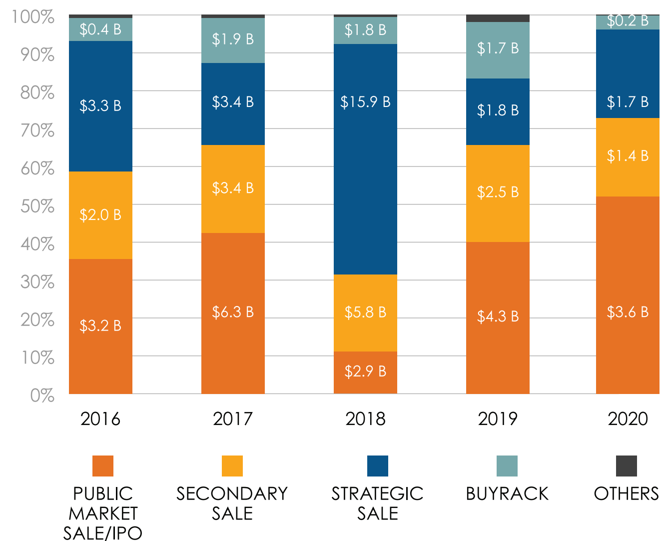
Exits

PEVC firms registered 1,261 exits from Indian companies, harvesting $67.5 billion during the five years 2016-2020. Of this, $31.6 billion (across 708 deals) represented complete exits from the portfolio companies (about 47% of the total value), with the remaining being partial exits ($35.9 billion) across 553 deals, representing 53% of the total. On the back of a bull run in the stock markets, public market sales (including IPOs) accounted for 40% of total exit volume during the period. Top exits via the public markets included Carlyle Group's $951 million partial exit from SBI Cards, via the company's IPO, followed by Bain Capital and GIC's exit from NYSE-listed BPO services firm GENPACT.

Strategic sales accounted for about 29% of the exits. While the outlier Flipkart-Walmart deal is the largest strategic sale to date (fetching $12 billion for Flipkart's investors), the average size of a strategic sale exit during 2016-2020 was about $209 million, rising from $130 million in 2016 and $142 million in 2017. The secondary sale route (that is, the sale of a stake held by existing investors to new investors) accounted for about 21% of the exits. Notable deals in this category included Apax Partners' $960 million exit from IT Services firm GlobalLogic and the $938 million exit by investors in Star Health Insurance.

The ultimate arbiter of a successful PEVC asset is the exit and the accompanying returns. With a string of mega-exits towards the end of the last decade, any lingering questions on the sustainability of the India PEVC story have been removed and the industry is set to move forward with confidence.

Private Equity Exits - 2016 - 2020



Source: Venture Intelligence

AUTHOR'S BIOGRAPHY

Arun Natarajan
Founder, Venture Intelligence

Arun Natarajan is the Founder of Venture Intelligence, the leading source of information on private company financials, transactions and valuations in India. Venture Intelligence has been tracking Private Equity, Venture Capital and Mergers & Acquisitions in India since 2002.

Arun has over 20 years of research and media experience. Before founding Venture Intelligence, he had worked as a Senior Research Analyst with The Hindu-Business Line, a leading Indian business daily. Arun has a B.Tech (Chemical Engineering) and PGD (Financial Management).

Arun is a Charter Member of The Indus Entrepreneurs (TiE) and currently serves as the Vice President of TiE Chennai.

An Industry Moving Towards Maturity

Takeaway: Historically for every four VC deals in India, there is one PE deal. This ratio is expected to reduce as the ecosystem attains maturity.

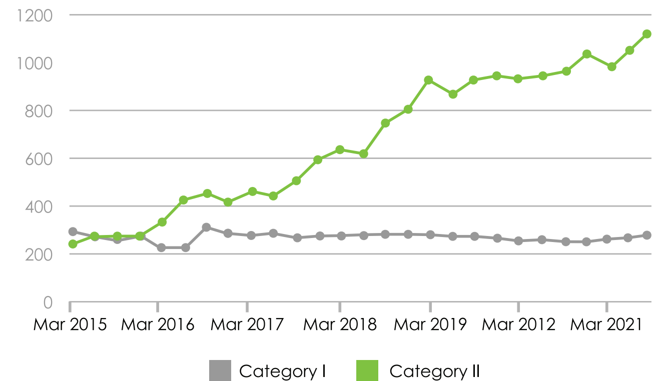
An Industry Moving Towards Maturity

In 2012, SEBI introduced the Alternative Investment Funds framework. Prior to 2012, these investment activities were governed by several regulations across a variety of legislation.

Since 2012, the average size of Category II funds (considered as private equity) has continued to grow, with slight flattening in 2020. The average size of Category II funds is $145 million, as on September 2021 data. Likewise, the average size of Category I fund (considered as venture capital) is $37 million.

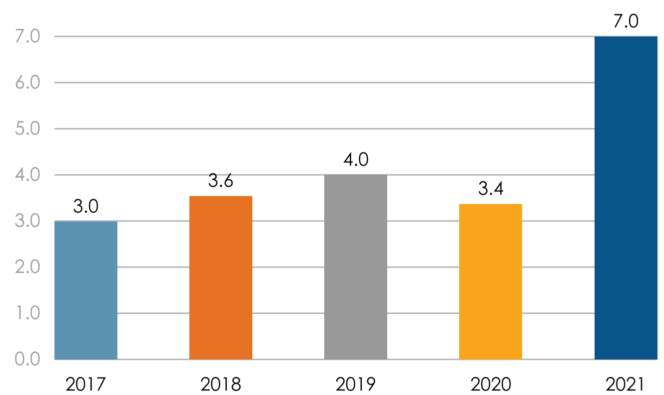
We expect the average size of Category II funds to rise on two accounts. First, because domestic fund houses with performance track records are likely to grow larger in size, as these players consolidate their dominant position in the mid-market segment. Second, India will attract global fund houses which have India-focussed funds and are currently active in the mid-market and late stages. We believe some fund houses will start to move into the International Financial Services Centre at GIFT city with larger operations, given the tax holiday and the startup possibilities in India.

Average SEBI Registered Fund Size (in INR 10 Mn)



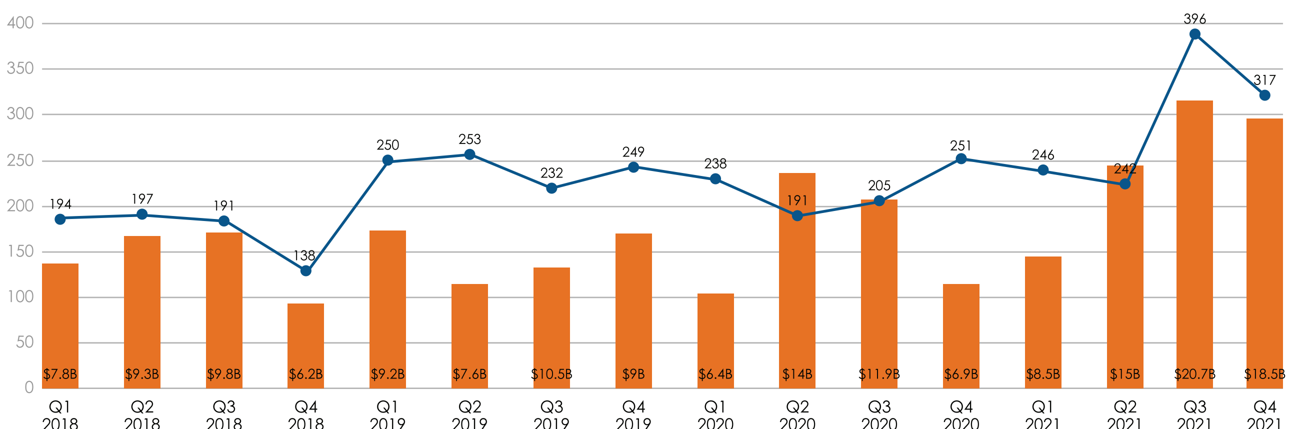
Source: SEBI, CAIA Analysis

Median Investment Size $ Million (PE and VC Combined)



Source: Venture Intelligence, CAIA Analysis

Private Equity and Venture Capital Investments by Quarter



Source: Venture Intelligence, CAIA Analysis

The median PEVC investment size has been gradually increasing (with a cautious 2020), as the market and its ecosystem continues to mature.

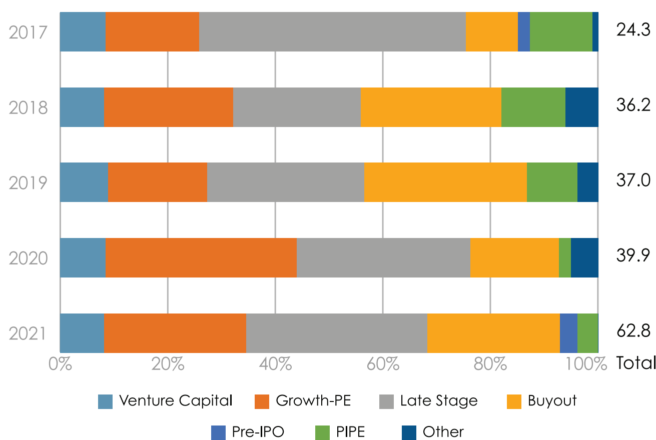
Deal count had averaged 800 - 1,000 over a calendar year with 2021 making a record 1,200+ deals. The increased deal activity is based around the target companies' aggressive, expansionary business plans, combined with similarly aggressive appetite from investors. This is especially true for businesses in sunrise sectors; IT and ITES services have historically accounted for close to 60% of the deal count.

Break-up of PEVC Investments

Historically for every four VC deals in India, there is one PE deal. This ratio is expected to reduce as the ecosystem attains maturity. These VC deals have contributed less than 5% to deal value historically, whereas the PE deals, which account for 20% of volume, have contributed close to 95% of deal value; so there is clearly room for growth.

Growth and late-stage PE on average contribute just under half the deal value over several years.

Distribution of Investment by Stage in USD Billion

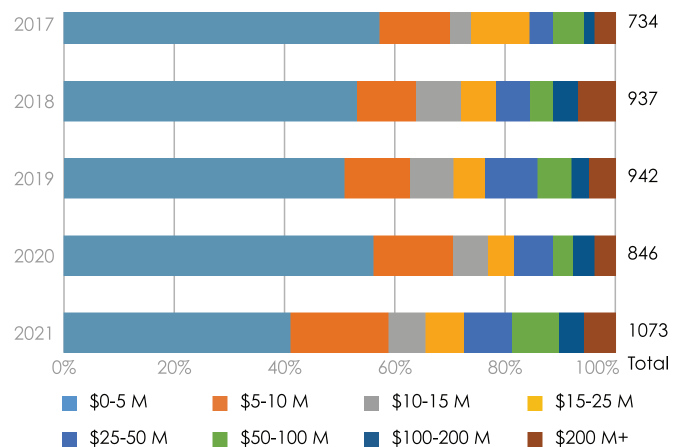


Source: Venture Intelligence, CAIA Analysis

Deal activity has remained dominated by the IT and ITES sectors which account for three-fifths of aggregate transactions. The size of these deals, though, has remained smaller than the average deal size in India by close to 40%. In 2021, IT and ITES contributed close to 80% of deal activity which denoted a value of 65%. This is on the back of some large investments in Hexaware Technologies and Mphasis.

The average deal size in 2021 was around $52 million v/s $54 million in 2020. The second most active sector has been BFSI which has a larger average deal size

Distribution of Number of Investments by Deal Size

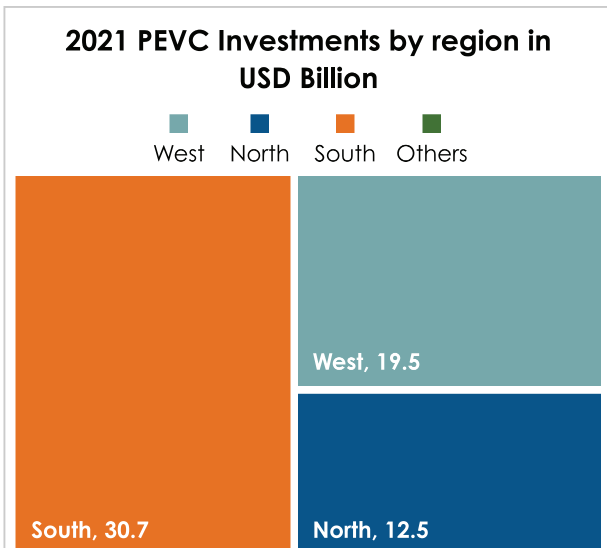


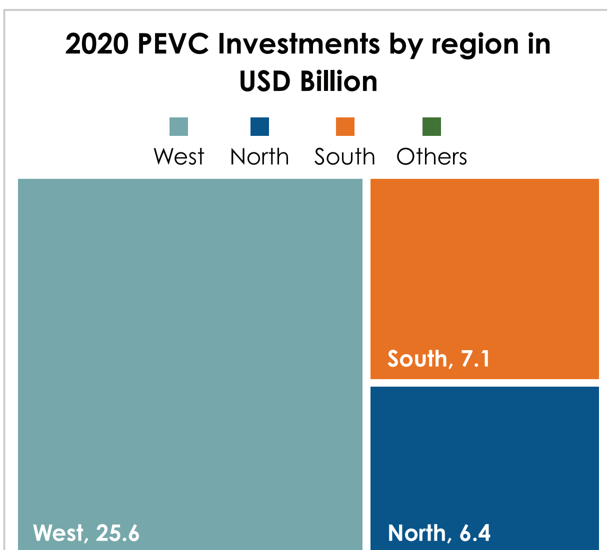
Source: Venture Intelligence, CAIA Analysis

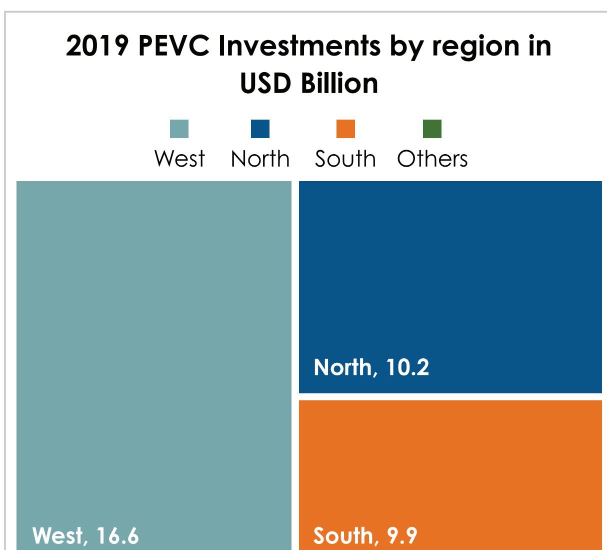
by close to 70%, when compared with aggregate numbers, and a 10% higher average deal size when compared with the remaining industries.

The popular belief is that cities in southern India are the hubs for startups in India, but the data actually points the other way. While southern India accounts for a high number of deals, western India (which includes Mumbai) accounts for substantially higher average deal value.

