

## **Analysis of Private Equity Investment Trends in India – Period 1996-2014**

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**ABSTRACT:-** Private Equity investment in India has helped creating some world class companies in India including companies like Bharti Airtel, GMR, Flipcart, Snapdeal.com etc. Private Equity companies help companies to grow and evolve. They help management of startup enterprises to execute their initial marketing and product development strategies. They help their portfolio companies to restructure operations, commercializing new products, acquiring or disposing assets etc.

This paper analyses the private equity investment trend and boom-decline phases in India starting from the year 1996 till 2014.

**Keywords:-** Private Equity, Strategy, Growth Funding, Investment, Venture Capital

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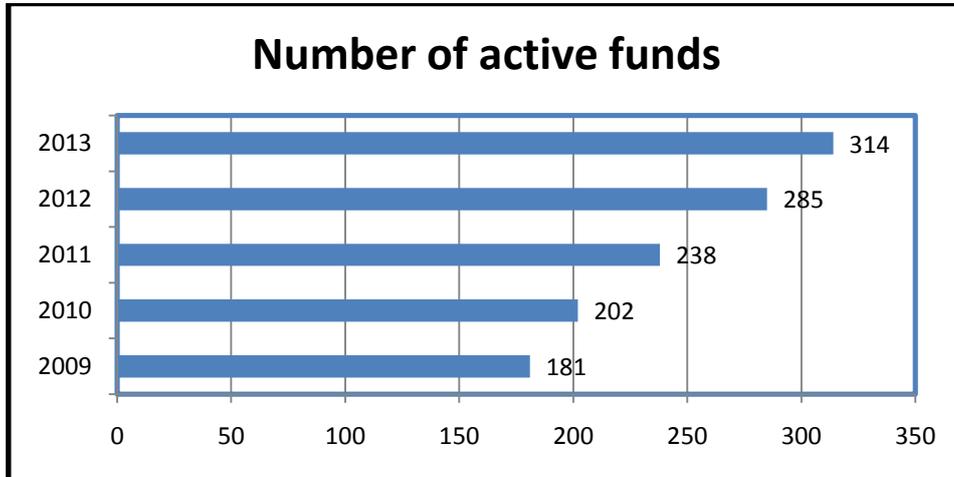
### **1. Understanding the concept of ‘Private Equity’**

‘Private Equity’ investment stands for investment in the primary equity of a company, the equity that is not freely tradable on a public stock market. Such an investment is outcome of negotiations between the company and the private equity company. This investment is primarily in the unlisted companies. A private equity company can provide support to the target companies at various stages of the company’s growth. ‘Private Equity Fund’ on the other hand, refers to the fund raised by a private equity company. In common parlance the reference to private equity company and the fund is used interchangeably. The fund managers or General Partners of the Private Equity firm find representation in the board of directors of the company they have invested in. A private equity fund also provides strategic managerial support and helps the company it has invested in, to build up competitive capabilities in the long run. The Private Equity fund obtains capital commitments from certain qualified investors such as pension funds, financial institutions etc. The source of fund of any Private Equity company can also be the funds raised from high net worth individuals and Governments of certain countries. Such Investors are passive investors designated as Limited Partners in the private equity fund. For example the Limited Partners for Indian investments have been organizations and entities like Harvard, Stanford and Columbia University, Prudential, CalPERS, Goldman Sachs, Cap Z, National Bank of Kuwait, Government of Singapore etc. Such investors are passive limited partners in the private equity fund, which otherwise is managed by professional fund managers designated as General Partners.

### **2. Current Status of Private Equity Funds in India:**

Private Equity investment in Indian market has passed through phases of boom and decline over last few years. Following are the numbers of active funds operating in India.