The number of deals in southern India has always been the lion's share of the pie, but with smaller ticket size. This is also because most southern India startups are IT and ITES sector focussed, which tend to have smaller funding rounds on average. There are three city hubs for startups which include Mumbai, National Capital Region (NCR) and Bangalore. Around 85% of startups funded by an institutional investor are located in one of







Source: Venture Intelligence, CAIA Analysis

these cities. Aggregate funding for startups in Mumbai is the largest compared to all other cities.

VC Activity Gives Fuel to PE Activity

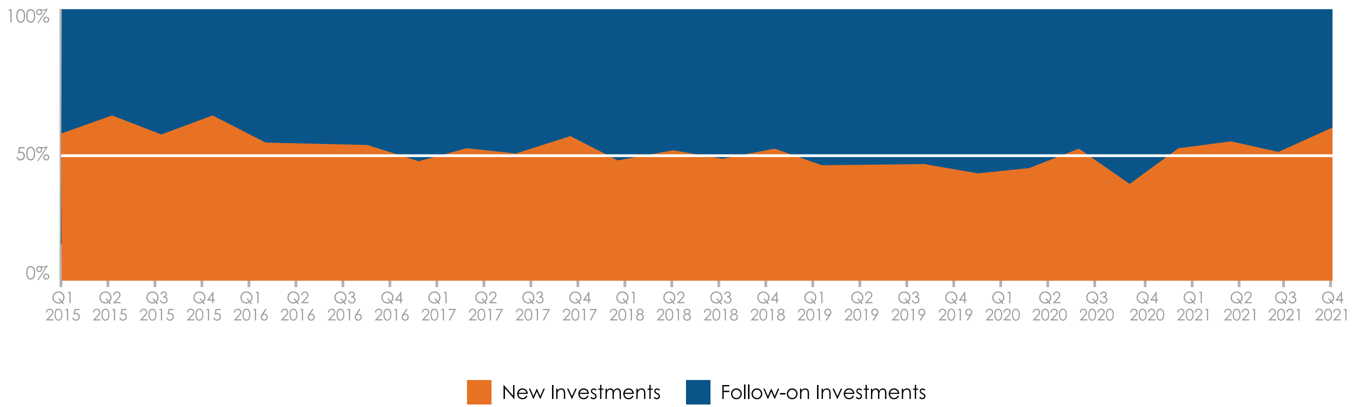
Similarly, fresh investments from early VC maintains the pipeline for growth VC. The 50% mark is critical in the breakup since it determines the pipeline. In a growing startup ecosystem, the new investments would continue to make up a majority of the pie.
The average number of VC transactions per quarter over the last 25 quarters was 156, with new investments accounting for at least half of transactions in 15 quarters. On a volume-weighted basis, the Indian VC ecosystem is well supported with ongoing fresh activity and early funding to support new businesses.

"While southern India accounts for a high number of deals, western India accounts for higher deal value."

The median size of early VC investing in India is $2.5 million as end of 2021. This is a significant shift upwards from a historic sub $2 million median deal size. Approximately 85% of VC funding in the same period has been for technology startups. This strong inclination towards tech is increasingly visible over the past several quarters.

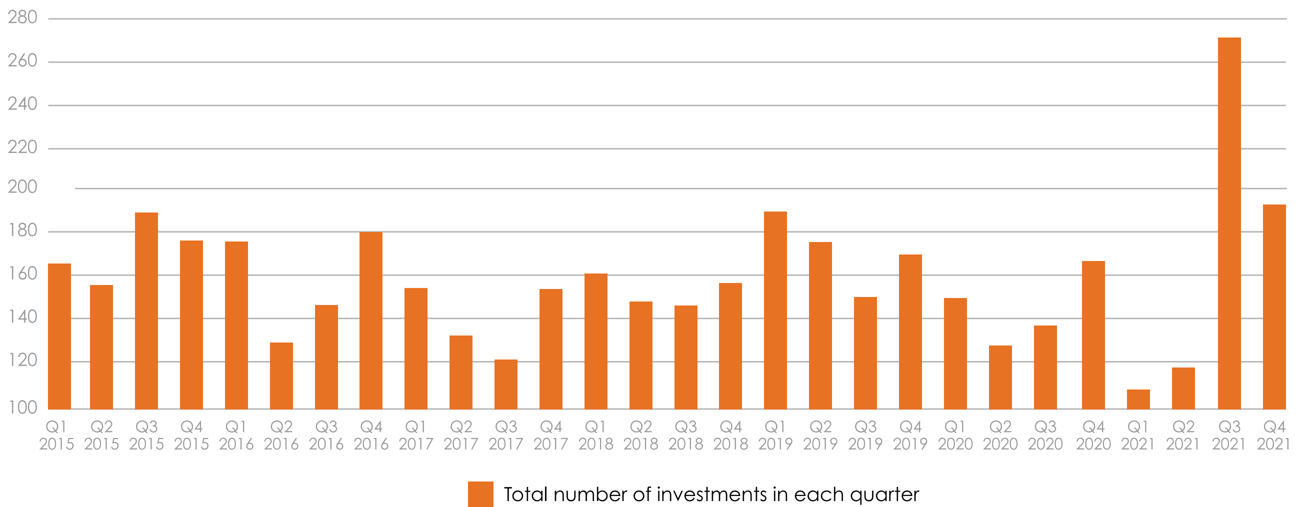
The revenue focus categorization for startups funded by VC has been tilted towards B2C, but based on recent quarters the funding preference has been moving towards B2B.

New or Follow-on VC Investments Based on Volume



Source: Venture Intelligence, CAIA Analysis

Volume of VC Investments



Source: Venture Intelligence, CAIA Analysis

Shreekant Daga
Associate Director, CAIA Association

Investing: Art or Science?

Takeaway: The science is about sector expertise that allows you to pick the macro segments well. The art is a nuanced judgement on the founder and management team.

Investing: Art or Science?

If one were to ask a contingent of investment professionals, 'Is investing an art or a science?', the popular answer may be quite predictable. There are codified frameworks on financial modelling, triangulation of valuation, technical/fundamental analysis of listed companies and so on – all of which make investing sound like a fully rational, technical activity; a science, if you will.

But if investing is a science, why do some investors generate a substantially different alpha in the same vintage?

Let us take a step back. Investing is about crystal ball gazing into the future 5-10 years to predict the potential of a business. Aim to build a detailed financial model and identify the top 3 assumptions that move the needle for the business. So, while modelling is a science, isolating the key assumptions is an art. Sometimes the key assumption may be an unknown risk factor and thereby may not even find a place in the financial model.

"Founders who have surrounded themselves with capable team members to cover for their blind spots are a cut above."

The reality though is that no amount of diligence will be able to give definitive comfort as to how each of these key assumptions may play out. In many cases, especially involving business transformation, there may be no past track record to due diligence on. Ultimately, it is a leap of faith that one takes – some call this conviction, intuition or maybe art.

So, what allows one to take the 'right' leaps more often than not and make that superior judgment in a consistent predictable manner? Is it even possible to codify this? If you pick the macro segment well and within that invest behind the management team that has the best DNA to win, you will more likely than not get the investment right.

Our belief is that investing is a lot more art than science. The science is about sector expertise that allows you to pick the macro segments well. The art is a nuanced judgement on the founder and management team. There is enough evidence that management teams which have the right DNA to win in an industry are best placed to capture the macro opportunities in that industry. So how does one identify this DNA? In India, it is neither possible nor practical to ask founders to undergo a psychometric test.

The closest we can get to understanding the founder psyche is to actively look for traits based on the founder's past choices and behaviour. We use a proprietary 20 factor model called Leadership Energy Level (LEL) to analyse the founder's DNA. These factors are then grouped to give us a picture on several leadership traits, such as how disruptive is the mindset, ability to influence, strategic agility, winning instinct and institution building capability.

We believe that these traits are important to assess irrespective of the stage and sector of the business. Obviously, the relative importance of each trait will be different depending on the choice of sector. For instance, in an early-stage consumer facing business, having a disruptive mindset may be more relevant than institution building.

This assessment brings to fore the natural leadership profile/style of the founder; their strengths and weaknesses. The question we often ask ourselves is how aware is the founder of their blind spots; how self-aware are they. Founders who have surrounded themselves with capable team members to cover

for their blind spots certainly are in another league, a cut above – they are aware, humble, accepting and will not allow themselves to limit the potential of the business. Ultimately, it is the people behind the business that create value.

As PE investors, we get ringside seats to a founder's journey and an opportunity to influence the outcome. This ability to influence the founder in minority investments is an earned right – it is effective only if it is commanded and not demanded. An investor earns the right to influence if he has the empathy to understand the founder, comes with the mindset to listen and not just tell; and more importantly gives the founder confidence to unleash his full potential. An investor who is constantly second guessing the founder makes for a very nervous boardroom conversation.

To summarise, successful investing is all about:

- Careful selection of the sub-segment to invest based on the macros
- Picking founders who have the DNA to win in that segment
- Enabling the founders to succeed by realising their full potential

AUTHOR'S BIOGRAPHY

Sridhar Sankararaman
Managing Director, Multiples
Alternate Asset Management

Sridhar has 2 decades of experience in financial services (including 15 years in private equity). He joined Multiples (US 1.5 bn PE fund manager) close to its inception in 2009. He currently leads investments in digital, B2C and consumer technology sectors. Previously, he led investments across healthcare, pharma and manufacturing sectors. He has actively contributed to building investment and founder evaluation frameworks for the firm.

During his investing career, he has been able to connect well with Founders and influence them on strategy and people decisions. He thinks of his ability to influence as his key strength and uses it to bring about positive change. He enjoys brainstorming ideas with Founders and derives immense satisfaction when they derive value from these interactions as well.

Sridhar received his MBA from Indian School of Business and is a Chartered Accountant by training.

Sustainable Investing in India – A Major Opportunity to be Tapped

Takeaway: Demand for investments that support more sustainable lifestyles is growing exponentially. What the Indian investment community needs is a thorough understanding of the positive and negative impact that growth sectors can have on our environment. Consistent data will be a key factor.

Sustainable Investing in India – A Major Opportunity to be Tapped

Despite the news headlines about raging floods and uncontrolled forest fires across the globe, action to limit the effects of climate change is far short of what is needed to get the world back to net-zero. In recent years though, the investment community has focused its attention on sustainability.

There is little surprise that sustainability is taking the centre stage in the world of finance and economics. Investors are looking to invest in environment-friendly companies, protecting their returns over the long term. At the same time, the definition of sustainability expands to encompass wider economic activities and create new opportunities for investors to contribute to change.

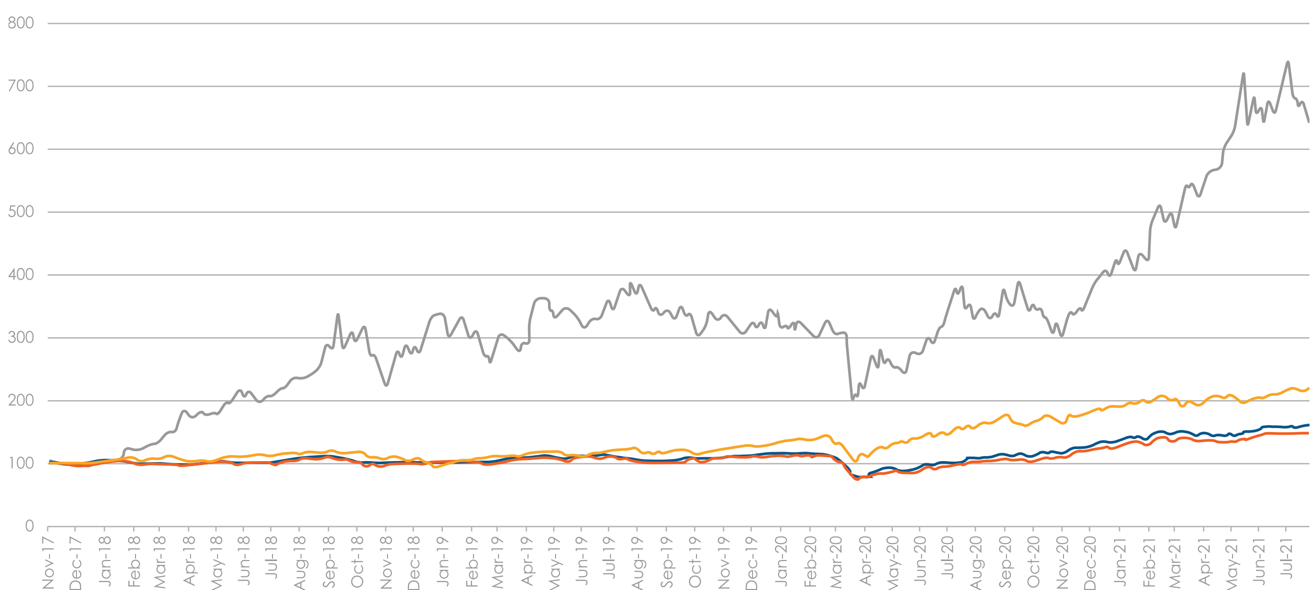
An increasing number of global investors are making sustainability the core of their investment strategy. Global investors with assets of $43 trillion (around half of global institutional capital) have pledged to reduce the carbon footprint of their portfolios in line with global pacts and benchmarks.

At CDPQ, we set a target in 2017 to reduce the carbon intensity of our portfolio by 25% by 2025. It is encouraging to report that by the end of 2020, the carbon intensity of our portfolio had fallen by 38%.

On the demand side as well, many recent surveys show that Gen Z prefers sustainable products more than other categories. In India, there has been 190% growth in online engagement on environmental issues, with about 70% of customers saying they are willing to shift to more sustainable brands .

"India has a big role to play in the global need campaign for reducing carbon emissions. Yet, Indian sustainable investing is yet to pick up the pace in India."

EUA, which is the European mechanism for buying carbon offsets, is up 6.5x in the past 3.5 years – much ahead of the NASDAQ and Indian markets (BSE 100 and even the BSE ESG index). This reflects substantial demand for sustainability-linked solutions and outcomes.



Source: S&P BSE, EUA, Nasdaq

India Has a Huge Opportunity Ahead

India is already seeing some of the adverse effects of climate change. It has many of the world's most polluted cities and has seen a doubling of the number of cyclones in the Bay of Bengal. Large swatches of the population reside along the coastline and the erratic monsoon rains create serious risks for millions of Indian farmers who rely on rainfall for irrigation.

Rapid action on climate change is essential. It has been estimated that if India can reach net-zero status by 2050 instead of by 2090, it would lead to savings of 41% of the global climate budget. We reach net zero when the amount of greenhouse gas we produce is no more than the amount taken away. So, India has a big role to play in the global campaign for reducing carbon emissions. Yet, sustainable investing is yet to pick up the pace in India.

On the brighter side, large scale renewable energy has attracted about $8 billion of capital over the past few years. In 2021, installed capacity of solar energy had gone up to 40 GW in India, much ahead of its initial target set in 2015. According to Venture Intelligence, $6 billion of capital has been invested in Series B (or prior stages) in companies in cleantech or socially sustainable business, in the past 5 years.

However, this is woefully short of what is needed. For example - India's target of achieving installed solar power capacity at 280 GW by 2030 will require more than $250 billion of capital. A similar magnitude of investment is required in other areas like electric vehicles, where India has barely scratched the surface.

Investor Experience Has Been Encouraging

One argument made against sustainable investing is that imposing investment restrictions or forcing divestments means the sector will struggle to generate returns; therefore capital available will always remain short.

But sustainable investing is no different from traditional investing, wherein carefully selected and well-built organizations will produce outsized returns for their investors. Given that the sector is still relatively recent, some companies may take time to become bigger and hence the sector will need patient capital.

Recent research indicates that global cleantech investments have grown 37x in the past 6 years and

Principles/ SDGe	Reduced Inequalities	Sustainable Cities And Communities	Responsible Consumption & Production	Climate Action	Life Below Water	Life On Land	Peace, Justice & Strong Institutions	Partnership For The Goals
Principles 1							✓	✓
Principles 2	✓		✓	✓	✓	✓		
Principles 3		✓					✓	
Principles 4		✓					✓	
Principles 5							✓	
Principles 6	✓		✓	✓	✓	✓		✓
Principles 7	✓	✓		✓	✓	✓		✓
Principles 8		✓		✓	✓	✓	✓	✓
Principles 9			✓		✓	✓		

Source: Business Responsibility and Sustainability Reporting

these companies are already giving substantial returns. Among the latest crop of Indian Unicorns are four companies focused on renewable energy – a sector that looked like a small experiment just a decade ago.

The introduction of 1.75 million electric rickshaws in the past 6 years is another good example of scaled-up demand for useful sustainable products in India.

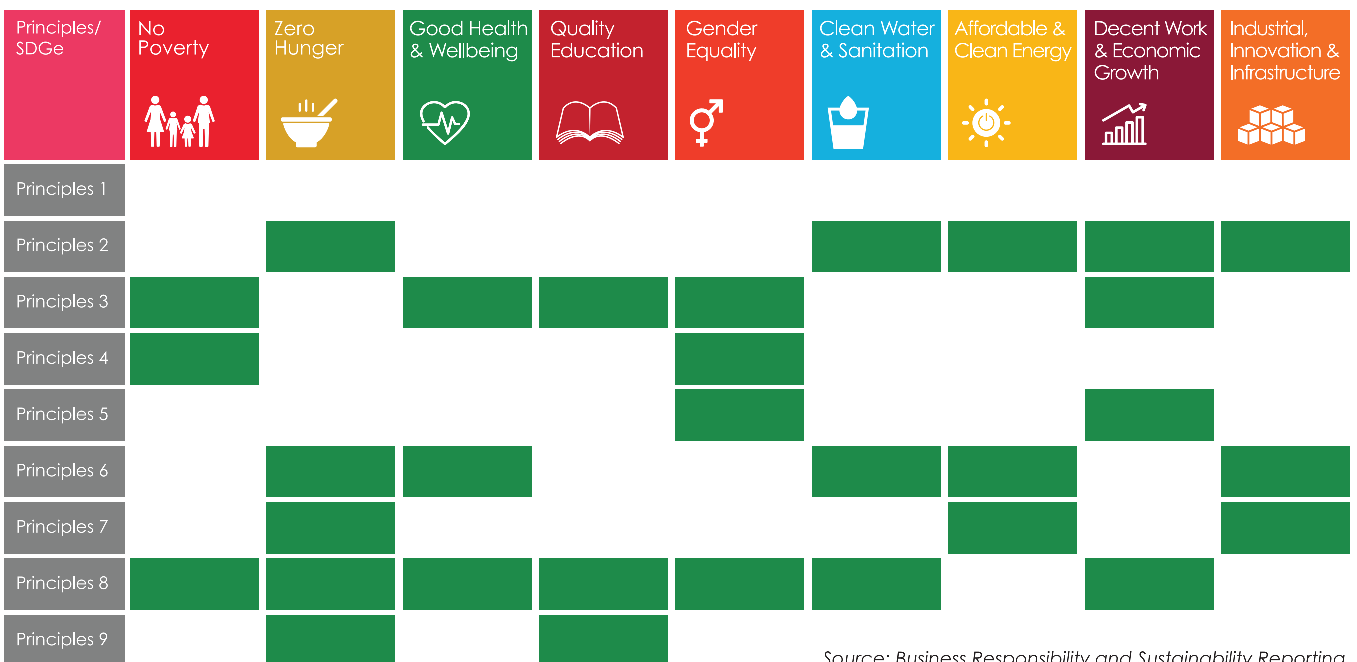
Considering that governments across two-thirds of the global economy have committed to carbon reduction targets, with more research and scale the cost of sustainable technologies is set for a dramatic fall. This, combined with increased demand, will ultimately produce greater returns.

India's per capita emissions are currently lower than most equivalent nations, but as the country industrialises, this is projected to grow. For India, this is an opportunity to capture economic growth with more advanced sustainable technology instead of adopting conventional ones; the classic technology leap, such as leapfrogging into digital payments without adopting physical credit cards.

Sustainable Investing is About Transforming Economies and Not Just Energy

It is important to remember that sustainability needs to be embedded in every sphere of the economy. For example, the current chip shortage in the world is linked to fresh-water availability in Taiwan. Increasing awareness of ocean plastics and the damage to marine life is making sustainable packaging important for customers. Sustainability has to take account of biodiversity as well as climate and environmental concerns. Therefore, even in conventional investing, there is huge scope to add sustainability elements.

Recently introduced 'Business Responsibility and Sustainability Reporting' (BRSR) will maintain the pressure on the 1,000 largest listed companies in India. The nine principles in the BRSR report rightly cover all the UN Sustainable Development Goals and will force large Indian companies to take a holistic view of sustainability.



Principles/ SDGe	No Poverty	Zero Hunger	Good Health & Wellbeing	Quality Education	Gender Equality	Clean Water & Sanitation	Affordable & Clean Energy	Decent Work & Economic Growth	Industrial, Innovation & Infrastructure
Principles 1									
Principles 2		✓				✓	✓	✓	✓
Principles 3	✓		✓	✓	✓			✓	
Principles 4	✓				✓				
Principles 5					✓			✓	
Principles 6		✓	✓			✓	✓		✓
Principles 7		✓					✓		✓
Principles 8	✓	✓	✓	✓	✓	✓		✓	
Principles 9		✓		✓					

Source: Business Responsibility and Sustainability Reporting

For investors, this has wide implications because a business that is not prepared for a thorough scrutiny via the BRSR framework may not attract quality investors, thus it may have limited multiple expansion. Moreover, existing companies will also need to adapt their business models to a sustainable basis to continue attracting quality investors.

There are other practical challenges in that India does not yet have a taxonomy of what qualifies as 'sustainable'. There is a push to harmonize ESG standards across the world, with IFRS launching the Sustainability Standards Board (SSB) at COP 26 last year. This and other global and regional pacts on climate and sustainability will eventually coalesce into a recognised best practice on ESG.

A well-articulated standard for sustainability will help both businesses as well as customers. For example, star rating of electrical goods helped the customers to buy more energy-efficient products, as a result this scheme along with other energy efficiency schemes helped India save 10% of electricity consumption in 2020.

Opportunity For Better Business Fundamentals

Ultimately, sustainability must be looked at as an opportunity for businesses to reduce risk and save costs over the longer term. There are many examples of Indian companies taking the lead in water conservation, responsible use of resources and the circular economy. They are benefitting immensely in terms of lower costs and a lower environmental footprint. We all need to do a better job of articulating and replicating such successes.

India can convert many of the challenges it currently faces into sustainable investment opportunities. For example, about 40% of Indians will still not have access to fresh water by 2030; this is a challenge but also represents a huge opportunity.

The use of technology will help India achieve more with less and faster. With tools like artificial intelligence, machine learning, 3D printing, and the Internet of Things (IoT), there are further efficiencies that may be unlocked for businesses that relentlessly focus on making their processes sustainable. India's software capabilities present a comparative advantage for it to leapfrog into sustainable, state-of-the-art manufacturing.

It is important that investors address climate change and India's development as an economic powerhouse presents an opportunity to build organisations of the future in areas critical to human survival.

AUTHOR'S BIOGRAPHY

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Harsh is a senior investment professional with experience across emerging markets. He is currently Managing Director with CDPQ India. Previously Harsh has worked with International Finance Corporation. He is passionate about spotting trends early and succeeding through investments and activities which lead to sector transformation and build organizations of the future. Harsh has experience across asset classes i.e. Private Equity, Public Equity, Infrastructure and Fixed Income. Harsh is a fellow member of Institute of Chartered Accountants of India and holds a management degree from Indian School of Business, Hyderabad.

Private Market Investments: The Family Office Experience

Takeaway: Private market investment could be a good gateway to scan various opportunities and convert some of these financial investments into strategic ones over time.

Private Market Investments: The Family Office Experience

Most family wealth has been created by building and nurturing one or more businesses. Having created their wealth, they now grapple with some of the common challenges regarding wealth and legacy: Where and how should I invest? What legacy do I create for my next generation and for the wider society?

While each family has its own mantra for creating wealth, they are continuously seeking new perspectives on how they should invest. They often go through an elaborate exercise of investment management trying to generate alpha by actively managing the portfolio.

In the case of public markets, the performance data shows that the majority of active investment managers fail to deliver alpha consistently and end up closer to market beta over an extended period.

In order to generate that elusive alpha, at times, a portfolio manager may take more risky bets. If large caps do not generate alpha, moving towards mid-caps or small-caps, or taking some momentum bets. A move towards lower-rated bonds with higher yield is equally common. Here, alpha is more often a result of taking increased risk, rather than better active management. When the bull run is over, such risks often come out in the open.

"NextGen may not be interested in the family business, or they may well have a different approach to the business and its work culture."

Family investors have come to see this reality and are now reallocating into passive funds to save the fees and costs associated with active management. ETFs and index funds are the boom areas of retail fund management.

An alternative route to generating alpha would be a more refined asset allocation. Additionally alpha can be generated by investing in private market assets.

Why Private Markets

It feels strange when business families ask, 'why private markets?' given that most of their wealth has been created by investing in and building businesses of their own. Possibly, they see the new-age startup ecosystem as an attractive opportunity, yet vastly different to their own family businesses and therefore inherently riskier.

Similarly, there are opportunities to invest through structured debt, based on the cashflows or underlying assets of growing enterprises. Opportunities such as revenue-based financing and Capex to Opex models are great avenues for high yield investments.

One can invest in public markets as well by following a private market approach of long-term investing in a few select businesses (PIPE approach). There are examples of investors who have done this successfully.

It is important to note that private markets do come with their own set of risks related to liquidity, valuation or exit. One has to factor the risks and possibly consider reallocation of risk from active public markets to private market investments to generate alpha.

For private market investment to succeed, one should also be able to attract the best of the technologies/innovations/opportunities; scan them, invest in them and then actively monitor them. This also requires collaboration with other pools of capital and a wider institutional network, so that there can be a shared ecosystem benefit.

Family Legacy

Family legacy refers to ensuring that future generations are armed with the knowledge and know-how to take the family success forward. This is easier said than done. Most families struggle with it, particularly beyond the second generation. NextGen may not be interested in the family business, or they may well have a different approach to the business and its work culture. Often, they are the ones who have studied overseas at the best universities. They have formed a different worldview and are trying to find disruptive or new age ideas.

Private market investment could be a good gateway to scan various opportunities and convert some of these financial investments into strategic ones over time. This allows the NextGen to witness the journey of building businesses and surround themselves with the best of founders and entrepreneurs. Private market investment, in that sense, actually plays a complementary role in building family legacy.

Societal Legacy

In order to do good for society, first let's understand the challenges and then look for a sustainable and institutional solution to address them. Philanthropical capital plays its part but cannot provide the long-term support required to tackle challenges at scale.

Climate change is a core challenge of this century. There is a significant emphasis on sustainability in every facet of business today. Need for access to affordable health care with greater emphasis on wellness cannot be ignored. Increasing farm productivity through sustainable agriculture and improving the farm value chain for enhancing farmers' income is required to ensure food security. This is not an exhaustive list.

What if private investment can be directed towards building businesses or enterprises to solve some of the pressing needs of the society? Here we are not talking about a philanthropic or impact type of investment, but a mainstream way of evaluating a private market investment. There is no compromise on return, just an orientation of enterprise selection which is towards solving the core challenges of society.

When private market investments are directed towards solving core social needs, they can meet some of the objectives of building societal legacy. With the right approach, families can build a strong foundation of human and social values for the NextGen to build on.

Private market investment can be a key approach to creating wealth, building legacy and serving society.

Welcome to a new breed of private market investments, where doing well and doing good do not have to be mutually exclusive.

AUTHOR'S BIOGRAPHY

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Founder, Blue Ashva Capital

Satya is the founder of Blue Ashva Capital, an investment firm based out of Singapore and India, backing sustainable and profitable businesses which are solving real challenges in sectors such as Food & Agri, Energy & Environment, Health & Wellness, Money & Finance.

Satya Bansal is an industry veteran with over three decades of rich experience in the Banking and Financial Services sector. Prior to founding Blue Ashva Capital, he was the Chief Executive of Barclays Private Bank, India for more than a decade and played a pivotal role in setting up the Private Banking business in India. He has also been the Head of Private Banking- South East Asia for ICICI Bank.

Satya is known to be an intrapreneur throughout his corporate career wherein he built standalone sustainable businesses within large organizations. He has been an active investor in the startup ecosystem for more than a decade having invested in both mainstream and impact startups globally.

Satya is a Chartered Accountant and has also undertaken Advance Management Program at Harvard Business School.

Evolution of the Exit Environment

Takeaway: The exit environment in India has been evolving. From a few narrow options available to founders some years ago, the exit options have increased dramatically. The rapid increase in the number of startups in India and the options available now to first-time entrepreneurs, who embark on a journey of wealth, can now be well-rewarded with various exit alternatives.

Evolution of the Exit Environment

Chess is a game of strategy. At the very start you need to envisage the endgame, then plan for the middle game and accordingly, make moves in the opening game. It may sound odd that one needs to plan the final outcome before moving the first piece on the board, but that can determine success or failure. As the game progresses, a seasoned chess player is also able to foresee more than eight possible moves – in fact, that is the hallmark of a champion.

The strategies used for playing chess hold important lessons for startup founders as well. Founders start with an innovative idea and a plan, build an MVP and gear up to pilot the product or offering. From here they build their business to scale. The endgame is an eventual exit. Analogous to a game of chess, founders need to have a different plan for each phase, envisioning their final move.

The startup sector in India has recently witnessed some feverish action. India had 16 unicorns created in the first half of 2021. There are now more than 70 unicorns in India and the number is likely to exceed 150 by the year 2025.

Just as the startup sector has evolved over the past three decades, so has the scope and variety of options for exit. The merger of startups into large companies is a time-tested option for exit. It gives satisfactory returns to the founders on their investment and the larger company, in all likelihood, will decide to merge all the products into their domain and absorb the innovation or the technology. By and large, in this merger process, the startup is submerged into the larger company.

As the importance of human capital has gained prominence, a new method of exit has evolved – 'acqui-hire' - a portmanteau of 'acquisition' and 'hiring'. Large companies may not have the structure and the DNA of rapid innovation and may rely on acquiring these assets from outside. In a people-intensive business, acquiring a startup primarily to recruit its employees and also gain control of the products and services could become a strategic move.