Figure 1: Number of active VC/PE funds in India (2009 – 2013)



Source: India Private Equity Report, 2014, Bain & Company, Indian Venture Capital Association (IVCA)

Following table and chart indicates the amount of Private Equity investment in India for the period 2004-2013:

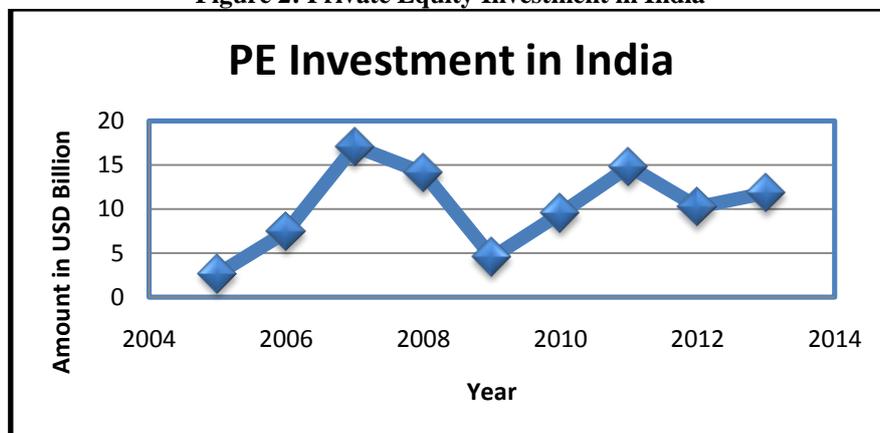
Table 1: Private Equity investment in India

Year	Amount in USD Billion	Average Deal size in USD Million
2004	1.6	21.9
2005	2.6	14.1
2006	7.4	25
2007	17.1	34.6
2008	14.1	31.5
2009	4.5	20.8
2010	9.5	24
2011	14.8	28
2012	10.2	18.4
2013	11.8	20

Source Bain Capital Reports – 2010,2011,2012,2013, 2014

Following is the chart indicating the investment data of private equity companies in India.

Figure 2: Private Equity Investment in India



Source: Bain Capital Reports

**3. Category wise Private Equity Investment in India:**

Private Equity companies can invest in and support a company in various forms. Their mode of investment in a company can be as follows:

- As Venture Capital Provider and Angel Investor
- As provider of funds for the growth and consolidation of a company
- Buyouts of distressed companies
- Buyout of majority or minority stake in well performing but undervalued companies
- Investment in publicly listed companies

Thus depending on the type of investment a private equity fund is targeting, the types of Private Equity investments can be classified as:

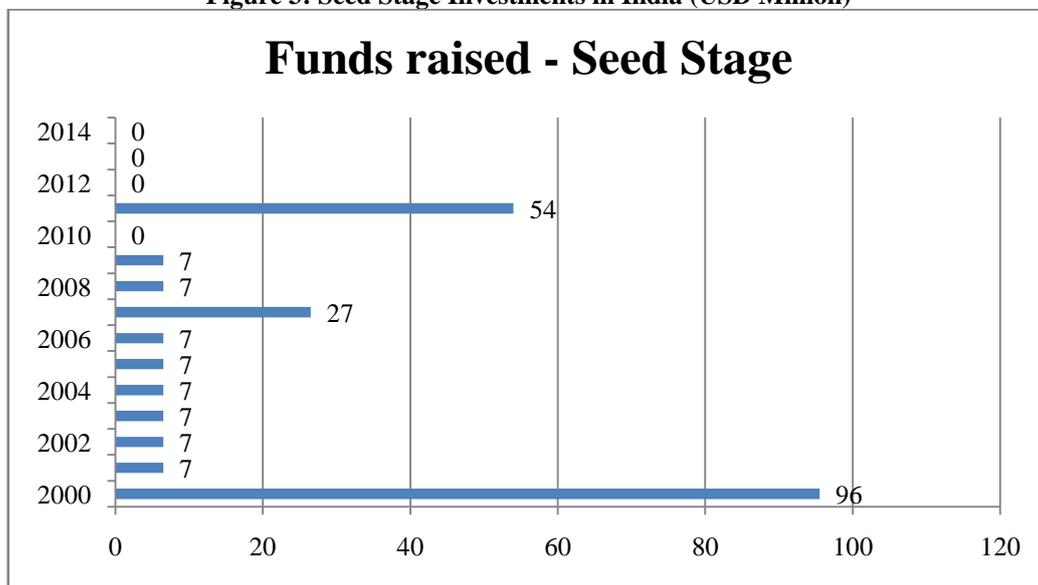
- Seed Investment/Angel Investing/Venture Capital investments – Early Stage investing
- Growth Capital funding / PIPE or Public Investment in Private Equity – Late Stage Investing
- Buyouts
- Buyout of Distressed companies
- Others – Mezzanine Investment and Sector Specific Investments