Acqui-hire is normally done for businesses which are adjacent to the main line of business. Normally, the founders get returns of around 3x to 5x of the investment made and it ensures that the technology or product survives in a larger company with more resources.

"There are many more startups now looking to do an IPO and a slew of them have hit the market."

If the startup has developed a strong IP around a product, there is also the possibility of a larger company merely acquiring the IP for a price and not the entire startup. This is a neater option for the larger company, as it does not need to bother about taking over the existing employees, doing a due diligence of the startup and engaging in other formalities. For the startup founder, it might also provide a faster exit route to encash the IP created.

If a startup scales rapidly and crosses a significant landmark of recurring revenues, it could become a potential target for PE investors. These investors have the capability to invest large sums of money to take control of a startup and put all the resources at their command to build scale in the business.

PE firms may invest large sums, appoint their own management team, give strategic inputs and bring it to a point where they can sell their stake to some other firm for a profit. Some PE firms, particularly in the US, have teams tasked with managing operations in companies in which they invest. In all these situations,

the founder would have cashed-out from the startup and would not be involved in the operations and management. Since PE firms are known to have deep resources for investment, they have the ability to buy out founders of startups and invest as much money as required for the business.

July 23rd 2021 was a historic day for startups, as Zomato was listed on the stock exchanges in India. Floating an IPO is the final 'judgement day' for a startup. Prior to the IPO of Zomato, the listing regulations in India did not permit startups with losses to list on the stock exchange. This tweak in the regulations has now opened up a huge opportunity for startups to list on the stock exchanges, despite incurring losses.

The mega public issue of Rs. 9,375 crores (USD 1.3 billion) of Zomato at a price band of Rs. 74-76 saw it over-subscribed 38 times - a strong response from investors (IPO valuation of USD 8 billion). Zomato is the first Indian internet unicorn to make its stock market debut. This public issue was the largest to hit the stock markets since the large IPO of SBI Cards in March 2020. After its debut, much to the dismay of those who predicted that the stock was overpriced, the share price held firm and increased by more than 40% over the IPO price.

There are many more startups now looking to do an IPO and a slew of them, including PayTm, have hit the market. For founders of startups as well as investors, this has now opened new possibilities of an exit. It is most likely that the founders which go for listing will sell part of their stake in the IPO and continue to manage the company. Importantly, it leads to a transparent price discovery of the startups and the founders are able to sell their remaining stake when required.

AUTHOR'S BIOGRAPHY

Ninad Karpe
Partner, 100X.VC

Ninad Karpe is a Partner at 100X.VC – a VC firm, which invests in early stage start-ups and aims to invest in 100 startups every year.

Karpe was the MD & CEO of Aptech Ltd. for more than seven years, till 2016. He previously served CA Technologies, a US headquartered leader in software products, as Managing Director of India.

Karpe has authored a book on business strategies, titled "BOND to BABA", which received rave reviews and was listed by Amazon in its prestigious list of "Memorable books of 2018".

He was the Chairman, Western Region of the Confederation of Indian Industries (CII) for 2017-18, an honorary position.

Besides his day job as a VC, Karpe is passionate about supporting theatre and has produced two Marathi plays, which have received wide acclaim. An avid follower of F1 racing, he switches off his mobile phone during race days.

Exit Trends and Developments

Takeaway: The traditional entry route of JV with an existing listed Indian corporate may see a decline, especially for sectors where technology is an underlying platform.

Exit Trends and Developments

The last several years have been peculiar with each year spelling out a different story: 2016 saw the highest number of exits count for return multiples ranging from 3 to 5x; 2017 and 2018 saw the highest exit activity on volume and value basis, respectively; 2019 witnessed a large number of lower multiple (1-3x) deals resulting from a higher number of public market exits; 2020 saw a quiet harvesting year for lower multiples or quicker turnaround deals.

The harvesting environment showed a strong recovery in 2021 with the highest exits recorded in Indian PEVC history. The interesting aspect of exits in 2021 is that complete exits accounted for $22.8 billion. Investors harvested only $6.8 billion in 2020, which was down by close to 35% when compared to 2019, and down by close to 50% when compared to 2018, even after excluding the Flipkart Exit.

The Flipkart deal was a landmark transaction not only because of its size but also because it points towards an entry route for large companies to enter India. Several unicorns in years to come are expected to facilitate the entry of multi-national corporations (MNCs) and could account for a lion's share of deal value. The traditional entry route of JV with an existing listed Indian corporate may see a decline, especially for sectors where technology is an underlying platform.

The linkage between public market exits and public market performance is still strong. In the first quarter of 2021, a large proportion of exits, around 45%, have come through public market sale. In 2017, 2019 and 2020, when the preferred exit route was again a public market sale, the NIFTY 50 market index gained over 18% on average.

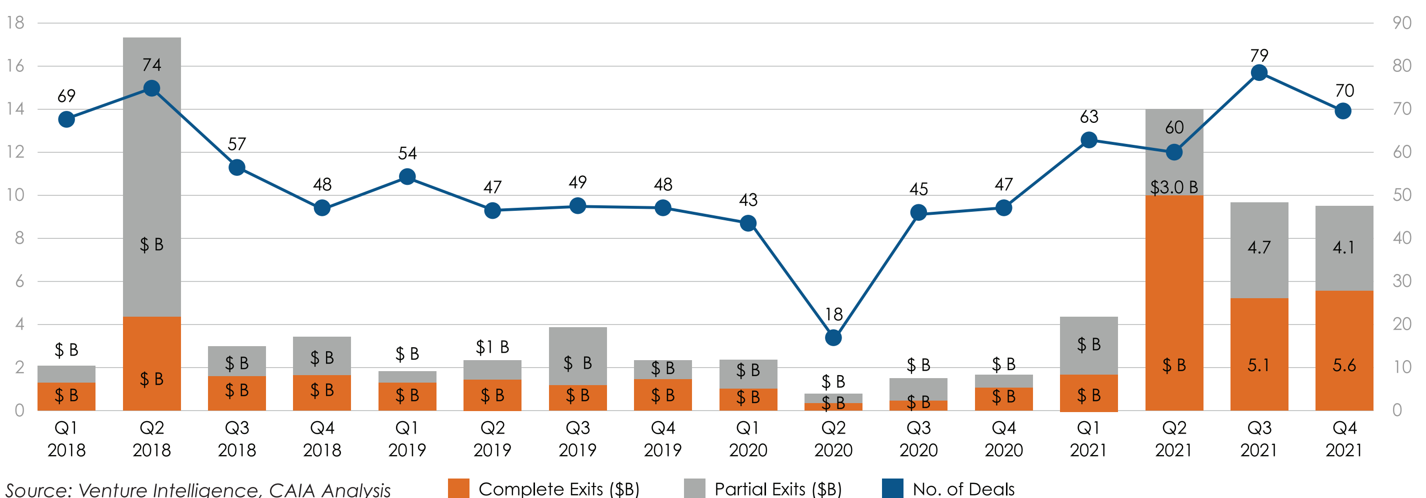
The average size of exit deals is largest for strategic sales, followed by secondary sales. Public market deal sizes are relatively smaller given the price impact of larger deals. For example, the Carlyle exit of SBI Cards was done over several quarters, rather than offering the stake for sale altogether. This is typically the case in years when public market performance isn't as strong.

IT & ITES Sector Dominate PEVC Exits

The IT & ITES, BFSI and Health Care sectors are the most active, with IT & ITES the most prominent, largely emanating out of South India (majorly in and around Bangalore).

The cumulative exits for the last 20 quarters stand at around $100 billion, over around 1,200 transactions. Q2 CY21 alone accounted for more than $14.3 billion exits. The average exit size of deals has ballooned in 2021 across IT & ITES, BFSI and Health Care & Life

Private Equity and Venture Capital Exits by Quarter



Source: Venture Intelligence, CAIA Analysis

PE and VC Exits by Type Ranked

Exit Type	Amount in US Million					
	2021	2020	2019	2018	2017	2016
Public Market Sale	12,129	3,395	4,265	2,912	5,925	3,209
Secondary Sale	11,034	1,428	2,522	5,805	3,320	1,838
Strategic Sale	14,549	1,683	1,800	15,576	3,357	3,275
Buyback	1,026	164	1,748	1,779	1,848	338
Rank		1	2		3	4

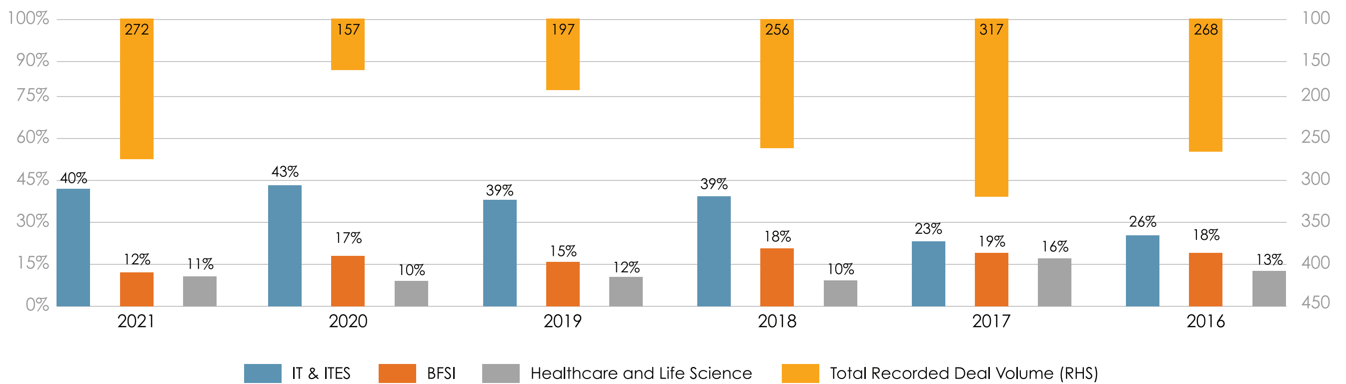
Source: Venture Intelligence, CAIA Analysis

Sciences. Across the 3 sectors the average exit deal is pegged to $180 million which is close to 3 times the running average for the preceding 5 years.

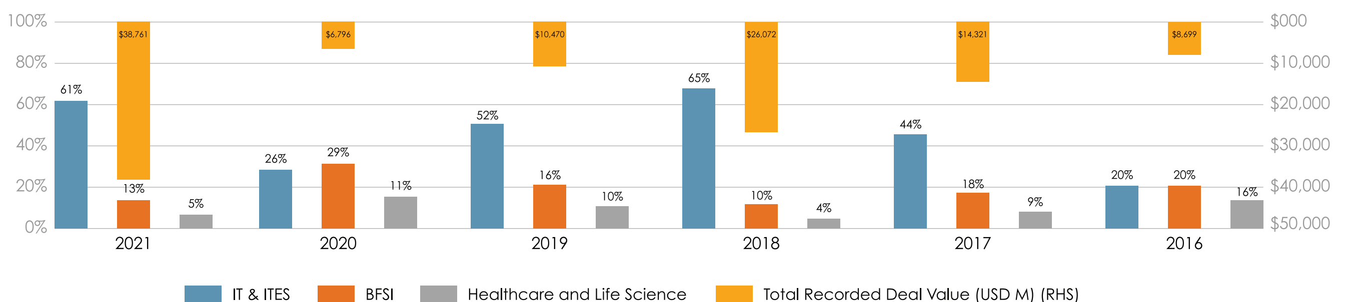
The average holding period for the top 10 multi-bagger exits across 2021 is around 9 years. The more liquid, lower multiple exits were impacted in 2020 due to the industry wide slowdown, but the long-term investments which provide higher multiples follow a similar trajectory to pre-Covid times.

In 2021 there were very encouraging signs of fruitful harvesting, recording 10 transactions with 22x+ return multiple. The average holding period for such deals was 9 years and a quarter. As 2021 was a great year for harvesting, 2022 promises to be on similar trajectory.

Sectoral Exits Share by Volume

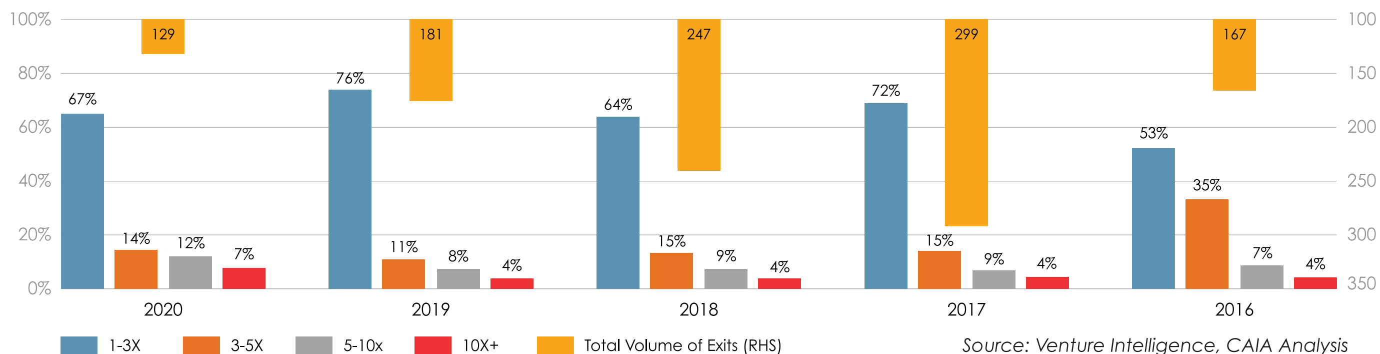


Sectoral Exits Share by Value



Source: Venture Intelligence, CAIA Analysis
Consideration: IT & ITES, BFSI and Health Care & Life Sciences are the major sectors for the industry.
Other sectors exist but no significant trends can be observed for specific remarks.

PE and VC Exits by Returns Multiple



Source: Venture Intelligence, CAIA Analysis

TOP PE Exits of 2021

Company	PE Firm(s)	Type	Acquirer	Return Multiple	Avg. Holding Period(yrs)	Exit Period	Exit Amount (INR Cr.)	Post Deal Valuation (INR Cr.)	Trailing Revenue Multiple
Zomato	Info Edge	IPO	NA	65.52	10.92	Jul-21	375	60,000	28.15
BillDesk	Clearstone	Strategic Sale	PayU	60.78	15.18	Aug-21	2205	34,310	18.00
Aptus Value Housing Finance	Granite Hill	IPO	NA	54.31	11.59	Aug-21	353	16,498	27.48
Sugar Cosmetics	India Quotient	Secondary Sale	Elevation Capital, A91 Partners	49.00	7.76	Feb-21		619	6
Playsimple	Chiratae Ventures	Strategic Sale	MTG Gaming AB	45.87	6.59	Jul-21	386	2,686	4.43
Nazara Tech	WestBridge	Secondary Sale	Plutus Wealth Managment	44.20	15.26	Jan-21	500	2,365	9.52
Nykaa	Sharrp Ventures	IPO	NA	33.52	5.17	Nov-21	180	7,153	21.69
Big Basket	Ascent Capital	Strategic Sale	Tata Digital Ltd	26.00	9.17	Apr-21		13,810	3.64
Play Simple	Elevation Capital	Strategic Sale	MTG Gaming AB	24.76	4.67	Jul-21	528	2,686	4.43
Purple	IvyCap Ventures	Secondary Sale	Sequoia Capital	22.00	6.17	Mar-21	330	2,200	25.35

Source: Venture Intelligence, CAIA Analysis

Shreekant Daga
Associate Director, CAIA Association

Rise of Venture Debt in India

Takeaway: Growth debt may not be the right choice for every firm, especially for those without a strong and stable business model, however it can be an efficient move for founders who have already gone through several rounds of financing, but need additional funding to reach their next milestone.