**(i) Seed Stage**

Investments into companies that are startup ventures with little or no revenues are termed as Seed Stage investments. Typically, these are companies that have identified that business idea and the target market. In many cases, first round of product development has also taken place and an initial traction in revenue has been seen. Since, most of the companies in the seed stage are in a very early stage of their development, these investments are typically perceived as high risk investments. These companies usually have a product prototype and are looking for markets to enter and grow. The funding received at the seed stage is used for activities like product development, R&D, marketing expenses, team strengthening etc.

Following are the details of Seed stage investments in India (Period 2000-2014)

**Figure 3: Seed Stage Investments in India (USD Million)**



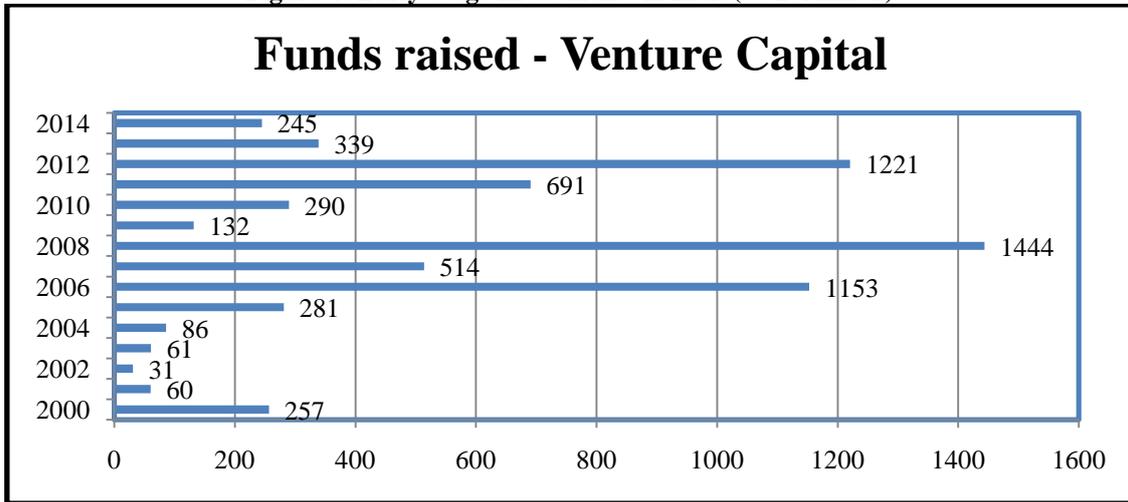
Source: India Private Equity Report, 2014, Bain & Company, Indian Venture Capital Association (IVCA)

**(ii) Venture Capital Investing**

Early Stage (or broadly known as “Venture Capital”) is investing in companies that have developed the product and are usually generating revenues. Generally speaking, early stage companies are in advanced stages of business growth and maturity when compared to seed stage companies. Consequently, the investment risk in such companies is lower than seed stage. The investments are done in venture capital investment format in

various rounds. First round investment is usually the smallest and then the capital invested in subsequent rounds is larger. Also, in many cases the follow on rounds are syndicated between various early stage funds. Following are the details of Early Stage investments in India (Period 2000-2014):

**Figure 4: Early Stage Investments in India(USD Million)**



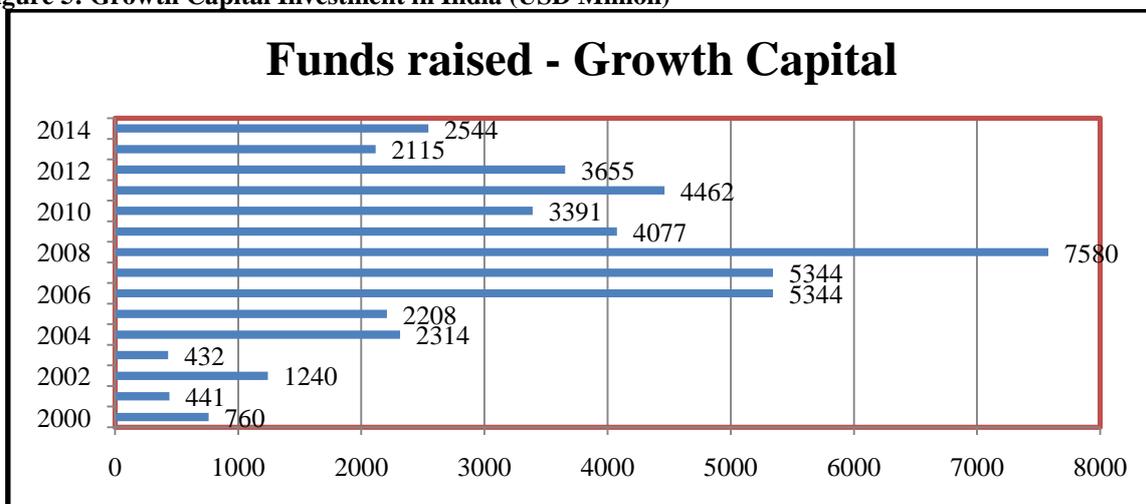
Source: India Private Equity Report, 2014, Bain & Company, Indian Venture Capital Association (IVCA)

**(iii) Growth Capital**

Companies that have reached a certain size and scale with a proven product, operating history and track record, often need capital for further expansion. This capital could be used for adding new products/services, entering new geographies, acquiring companies, strengthening team, growing existing products/services, brand building, R&D, marketing etc. Generally at this stage the funds that invest in these companies infuse capital for a minority stake in the company. The target companies that opt for growth capital are more mature companies than those that go for seed stage or early stage with a higher revenue, profitability and operating history. Such companies accept private equity support as internal cash accruals from the company are not sufficient to fund its further expansion. In other words, the company has limited free cash flow.

Following are the details of Growth Capital investments in India (Period 2000-2014)