Rise of Venture Debt in India

The venture debt model originated in Silicon Valley in the 1970s and has since become an established form of alternative capital that is available to VC backed companies globally. Many well-known technology companies have taken venture debt at some point in their growth journeys including Google, Facebook, Uber, Airbnb etc.

At its core, venture debt is entrepreneur-friendly as it helps founders and cash-hungry startups avoid over-diluting shareholder equity at early stages of a company's growth. Used appropriately, venture debt can also extend the cash runway between fundraising rounds, sometimes helping companies achieve performance targets set by equity investors (or avoid dreaded valuation down-rounds). Another benefit of venture debt is that, in appropriate instances, it can support companies facing unexpected market turbulence or short-term capital traps as witnessed during covid times.

Factors Leading To Emergence of Venture Debt

The traditional banking system has several lending criteria that do not apply to startups; things like profitability, business vintage, financial history and sufficient collaterals, with a preference for hard collaterals, personal guarantees, etc.

The turnaround time of traditional banking is also unhelpfully lengthy, while for high-growth companies, timely availability of capital is the key.

Traditional lenders typically have domain expertise limited to traditional businesses and industries, while startups, by their nature, are set up to disrupt the old industries and therefore need to be assessed with a different lens.

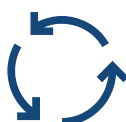
While PEVC provides the necessary growth capital for startups to prove their business model and scale up, it's still an expensive source of capital and leads to dilution of a promoter's equity. Hence, high growth and cash-hungry startups prefer debt for their working capital requirement or for any specific capex or contract financing requirements. This helps founders to avoid the risk of losing out on richer valuations at the later stage exit options, when the company grows to its full potential.

The cost of the venture debt is also tax deductible, resulting in lower after-tax cost of capital.

Type of Venture Debt Investments

Venture debt can structure financing best suited to a business and its characteristics. Apart from lending against defined repayment structures, venture debt firms prefer to have an option to subscribe to equity of the company to the extent of 10%-15% of the debt amount. The primary objective is to enhance returns through an equity kicker.

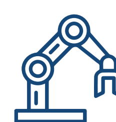
Term Loan/NCD



Revolving Credit Facility

Revenue Linked Loans

Rceivable/ Lease Discounting



Equipment Financing

Contract Financing

Right Time to Avail Venture Debt

Venture debt's biggest drawback is that it is not readily available to startups that have not done an institutional VC round.

Since most startups are burning cash to scale their business, there is a constant need of equity infusion for various activities including debt repayment.

Hence, venture debt is not a replacement for equity. While VC firms bring sector expertise, growth knowledge and are the first line of backers for a startup, venture debt augments this and supports both the founder and the investors through the journey. It is also generally limited to 20% of the equity fundraise.

Therefore, most venture debt firms show interest post the Series A equity round, as by then a startup would have proved its business model and is entering the growth phase. Similarly, a new entrant in the lending industry is Revenue Based Financing, which links repayments with revenue of companies and therefore lends even to Pre-Series A startups.

Case Study

A Healthtech startup raised an initial round of angel and seed capital and reached a revenue of $3 million. The company is expecting to grow its revenue at an average of 6% per month over the next few years and is therefore looking to raise further capital.

As can be seen from the tables, here the Healthtech startup clearly has an advantage by using a mix of VD and VC rather than just VC funds. The mix of VD and VC led to the extension of runway of the startup by 4 months (from Nov-22 to Mar-23) and ~5% less dilution of the promoters.

"Since most startups are burning cash to scale their business, there is a constant need of equity infusion for various activities including debt repayment."

Investment Rounds Without Venture Debt

Particulars	Apr-21	Nov-22
Investments Round	Series A	Series B
Invested Amount ($ Mn)	5	8
Pre-Investment Revenue ($ Mn)	3	9
EV/Revenue	5	3
Enterprise Value ($ Mn)	15	26
Runway (months)	18	24
Investor's Stake (%)	33%	54%
Founder's Stake (%)	67%	46%

Investment Rounds With Venture Debt

Particulars	Apr-21	Jul-21	Mar-23
Investments Round	Series A	Venture Debt	Series B
Invested Amount ($ Mn)	5	1	8
Pre-Investment Revenue ($ Mn)	3	4	11
EV/Revenue	5	NA	3
Enterprise Value ($ Mn)	15	NA	32
Runway (months)	18	19	24
Investor's Stake (%)	33%	33%	49%
Founder's Stake (%)	67%	66%	51%
Venture Debt's Stake (%)	-	0.8%	0.6%

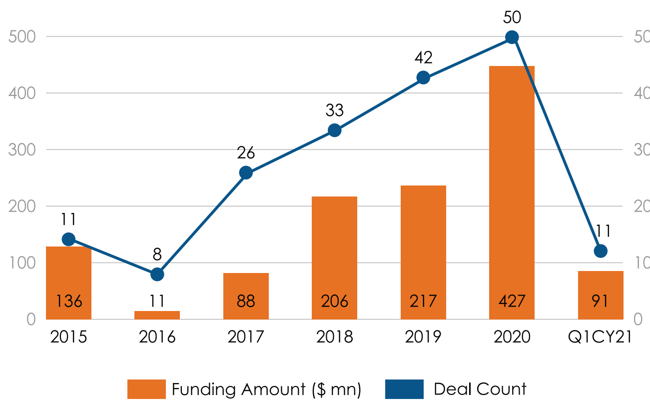
It is true that growth debt may not be the right choice for every firm, especially for those without a strong and stable business model, however it can be a wise and efficient move for founders who have already gone through several rounds of financing but need additional funding to reach their next milestone.

Some of the key benefits of Venture Debt over Venture Capital are:

1. Debt Financing is cheaper than equity
2. Debt allows to maintain control over businesses
3. Cost of Debt is Tax Deductible resulting in lower after-tax cost of capital
4. Debt can be made available faster than equity, as equity investment takes longer due to in depth diligence

Current Trends in Venture Debt

Venture Debt Funding in India



Source: Inc42 and Business Line

In India, the total amount raised by venture debt funds jumped from $62 million in 2020 to $85 million in 2021. Deals took place across diverse business models and industries such as e-Commerce, Fintech, Consumer Services, EdTech and SaaS. In Q1 2021, startups raised $91 million through venture debt financing, hitting a 25-quarter high. In CY21, venture debt financings were estimated to have grown by 40% year-on-year.

E-Commerce

Urban Ladder, bigbasket, Spinny, purple.com, CarDekho, industrybuying, Zetwerk, HomeLane.com, Furlenco

Education / EdTech

Eruditus Executive Education, BYJU'S The Learning App, classklap, toppr, iNurture Education Solutions, embibe

IoT

Active.Ai, emotix Emotional intelligence, Securens, ideaForge, zenatix

Logistics

Freightwalla, blowhorn, holisol, Rivigo, cogoport, GoBolt, Blackbuck

Finance / FinTech

Lendingkart, BharatPe, Aviom, MobiKwik, zest, EarlySalary.com, freecharge, mswipe

Food & Beverages

Box8, Licious, epigamia, paper boat, Raw Pressery, Rebel Foods

Online Content

dailyhunt, TVF, 123RF

SaaS

Deskera, Indus, WebEngage, Nowfloats, Intelligence Node, germin8 Social Intelligence

Healthcare

cure.fit, Koyé, Oliva Skin & Hair Clinic, 1mg, PharmEasy, HealthifyMe, practo, hospals

Mobility

Shuttl, ZipGo, Bounce, Vogo, Ather

Impact of Covid on Venture Debt

Startups are not sheltered from the disruptions caused by the Covid-19 pandemic. Many had to turn conservative in their operations when the first wave hit. As a result, the venture debt industry saw a boom during this period and came into the limelight as an asset class both for investors and borrowers.

Deal flow increased for venture debt firms, though only the startups with a strong business model, high capital efficiency and some degree of profitability were able to raise the required capital. Trending businesses sectors such as SaaS, e-Commerce, Gaming, Agri-Tech, Med-Tech, Ed-Tech & Logistics found it relatively easy to raise debt funding, due to the efficient tech play and tailwinds from Covid-19. Overall based on market reports, there was a doubling of venture debt funding from $217 million in 2019 to $427 million in 2020.

The pandemic has left a long-lasting impact on the way business is done. For some companies Covid-19 has been a blessing in disguise and they enhanced their business substantially on the back of technology. Others, especially in bricks-and-mortar businesses, felt the most heat and have had to resort to cutting cost, or even shutting up shop.

AUTHOR'S BIOGRAPHY

Ankur Bansal
Executive Director, Blacksoil

Ankur Bansal is Co-Founder & Director of BlackSoil Group, which is a new-age venture debt platform also focused on structured and real estate debt. With over 15 years of experience in idea origination, credit, M&A execution, investment thesis, commercial negotiations, and post-deal investment management.

Under his leadership, Blacksoil Group has made credit disbursements of over INR 1,650 Crs across 110+ transactions with 60+ notable exits at an average IRR of 18%. Blacksoil has provided INR 1,160+ Crs across 90+ growth and VC backed companies, such as – Oyo Rooms, Infra.Market, Zetwerk, Udaan, Koye Pharma, Furlenco, Purplle, EarlySalary, BTI Payments, Chumbak, Homelane, etc.

Previously, Ankur was employed with J P Morgan investment banking, Mumbai. He was also associated with Citi Group where he completed multiple complex capital market transactions encompassing equity, equity linked and retail bond deals across formats like IPO, QIP, FCCBs, block trades etc.

Ankur's academic background includes a degree from the Institute of Chartered Accountants of India, Chartered Financial Analyst (CFA) Institute and graduation from Narsee Monjee College of Commerce and Economics.

The Evolution of the Term Sheet in India

Takeaway: VC terms have become very founder-friendly and have broken away from PE terms. The focus is now less on downside protection and more on upside participation.

The Evolution of the Term Sheet in India

Founders and investors have benefited in recent years thanks to the positive undercurrents in the economy as well as the IPO boom. As a result, the investment term sheet has finally evolved from a scarcity mindset to an abundance mindset.

Intense competition for good deals and highly informed founders have also played a role in how the term sheet has evolved. VC terms have become very founder-friendly and have broken away from PE terms. The focus is now less on downside protection and more on upside participation.

Today it is common to see a pure one-time liquidity preference with all money at par. Earlier, there was invariably a waterfall depending on the series of funding and liquidation preference minimum of 2X or even 3X for investors. Double dipping was common too, particularly in growth stage rounds.

Today big rounds are being raised at high valuation, but many startups will hit the anti-dilution clause in subsequent rounds when the valuation parameters change in response to external market conditions. A full rachet can permanently damage a cap table, and founders and early investors will do well to ensure a broad-based weighted average anti-dilution clause.

Founders think of super pro-rata rights as a great validation of how hot their company is. But super pro-rata means that a large portion of the next round is already given to those who won't lead or price the round. Incoming investors find this clause almost impossible to work with.

Let's say that your lead investor in Series A owns 8% in the company but has got super pro-rata to go to 15%. If you raise $10 million in your next round at a $40 million pre, a 20% dilution, you will have to give almost half of the round to the existing investor and the investor who wants to lead will not get enough ownership. You will likely end up diluting much higher than 20%. You are merely deferring the problem.

If super pro-rata is complex to manage, think of a lot of convertibles that you raise between rounds. It's great to have those in a very small quantity but they can create the same damage to the cap table as super pro-rata would.

One change that has not happened is on the Employee Stock Ownership Plan (ESOP) pool. The responsibility of ESOPs is put squarely on the founders, and ESOPs are not counted in pre-money calculations. As more and more companies go public, investors need to solve for the founder equity upfront and price the ESOP pool from the pre-money calculations.

"Differential voting rights for founders are becoming common and board compositions are in favour of founders too."

Veto rights and voting rights are another thing that have evolved but have some way to go, as founders prefer more power with themselves. Differential voting rights for founders are becoming common and board compositions are in favour of founders too. The scope of veto rights has also diluted in the wake of shifting of power from investors. In good times, investors are OK to give these things a pass.

Finally, one cannot forget the contribution of social media and the internet in easing of the standard terms. There are enough sample term sheets on the internet and this ensures that no VC fund can try to put onerous terms and risk their reputation even while dealing with first-time founders.

Know Your Term Sheet: What it Says and What it Actually Means:

Due Diligence	We were rushed by you to make this term sheet- we will use this to actually decide on whether we will invest or not.
Vesting Clause	We bring the capital, and you bring the time.
Liquidation Preference	Our money has the first dibs. And if you are not watching, we might double dip too.
Anti-Dilution	It's just a simple formula and comes into play only if you do a down round.
Tag Along Right	If you sell and go away, who will we 'mentor'?
Drag Along Right	Let's create a long-lasting institution; at least till a FAANG comes calling.
Veto Rights of Lead investor	So, we spoke about the long rope we give to our Founders? This is how long it is....
Buyback	No, the company is not borrowing. This 30% IRR clause is just capturing the edge case. You got to trust us on this.
Lock in Period	If you need a bridge, you must responsibly find a new investor, but if you do well, I am in! In fact, we will invest more than pro-rata.
Reps, Warranties, & Indemnification	You know that workaround on the e-commerce laws we asked you to implement? Well, that's on you.
Sunset Clause	Long after we stop investing, you will feel our presence...
Exclusivity	While we decide on our investment during the 'diligence' it won't be fair that you look for other investors, right?
Diligence and Legal Expenses	The lawyer is my golf buddy and let's not get a reputation of being cheap.

AUTHOR'S BIOGRAPHY

Anand Lunia
Founding Partner, India Quotient

Anand wakes up every morning with one thought: 'Let's make India great again.' He loves writing on startups, studying market opportunities, and helping entrepreneurs.

Before India Quotient, he bet his farm (literally) on an angel investment in Rebel Foods, one of the largest cloud kitchens in the world. Earlier, he was a partner at Seedfund, known for its exits in Carwale and Redbus. He co-founded an edtech company which he exited in 2005.

His Twitter handle says it all: 'Entrepreneur is the king. Not the VC.' He feels that leading the simple, Indian middle-class life is an investor's superpower.

Unicorns in India

Takeaway: In 2021 the median period to attain unicorn status dropped to six years, which gives an indication of the pace of change.

Unicorns in India

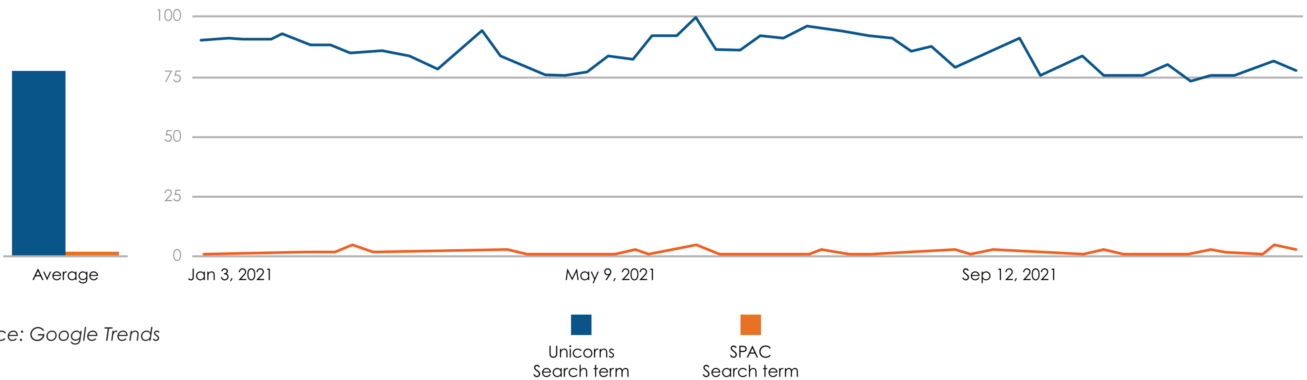
By the end of 2020, India had emerged as the third-ranked country on the unicorn count list and data from CB Insights shows that in 2021 India consolidated its third position. Venture Intelligence reports there were 70 live unicorns by 2021 year-end and another 7 added in the first 40 days of 2022.

Country-Wise Number of Unicorns at The End of the Year

	2021	2020	2019	2018	2017	2016
	484	242	169	110	59	40
	167	135	121	101	57	34
	55	24	17	11	7	5
	37	23	18	13	9	4
	25	11	10	5	1	0

Source: CB Insights

Interest Over Time



Source: Google Trends

Unicorns as a term has been a buzz word in India and contrasting it with the global private equity term SPAC, clearly draws the comparative distinction for appetite to track developments within the private equity space.

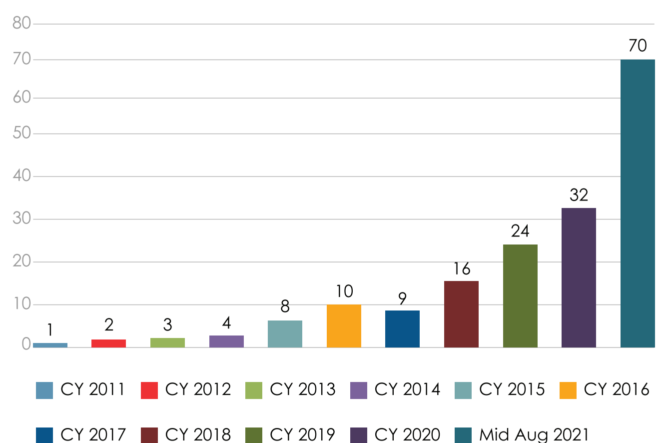
These rapidly growing new businesses are certainly not small on the valuation front. India's listed equity markets, which have tripled in market cap over the last 10 years, have raised less than half the amount of the private equity market.

Several Regional Ecosystems Develop Along with a Strong Pipeline

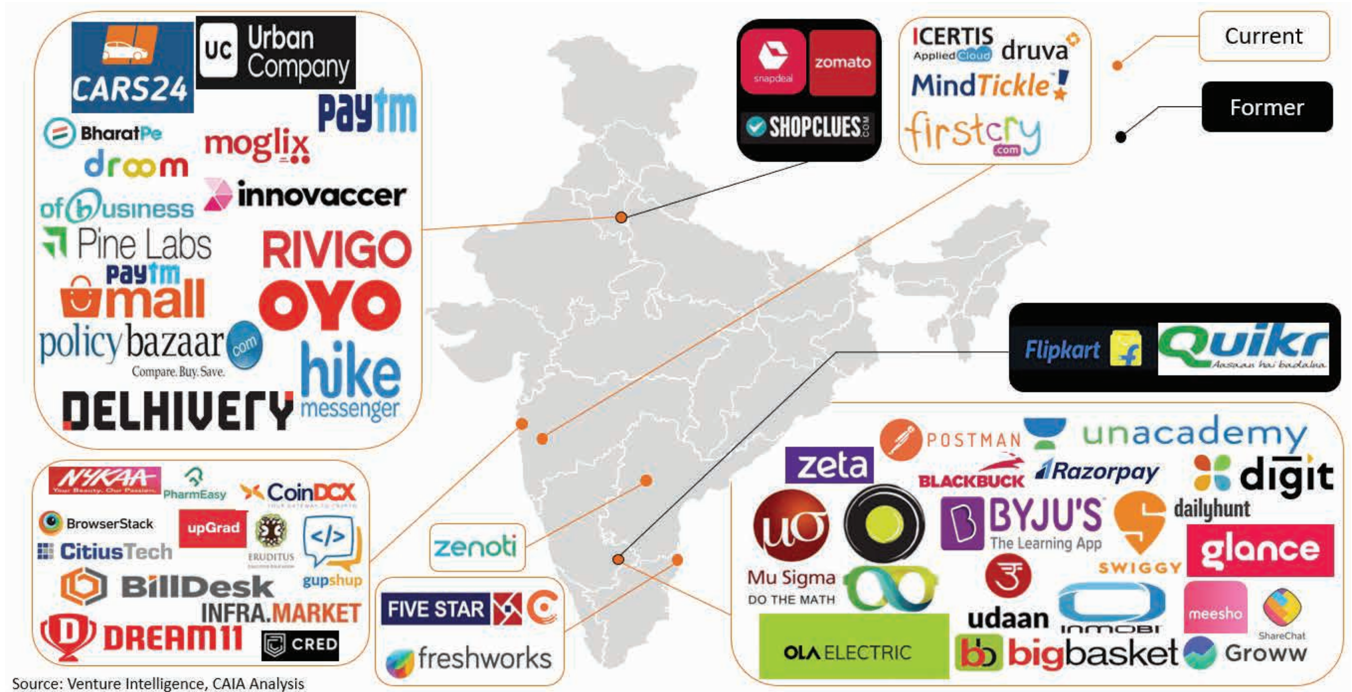
'Unicorn hub' is a term used to denote cities where more than five unicorns exist. There are three in India: Bangalore, Mumbai and NCR. Close to 85% of the unicorns are based in these locations. Other up-and-coming regional eco-systems include Chennai, Pune and Hyderabad.

We believe that at the going rate India could have more than 100 unicorns by 2025 year-end given the pipeline of startups closing on $500 million+ valuation, the current business environment, private markets activity and the shorter time it takes to reach unicorn status. By CAIA Association's analysis and Venture Intelligence data, until 2019 a unicorn-like valuation was attained in India around eight years after founding. In 2021 the median dropped to seven years and now stands at six years, which gives an indication of the pace of change.

Number of Unicorns



Source: Venture Intelligence, CAIA Analysis



Source: Venture Intelligence, CAIA Analysis

Note: Depiction is not exhaustive

Shreekant Daga
Associate Director, CAIA Association

Fund Raising Activity

Takeaway: Given the high level of interest in India from LPs, the number of active PEs is expected to remain strong in the near future.

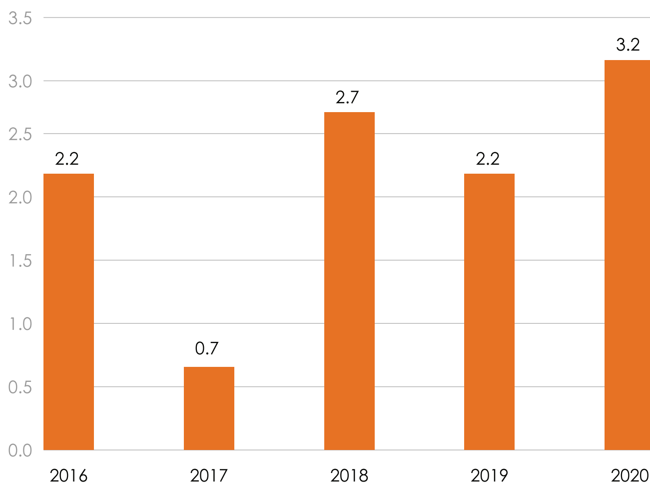
Fund Raising Activity

Venture Capital

In 2020 VC fundraising in India was at a record $3.2 billion, despite the Covid-19 pandemic. The high level of fundraising was driven by three large funds, accounting for 60% of the total for the year. Two were closed by Sequoia Capital India: India Venture Fund VII ($525 million) and India Growth Fund III ($825 million). The other fund was Elevation Capital's Fund VII ($400 million).

VC fund raising in 2020 was a new record despite Covid-19, driven by smaller number of funds raising larger amounts of capital.

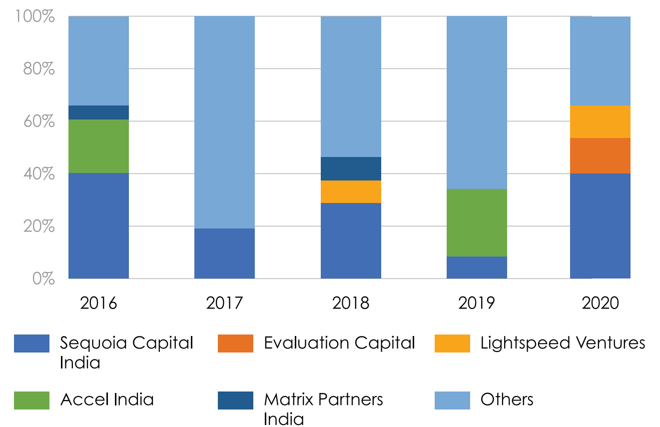
Total Funds Raised by VC for Investments in India (US$bn)



Source: Venture Intelligence, CAIA Analysis

On average, the top five fundraising VC funds each year take two-thirds of the total capital raised. Notably these five VC firms accounted for over 50% of total capital raised in the last 5 years. As shown in in the next column, Sequoia Capital India leads the pack, with significant fund raising in each of the last 5 years. They are followed by Accel India, Lightspeed Ventures, Matrix Partners and Elevation Capital. This group of five has a long track record in India having operated for between 10 and 15 years in the market.

VC Fund Raising by Group of 5 in Last Years

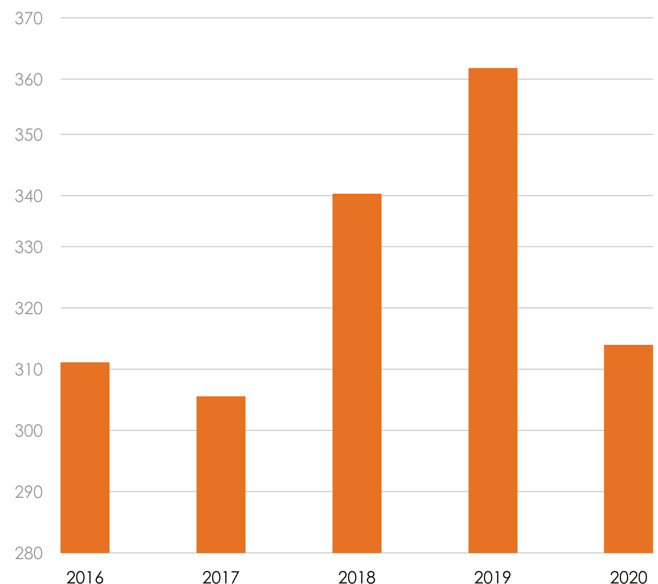


Source: Venture Intelligence, CAIA Analysis

The top group of 5 VCs accounted for over 50% of cumulative capital raised in last 5 years.

Despite the established VC firms taking a majority of the fundraising, the number of active VCs in India has remained stable, at between 300 to 360. In fact, the number of active VCs was growing before 2020, suggesting that the VC ecosystem was in good health.

Number of Active VC's in India



Source: Venture Intelligence, CAIA Analysis
Note: A VC is considered active if at least 1 deal was made in the year.

The number of active VCs in India in the last 5 years has been steady between 300 to 360. The new VC players who entered the India market in 2020 were also active.

The top 10 active new VCs are shown below. They were able to do multiple deals in 2020 despite the challenges from Covid-19.

New VCs Who Have Been Active in 2020

Top Active New VC	Deals in 2020
Beyond Next Ventures	4
Circulate Capital	4
NAB Ventures	4
Pureland Group	3
UpSparks	3
Village Global	3
Eden Ventures	2
iSeed	2
Makers Fund	2
Modulor Capital	2

Source: Venture Intelligence, CAIA Analysis
Note: A VC is considered active if at least 1 deal was made in the year.

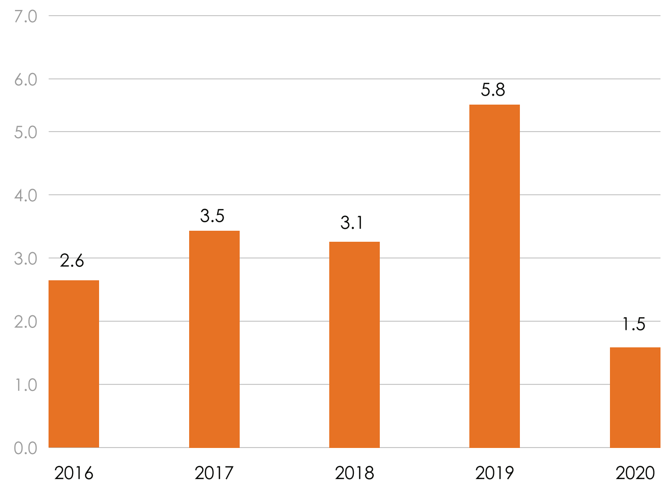
Private Equity

In 2020 PE fundraising in India recorded a lower level of $1.5 billion due to the disruption caused by Covid-19. This trend is in line with the global PE fund raising trend. The number of funds with successful fundraising in India was only 12, which was fewer than half the total of the last four years average.

Like VC fundraising, there was a flight to quality in 2020 as LPs were more interested in the large well-established funds. Notably, the two largest funds raised in 2020 accounted for 85% of 2020 total and they are specialized funds. Edelweiss Alternative Asset Advisors raised $900 million for Edelweiss Special Opportunities Fund III (ESOF III), focused on providing structured credit to Indian companies and Quadria India raised $401 million for Quadria Capital Fund II, a healthcare-focused fund. They are looking to deploy the majority of the capital in India, as they see greater spending in healthcare post-pandemic.