**Figure 5: Growth Capital Investment in India (USD Million)**

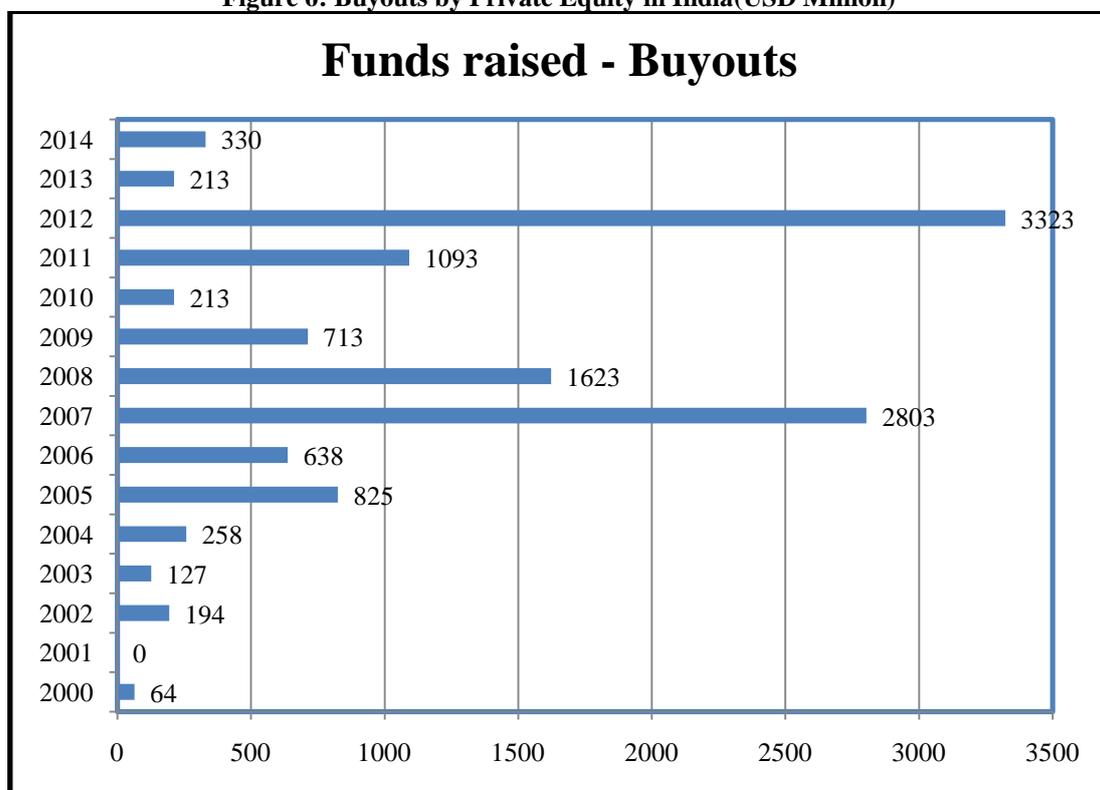


Source: India Private Equity Reports, Bain & Company, Indian Venture Capital Association (IVCA)

**(iv) Buyouts**

Transactions where Private Equity funds invest in companies to take control positions are termed as buyout transactions. Private Equity funds will take majority ownership of companies and then either retain or hire managers to run operations more efficiently. In many buyout transactions, the private equity funds take on additional debt in the company to fund the acquisition. Adding leverage to the company increases the return to equity holders. Such buyouts are termed as Leverage Buyouts (LBO). Often Private Equity funds after taking over companies undertake strategic decisions that result in improving overall operational efficiency of the company. Funds bring in new management, devise better incentive policies, restructure products/service, enter new markets etc. Such initiatives help in increase revenues and profitability of the acquired companies, resulting in increase in margin and hence overall valuation of the companies thus driving returns to the equity holders. Following are the details of Buyouts investments in India (Period 2000-2014)

**Figure 6: Buyouts by Private Equity in India(USD Million)**



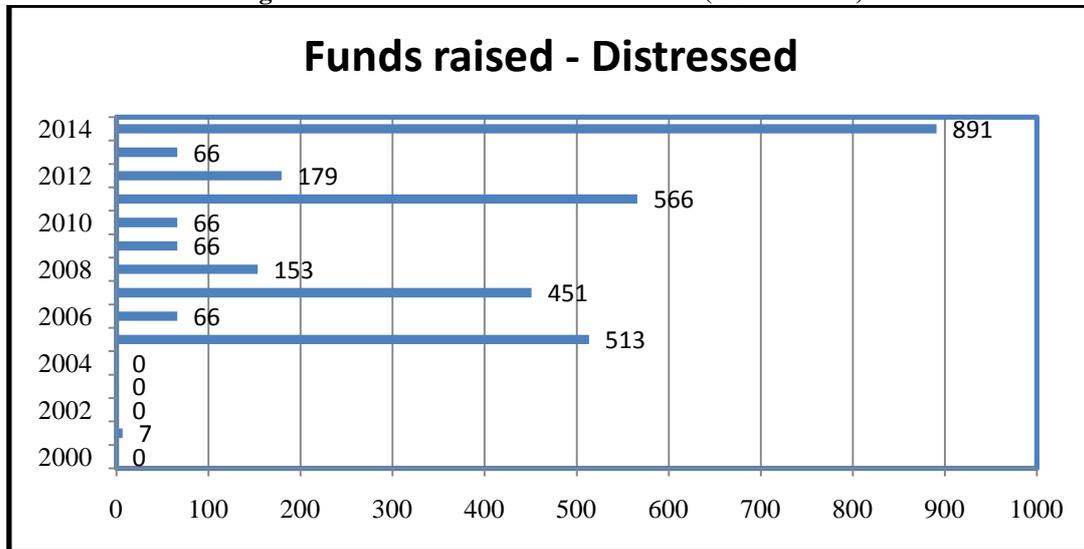
**Source: India Private Equity Report, 2014, Bain & Company, Indian Venture Capital Association (IVCA)**

**(v) Distressed:**

Investing in assets that are in a distressed state forms a large part of private equity investing activity in United States. However, India being a growth economy, availability of distressed investing opportunities has been limited. Still there are a number of funds that have been set up to invest in assets that are not doing well with a view to be able to execute turnaround in those companies. With RBI's latest push on finding solutions to the increasing NPAs on balance sheet of banks, the number of distressed investing opportunities is slated to rise in the coming years.