Fund raising in 2020 dropped and only 12 funds raised capital, which is about 48% of last four year average. The concentration of fund raising by the top PE firms is not as high as that of VC firms. The top 5 PE firms

Total Funds Raised by PE for Investments in India (US$bn)

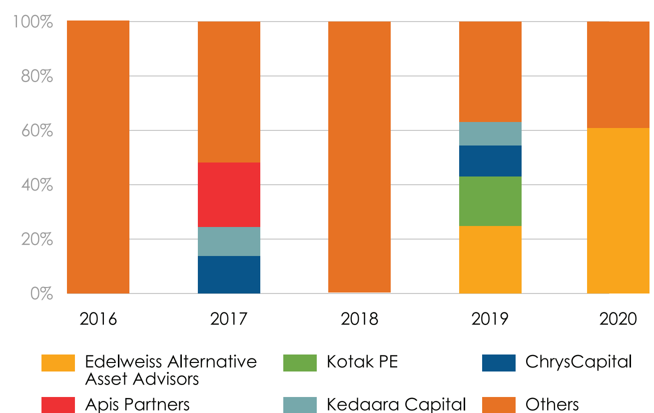


	2016	2017	2018	2019	2020
Number of funds with capital raising	20	32	28	21	12
AVG capital raised	128	108	110	275	127

Source: Venture Intelligence, CAIA Analysis

by fund raising accounted for 37% of total capital raise in the last five years, compared to 50% for the top 5 VC firms. As shown in the figure below, the top 5 PE firms by fundraising are Edelweiss, ChrysCapital, Kotak PE, Apis Partners and Kedaara Capital. Edelweiss stood out for the large amount of funds raised in 2019 and 2020.

PE Fund Raising by Top 5 in the Last 5 Years

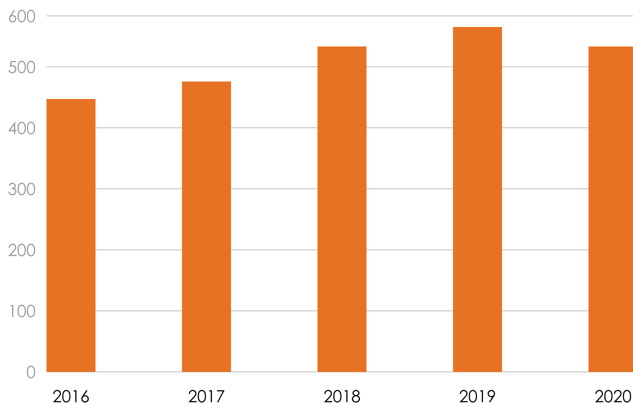


Source: Venture Intelligence, CAIA Analysis

The top 5 fund raising PE funds accounted for over 37% of cumulative capital raised in the last five years.

The number of active PE firms has been stable in the last five years. According to an EMPEA 2019 LP survey, India is ranked third out of 10 emerging markets, after Southeast Asia and China. Given the high level of interest in India from LPs, the number of active PEs is expected to remain strong in the near future.

Number of Active PE Investors in India



Source: Venture Intelligence, CAIA Analysis
Note: PE is considered active if at least 1 deal was made in the year.

AUTHOR'S BIOGRAPHY

Jack Wu
Senior Director, CapitaLand

Jack Wu is a Senior Director at CapitaLand Investment Management, and he is responsible for acquisitions and divestments for private equity real estate funds. Jack has over 15 years of institutional investment experience in Asia Pacific private equity real estate. Prior to joining CapitaLand Investment Management, Jack served as Director of Content, Asia Pacific at CAIA Association. He also served as investment professional at fund manager - Credit Suisse and SC Capital Partners - focusing on Real Estate asset class where he completed over $800 million of direct investments across Asia Pacific markets, and across real estate types.

Jack earned a 1st class hons in Bachelor of Engineering (Computer Engineering) from Nanyang Technological University. He also a Charted Financial Analyst (CFA) charter holder and a CAIA charterholder.

Observation on AIF Benchmarking – Category I and II

Takeaway: This section specifically evaluates the current Alternative Investment Funds benchmarking practice in India. Investors will benefit from benchmarking data on average fee levels and hurdle rates.

Observation on AIF Benchmarking – Category I and II

Large markets have some cardinal rules which lead to their growth: uniformity, transparency and protection. Uniformity allows for scalability. Transparency makes for investor confidence as the necessary disclosures help investors operate with efficiency. Protection permits resolution where one of the counter parties have erred. Without adequate protection, markets can be in free fall as assets experience a domino effect.

In recent years, SEBI has provided the alternative investment industry with plenty to focus on. The Template for Private Placement Memorandum (PPM) paved the way for greater standardization within a constantly ballooning industry. Benchmarking of fund performance has brought greater transparency. The involvement of investment banks during fund registration has been a welcome step towards bringing alignment and building functional capabilities within the industry. Investor protection measures are critically important for the Indian Alts market, as proactive measures are needed in all spheres of finance to help protect against malpractice.

CRISIL is the provider of benchmarks to the alternative investment industry. SEBI regulations divide the industry into three categories - in common market parlance, Category I is VC, Category II is PE, while Category III are hedge funds.

In principle, benchmarking covers all funds registered with SEBI and data submission by AIFs is compulsory. The benchmarks serve investors with metrics to compare/evaluate performance of category averages. The semi-annual report provides investors and market participants with parameters, such as internal rate of return, multiples ratio (further divided into realised and unrealised) and quartile analysis for Category I and Category II across vintages.

Data submission by AIFs translates into reporting a minimum number of data points, along with data consistency and accuracy. The returns depicted are on a post-expense basis and are denoted in Indian Rupees and US Dollars. Reporting for Category I and Category II is identical.

Vintage Year	No. of Schemes	Pooled IRR (%)	DPI*	RVPI*	TVPI*
FY14	6	9.17	0.11	1.25	1.36
FY15	10	6.97	0.22	1.10	1.32
FY16	21	20.41	0.14	1.46	1.60
FY17	13	24.80	0.05	1.54	1.58
FY18	12	11.45	0.09	1.07	1.16
FY19	14	16.06	0.01	1.19	1.20
FY20	8	-9.30	0.00	0.92	0.92
Total Schemes	84				

Values as on September 30, 2020

Source: CRISIL, Sept 2020 AIF Benchmark Report

For an AIF investor, there are several questions that could arise from the benchmarking report:

- Average management fee
- Average hurdle rate (standardized)
- Average carry or performance fees (comparable)
- Approximate taxation

The returns depicted in the benchmarking report are net of expenses, but for an investor it would be beneficial to gross up returns. Grossing up returns

indicates absolute manager performance relative to the management fees. In case of subsequent changes in management fees in newer funds it would be noteworthy for an investor to know absolute performance in the previous funds relative to the management fees.

Assumed Inputs	Percentage
Absolute Annual Return	12.0%
Annual Fees and Levies (all tyoes)	2.5%
Return Net of Annual Fees	9.5%

		Performance Fee		
		15%	20%	25%
Hurdle Rate	5%	8.83%	8.60%	8.38%
	6%	8.98%	8.80%	8.63%
	7%	9.13%	9.00%	8.88%
	8%	9.28%	9.20%	9.00%
	9%	9.43%	9.40%	9.38%

Source: CAIA Analysis

To illustrate the importance of the other bullets, we ran a sensitivity table with varying level of inputs for the hurdle rate and performance fee. A return with varying levels of hurdle rate and performance fees can move that fund performance across quartiles. Average terms of a fund bring clarity to the fund performance for an investor. A top quartile fund performance with steep terms can turn to be less attractive than the median with lower levels of fees.

The above points are return movers and bring contrast to a fund's terms vis-à-vis the industry terms. An investor can make a better call provided there is clarity on dollars received for every dollar invested across AIF categories.

Pooled IRR (%)

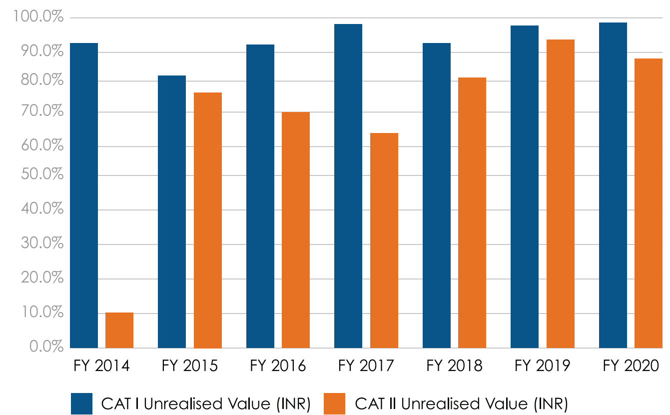
Vintage Year	No. of Schemes	Top Quartile (%) (Threshold for top 25%)	Median	Bottom Quartile (Threshold for top 25%)
FY14	13	12.03	10.63	6.59
FY15	11	11.17	8.28	6.07
FY16	18	12.70	10.53	5.39
FY17	36	14.24	11.19	5.03
FY18	47	15.24	11.00	4.15
FY19	52	15.76	5.65	-0.69
FY20	27	12.70	6.81	-6.33
Total Schemes	204			

Values as on September 30, 2020

Source: CRISIL

With most AIF returns showing unrealized gains, the valuation practice for AIF is at a critical juncture

Unrealised Value Based on Vintage Year



Source: CRISIL (Sept 2020 AIF benchmark report), CAIA Analysis

A careful observation of the return multiples ratio (realised and unrealised) points out that a large chunk of the return is unrealised. A vigilant eye on the movement in valuation is necessary to avoid or flag malpractices. An unrealized value bucket should eventually move into a realized value bucket, without slippage and with consistent industry growth.

Comparison of valuation and price will pinpoint the state of valuations within the industry, allowing SEBI to make a judicious call in shaping the valuation functions of the alternative industry. It is important to note that the valuation industry is driven by the principal agency concept.

Shreekant Daga
Associate Director, CAIA Association

The Future: Where is the Indian Market Going?

Takeaway: India's economic progress in recent years has allowed the country's vibrant entrepreneurial spirit to be sustained by domestic and foreign investors. The industry's continued growth brings a requirement for a deeper pool of investment talent.

The Future: Where is the Indian Market Going?

Venture capital and private equity are rapidly growing sources of capital in India. This growth has been spurred by many factors: India's market size, a combination of new and established entrepreneurs and greater creativity in managing businesses; all of which has fed the enthusiasm of foreign general and limited partners.

Market Size

A fundamental factor driving the rapid growth in PEVC is simply the gargantuan size of the Indian market - over one billion people. A key investment rationale of GPs like Sequoia is market size. The reason is simple - they have billions of dollars to invest and portfolio companies must grow to become large enough to absorb such capital and provide a risk-adjusted return. One of Sequoia's ed-tech portfolio companies in India, Byju's, has nearly 80 million registered users. The startup, in business for nearly a decade, commands a valuation of nearly $20 billion.

The other key factor driving market size is the high potential demand for various products and services that remain unsatisfied. For example, there is a shortage of healthcare, infrastructure, financial services and many other products which provide viable investment opportunities for PEVC.

Scaling Potential

India is promoting a knowledge-based and digital economy. A driving force of the growth in tech startups is that technology is now readily available to achieve the scale needed to meet this huge demand. The growth of mobile phones and their affordability, supported by the internet, are creating new sources of demand not only from urban areas but from rural areas and the vast hinterland of India's geography.

In the field of E-commerce, delivery agents are now widespread, providing the convenience of home deliveries. A good example is the 10-year-old Indian startup, Zomato, which, aided by its mobile phone app and delivery agents, has made more than a billion food deliveries to customers across the Indian landscape. Following its July 2021 IPO, Zomato is now valued like a "decacorn" at nearly $12 billion. Zomato employs more than 250,000 delivery riders, giving them much needed income. The seed round domestic venture capital investors - InfoEdge- multiple of invested capital (MOIC) exceeded 1050x. InfoEdge financed the first four rounds solo. Other investor rounds later included Jack Ma's Ant Financial, Tiger Global and other major names.

Success begets success and such returns are now attracting even more entrepreneurs and venture capitalists into India.

Government-driven Reform Policies for PEVC

According to a paper published by the Asian Development Bank (ADB) Institute in Tokyo in 2020, India has an estimated 26,000 startups, making it the third-largest startup ecosystem in the world, recording consolidated inflows of over $36 billion in the past 3 years. Credit for much of the excitement must go to the Government of India and its institutions like InvestIndia, based in New Delhi.

Government policies which have caused a large influx of venture capital and private equity include: (a) subsidies for the establishment of startup accelerators across the country; (b) establishing fund-of-funds such as that of SIDBI; and (c) listing reforms introduced by the SEBI.

SEBI has made it easier for entrepreneurs to exit their ventures, approving a reduction of the lock-in period on the 20% minimum entrepreneur shareholding, from three years to 18 months and on other pre-IPO shares

to six months, except in situations of project financing. The government has also committed that it will not resort to retrospective taxation. These policy reforms have substantially improved the investment environment for both domestic and international PE investors.

Government efforts have been complemented by venture capital funds like Sequoia setting up an incubator named Surge in New Delhi. Accel Partners has also set up their accelerator in Bengaluru.

"Government policy reforms have substantially improved the investment environment for both domestic and international PE investors."

New-age entrepreneurs have flourished in India's digital economy, given their access to low-cost digital tools. These aggressive and creative entrepreneurs come from a variety of backgrounds, including engineering. Most are starting off alongside co-founders with complementary skills. They are typically in their late twenties to early thirties. They have embarked on innovative and disruptive business models, backed by seed capital and venture capital.

These firms are often loss-making in pure balance sheet terms, but have grown rapidly in terms of the number of customers and improving economies of scale. Some of these new-age entrepreneurs are becoming serial entrepreneurs, moving from one successful venture to the next.

Diversity of Deal Archetypes

The wide variety of deals taking place bode well for the future of PEVC. Seven types of deals are noteworthy in the Indian PEVC marketplace.

1. Growth investments aiming to capitalise on the rising consumer in India;

2. Buyouts are attracting more capital from the likes of Blackstone, TPG and KKR. Both young and mature entrepreneurs are willing to exit;

3. Distressed investing has also emerged as an asset class with private equity funds and strategic investors taking part. Goldman Sachs, Apollo Capital, Cerberus Capital, Bain Capital and Varde Partners have all made distressed investments in India;

4. At least two SPAC deals have been closed including the $8 billion RenewPower, a Goldman Sachs portfolio company producing and selling renewable energy, and Caisse de Depot et Placement du Quebec (CDPQ) did a buyout deal when it acquired the majority of the shares of Azure Power, another late-stage startup, retail energy company;

5. Real estate vehicles like REITs and direct real estate investments. Examples are the Blackstone-backed REIT and a direct investment by a US pension fund CalPERS, a greenfield real estate development in Gurgaon.

6. PIPE (Private Investment in Public Equity) deals are also attracting leading fund managers which help portfolio companies raise capital speedily; and

7. Venture Debt funds are in operation but the industry is at a nascent stage in India, though growing. The major player in this space is Singapore's Temasek, having acquired the India operations of Silicon Valley Bank.

In the distressed space, further reforms are needed in the Insolvency and Bankruptcy Code, so that the whole investment process can be completed with finality in a set period of time. The Government has taken a favourable attitude towards distressed investing, primarily because jobs are protected if a distressed company can continue as a going concern, providing much-needed employment.

Limited Partners and Angels

The bulk of the capital flowing into PE funds (around 85%) is sourced from LPs in the US, Canada, Europe and sovereign wealth funds like the Abu Dhabi Investment Authority, Qatar Investment Authority, Temasek and the Government of Singapore Investment Corporation. The challenge facing India is to develop its domestic LP community. The potential of domestic LPs is as yet untapped in any meaningful way.