Following are the details of distressed investments in India (Period 2000-2014)

Figure 7: Distressed Investment in India (USD Million)

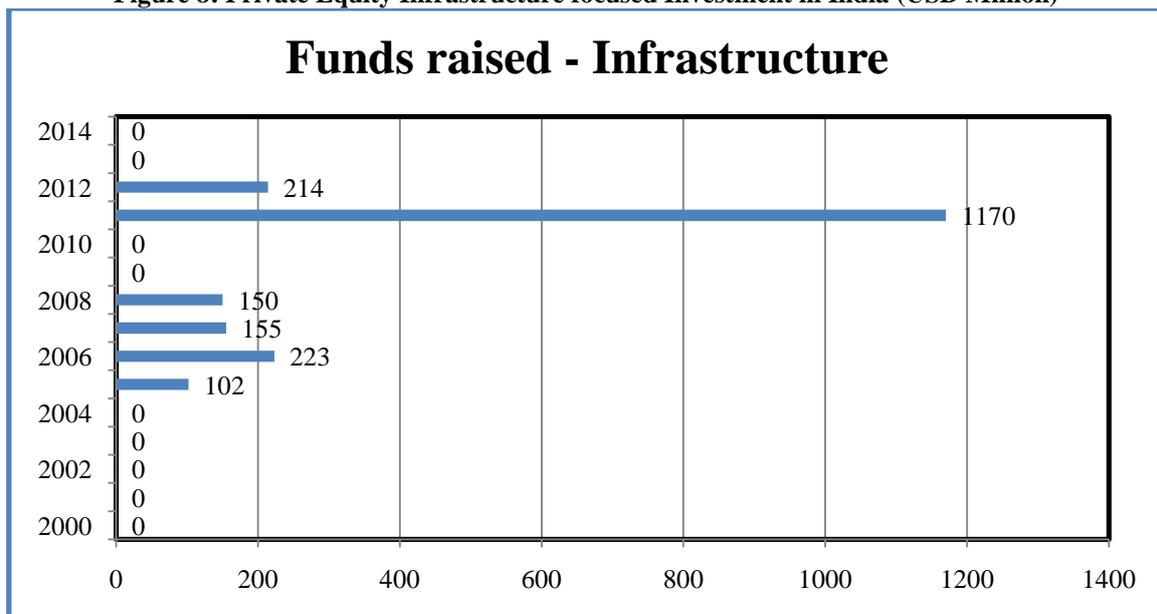


Source: India Private Equity Report, 2014, Bain & Company, Indian Venture Capital Association (IVCA)

(vi) **Infrastructure**

There are a few private equity funds that are dedicated to investing in Infrastructure. Infrastructure private equity funds are structured similar to other private equity funds. Return expectations from infrastructure private equity funds is typically a bit lower than other private equity funds. Even if the fund might not be completely dedicated to infrastructure, there are a few cases where majority of the investments that the fund has made are in the infrastructure space. Even in such cases, for the purpose of this study, the fund's stage is called out to be infrastructure. Funds dedicated to infrastructure are usually restricted to invest in public and private infrastructure including roads, ports, airports, hospitals, education institutes, power, telecom etc. Following are the details of Infrastructure investments – Private Equity in India (Period 2000-2014)

Figure 8: Private Equity Infrastructure focused Investment in India (USD Million)



Source: India Private Equity Report, 2014, Bain & Company, Indian Venture Capital Association (IVCA)

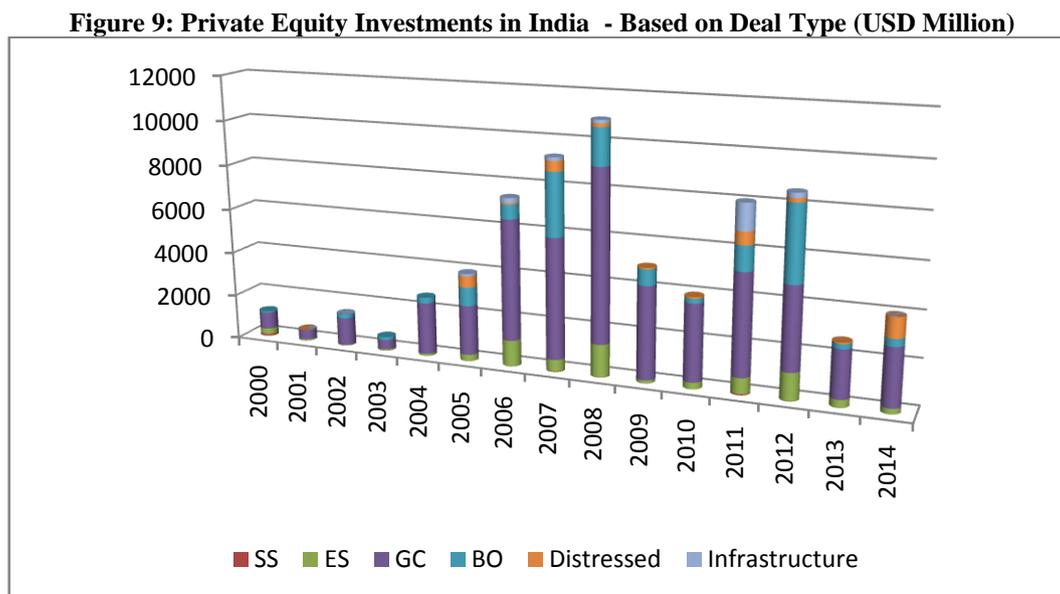
**4. Analysis of Private Equity Investment Trend – Investment Type Basis:**

It is evident from the chart below that growth of private equity funds focused on growth capital has been the largest amongst all the funds.

In 2008, when the funds raised were highest, out of a total of USD 10.9 billion capital raised, 70% of it was raised by funds focused on growth capital. Except in 2012, when funds raised by growth capital and buyout funds were close to each other at USD 3.6 billion and USD 3.3 billion respectively, in all other years, funds raised by growth capital funds is much higher than raised by other funds.

In years 2001, 2002 and 2004, contribution of growth capital to overall capital raised has been relatively much higher at 86%, 84% and 87%. The minimum contribution of growth capital to overall capital raised has been in the year 2012 at 43%. Except 2012, in all other years, growth capital has contributed a minimum of 55% to overall capital raised.

In 2007 and 2012, buyout funds also raised a significant capital contributing 30% and 39% respectively to the overall capital raised by private equity funds in those years. Apart from these 2 years, growth of buyout funds has not been consistent and has varied from 0-20% of capital each year out of overall capital raised. Infrastructure funds saw a peak of USD 1.2 billion in 2011 whereas distressed funds witnessed a peak of USD 891m in 2014.



Source: India Private Equity Reports, Bain & Company, Indian Venture Capital Association (IVCA)

**5. Trend Analysis of Private Equity Investments in India:**

From the US Market experience it is clear that Private Equity is a Cyclical Business. As per a study by Bain Capital - Since 1980's the Private Equity Market in US has gone through three major booms. In 1980's the Private Equity business thrived on poorly managed public companies and corporate divestitures available at lower cost. During 1990's private equity investment returns were driven mainly by GDP growth and PE multiples resultant of the same and in the last decade (2000) private equity companies thrived on credit bubble inflated by low interest rates. Leveraged buyouts reached all-time high in the decade of 2000 in United States.