Some steps have been taken in this regard. For example, domestic insurance companies have begun investing in SEBI-registered AIFs. Potential investors that need to grow their skill sets include the EPFO and the National Pension Scheme. In the long run, more capital flows should come from these domestic institutions.

Angel investors and associations have sprung up in many cities. This bodes well for the flow of angel capital into AIFs. An example is the IAN Venture Capital Fund established by the Indian Angel Network.

Risk Factors

Besides the usual venture-specific factors, a number of critical risk factors are present in the Indian marketplace, with which fund managers are learning to cope. Two key risks in particular merit consideration: governance and ESG factors. Private equity funds are addressing these concerns in their portfolio companies at the due diligence stage, by identifying gaps and preparing a corrective action plan which is closely monitored. Where the concerns cannot be addressed, investors will walk away from the deals. On the governance front, director independence is being given more weight.

Conclusion

Considering the prospects mentioned above, the progress already achieved and case studies of successful private equity and venture capital funds, the outlook for such investments is positive. The strengths of the Indian economy and the quality of its young founders is durable. The market has become mature to a large extent, though there is scope for further development. Annual capital flows in private equity and venture capital in India should rise from the current 2021 run rate of $48 billion to much higher levels in the years to come.

AUTHOR'S BIOGRAPHY

Arvind Mathur
Chairman, Private Equity Pro Partners

Arvind has 40 years' experience in investment banking, private equity and venture capital.

He managed a portfolio of 30 private equity and other funds as a limited partner, a direct investor and an investor in general partnerships. Arvind has engaged globally with the world's largest limited partners including sovereign wealth funds, pension funds and insurance companies. He has invested in, or raised capital from, many countries.

He held leadership positions at the Asian Development Bank, Citi, The Indian Private Equity & Venture Capital Association (IVCA) and the Impact Investors Council. Arvind teaches masterclasses in private equity, venture capital and M&A. He delivered a lecture on Asian Buyouts at the Harvard University.

His training in investments, M&A and credit analysis was at the Harvard Business School, Citi, Goldman Sachs and the US SEC. He is the Chairman of Private Equity Pro Partners and an adviser to a cross-border hedge fund. He is a CFA Charterholder and FRM, GARP. He lends a hand to the Laksh Foundation.

CAIA Association's Call to Action

Takeaway: India's private capital industry has all the ingredients to explode onto the global stage and provide for significant wealth creation for large portions of the population.

CAIA Association's Call to Action

We first introduced our Call to Action for CAIA Members and those in the broader global investment community in our 2020 'Next Decade' report. Here we put them in context for the investor in India.

Commit to Education

Close to two-thirds of India's population is of working age, yet less than half of these new young men and women are employable. Asset management organizations, business schools and regulators need to work together to engender a generation of properly trained, ethically sound investment professionals to steward the ongoing growth of alternatives.

Embrace Transparency

Over the years, the Securities and Exchange Board of India (SEBI) has made significant progress in designing a framework for reporting and representation that can be built upon. Moving forward, we encourage practitioners and SEBI to prioritize action on cost disclosure, sponsor contribution requirements, unnecessary financial engineering and irresponsible debt covenants. Fee levels, hurdle and carry calculation methodologies and uniform performance reporting all need to be addressed.

Broadly Diversify

Indian financial market volatility showcases the unforgiving nature of wild price swings on retirement savings and income requirements. A fiduciary's role at its very core is to construct a basket of beta exposures that provide for income, inflation protection, capital preservation, and principal growth. Investors should complement allocations to fixed income, gold, and public equities with appropriate levels of private capital to improve risk-adjusted returns over the long term.

Protect Investors

India's private capital industry has all the ingredients to explode onto the global stage and provide for significant wealth creation for large portions of the population. However, this transition must be done with clients' interests paramount and with a keen eye towards demanding professionalism.

CAIA Association's Call to Action

The collection of narratives above, providing a variety of perspectives, intersect into one common conclusion; that India's private capital sector has arrived. For well over two decades, the world has been watching India muddle in the shadow of its more prominent northern neighbor. Seemingly trapped on the 'almost there' treadmill.

Previous false starts have been brought about by a banking crisis, political divisiveness and privatization paralysis; and then there was Covid-19. But in spite of the perfect storm created by the global pandemic, private markets have continued to gain steam and impact both national and global capital formation.

"Private investment facilitates a more natural channeling of long-term capital into impact and ESG projects such as infrastructure, real estate, clean energy, agriculture and water."

On the heels of a record 2021, India is poised to consolidate its place amongst the largest economies in the world, and in doing so to generate even greater heights for its startup ecosystem. In the sheer number of new unicorns, India's PE market has built up strong momentum.

Several of India's unicorns are rumored to be flirting with a public listing, some of which could match the global record set by Alibaba in 2014. Couple these trends with China's debt excesses and the developed world's complete absence of yield, and this relative story is shaping up to be very appealing for investors of all types.

The West's development of private markets has been a lesson in the power of capitalist creativity. The tectonic shift of capital formation off-exchange in the last two decades has been an unparalleled engine for job creation and middle-class wealth. The ability for private markets to more quickly and effectively revitalize stagnant businesses - or simply redeploy that capital to entrepreneurs' innovative ideas - is a disruptive force that is a critical principle of any competitive and growing economy.

Further, private investment facilitates a more natural channeling of long-term pools of capital into impact and environmental, social and governance projects such as infrastructure, real estate, clean energy, agriculture and water. India has seemed to grasp that crucial point. The world of investment is changing as we work to tackle the challenges of over-population, climate change, biodiversity and the world of work.

But what do we do with all this potential? What guiding principles must India's capital market apparatus employ to ensure this age of energetic adolescence results in a mature profession where investor outcomes are front and center? We believe a four-part clarion call is in order:

Commit to Education

Close to two-thirds of India's population is of working age. Another 12 million individuals are expected to join the workforce annually. Yet less than half of these new young men and women are ready to take-up jobs or are employable; such is the plight of a dysfunctional system converting a demographic dividend to a demographic burden.

Education overall has failed to keep pace with the modern world's demands for skilled and literate individuals. Hence people are hungry to pursue additional qualifications to supplement their understanding with knowledge of modern, global practices.

Alternative Investments, in need of a disproportionate

amount of skilled labor, finds a dearth of ready talent through traditional academic paths. Recruiters are forced to draw from a pool of less qualified and experienced candidates for these high demand disciplines. Asset management organizations, business schools and regulators need to work together to engender a generation of properly trained, ethically sound investment professionals, to steward this rapidly growing slice of capital allocation and product development. This should not be a function of social status or school pedigree, but rather an extra-curricular objective assessment based on merit and relevant expertise.

CAIA Association, as the global professional body for alternative investments, aspires to play a leadership role in fostering dialogue, partnership and solutions amongst these stakeholders. It will also continue to offer its world class CAIA credential with a fresh pledge to ensure the designation remains on the leading edge of global alternative investment practice.

Embrace Transparency

As alluded to above, because private capital is removed from the gyrations of moment-to-moment market making, enterprising investors can take advantage of market dislocations, information asymmetry and out-of-favor or counter-cyclical opportunities. But inefficiency is no excuse for lack of transparency and fairness that puts clients' interest first.

SEBI has made significant progress in designing a framework for reporting and representation over the years that can be built upon. From bringing alignment in mutual fund product offerings to more recently templatizing alternative investment placement memorandums. We are pleased with the precedent and the momentum the regulator has generated in building a sustainable capital markets system. These amendments will help to distinguish credibility and align interests among all the stakeholders for the benefit of the greater good.

We would encourage practitioners and SEBI to prioritize attention to improved cost disclosure, steeper sponsor contribution requirements, unnecessary financial engineering and irresponsible debt covenants. Unreasonable fee levels, hurdle and carry calculation methodologies and uniform performance reporting also need to be brought under closer control. CAIA Association stands committed to help support and encourage this journey.

Broadly Diversify

Risk control by diversification has not been a concept that has taken root in India outside of the most sophisticated of institutional investors. Partly this is due to the relatively high risk-free rates, as well as Rupee returns on gold in recent years. However, the dismally poor participation from the general public in listed equity markets is also a function of chasing the most favored asset class, subjecting oneself to concentration risk based on market-timing.

Indian market volatility measured by the VIX showcases the unforgiving nature of wild price swings on ordinary investors. It is particularly cruel to those nearing retirement who, caught out by a market correction at an advanced age, face a less than comfortable retirement.

A fiduciary's role at its very core is to construct a basket of beta exposures that provide for income, inflation protection, capital preservation and principal growth. The recipe for any one client or institution is incumbent on time horizon, liquidity needs, return expectations and appetite for loss. The client is the only true benchmark. As such, complementing allocations to fixed income, gold and public equities, with appropriate levels of private capital, can provide for uncorrelated cash flows and drivers that significantly mitigate volatility and improve risk/return measures over the long term.

Protect Investors

The profession of asset management is a noble fiduciary duty with an obligation to provide the highest standard of care to the client. This relationship is built on trust. Conflicts must be identified and vigorously avoided. Product choices and fee methodology must ensure that the agent's success is tied up in the principal client flourishing; interests must be aligned. SEBI's decision to have a minimum of 20% of compensation paid in units of the mutual fund scheme they are involved in with a lock-in is a healthy step in this direction.

Further, while we argue throughout this piece that private capital can have advantageous effects on long term investor outcomes, we must tread wisely. These instruments and funds are opaque and complex and require certain levels of technical training to properly evaluate their fit, even within a diversified portfolio.

Dispersion between strong and poorly performing general partners is extremely wide, rendering manager selection much more important than in traditional asset classes. While we applaud the recent accredited investor regulation, we would urge SEBI to add requirements to demonstrate a minimum level of sophistication to either invest in private capital directly, or as a fiduciary on behalf of a client.

CAIA Association exists to improve investment and societal outcomes of capital allocation through professional education, transparency and thought leadership, across all investor alternatives in our industry. India's private capital industry has all the ingredients to explode onto the global stage and provide for significant wealth creation for large portions of the population. However, this transition must be done with clients' interests paramount and with a keen eye towards demanding professionalism. This will take unprecedented collaboration and vigilance from industry professionals, regulators and the academy. We are optimistic that this vibrant country is ready for the challenge and CAIA Association looks forward to contributing to this exciting next phase.

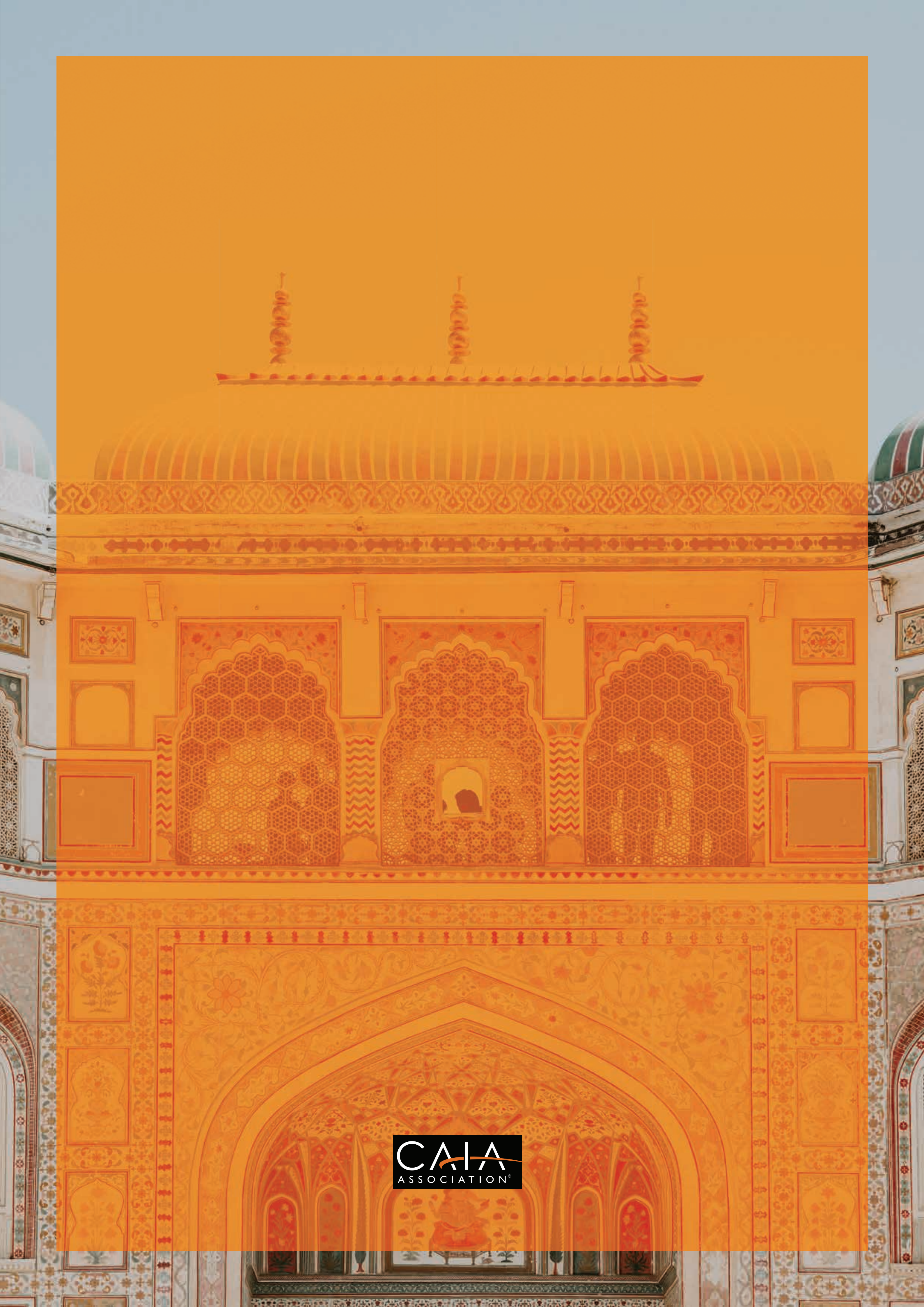
AUTHOR'S BIOGRAPHY

John Bowman
Executive Vice President, CAIA Association

John serves as Executive Vice President for the CAIA Association, overseeing the industry leading CAIA charter, thought leadership and content development, and CAIA's Asia Pacific strategy. John has devoted over 20 years to the asset management industry to recover the narrative of the value that the investment profession bring to society. He is a staunch public advocate for market integrity, long-termism, investor outcomes, diversity, human dignity and educational standards, as necessary ingredients to building a sustainable and healthy profession. John previously served as Managing Director for the Americas for CFA Institute, a region comprised of 40+ countries from Canada, the U.S., Central America, South America and the Caribbean. Bowman joined CFA Institute in 2004 after holding several industry positions.

About the CAIA Association

The CAIA Association is a global professional body dedicated to creating greater alignment, transparency, and knowledge for all investors, with a specific emphasis on alternative investments. A Member-driven organization representing more than 12,000 professionals in more than 100 countries, CAIA Association advocates for the highest ethical standards. The organization provides unbiased insight on a broad range of investment strategies and industry issues, key among them being efforts to bring greater diversification to portfolio construction decisions to achieve better long-term investor outcomes. To learn more about the CAIA Association and how to become part of the organization's mission, please visit www.caia.org.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