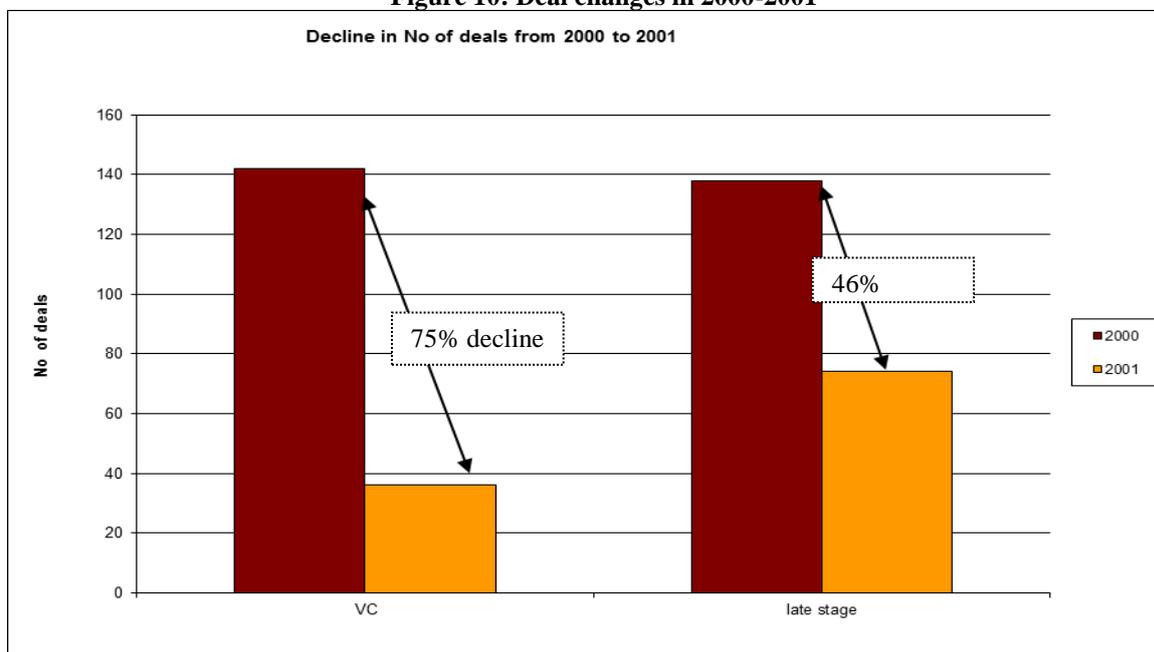
In Indian Market as well three distinct investment boom-decline phases can be identified.

- (i) Phase I – (1995-2004)
- (ii) Phase II – 2005-2008
- (iii) Phase III – 2009-2014

**(i) Phase - I -**

Private Equity companies got interested in the Indian Market during the mid-1990's when the unfolding of the process of liberalization and globalization generated a lot of global interest in the Indian economy. However, most of the private equity funds at that time were interested in the IT (Information Technology) sector. This was on account of the success demonstrated by India in assisting Y2K (Year 2000) related issues as well as the overall boom in the information technology, telecom and the Internet sectors. Many such funds lost money when the dot com boom fizzled out. Consequently, as observed by Evalueserve, a global research firm, the Private Equity funds started investing less in Indian market. The trends, which were observed in private equity firm's investment format post year 2000, are as follows: The number of venture capital deals declined substantially from 142 in 2000 to 36 in 2001. The number of late stage deals also declined from 138 in 2000 to 74 in 2001. Investments in Internet related companies declined from \$ 576 million in 2000 to \$ 49 million in 2001. As per study conducted by Grant Thornton, less than 10 funds survived post 2000 in India out of 70 existing at the peak of 1999.

**Figure 10: Deal changes in 2000-2001**



Source: Evalueserve, IVCA, Venture Intelligence India

**Table 3: Private Equity/ Venture Capital Investments in India during the period 1996-2004**

Year	1996	1997	1998	1999	2000	2001	2002	2003	2004
Number of Deals	5	18	60	107	280	110	78	56	71
Value of Deals (USD million)	20	80	250	500	1,160	937	591	470	1650
% Change over the previous year	-	300	212.5	100	132	(19.22)	(36.92)	(20.47)	251.06

Source: Evalueserve, IVCA and Venture Intelligence India

The private equity investments were very marginal in India till the beginning of the year 1997. However in the year 1997 such investments grew by 300% over the previous year figure on account of liberalization of Indian economy, growth of Indian Information Technology firms and positive global outlook for Indian economy. As stated above, maximum amount of such investments mainly focused on IT or ITES companies. Starting from the year 1998 till the end of year 2000 private equity-venture capital investments in India grew on an average at a rate of 150% year on year basis. However, starting from the 2001 till the end of year 2003, the private equity-venture capital investments fell on an average by 25%, year on year basis.

**(ii) Phase II – 2005-2008**

Following are the investment details of Private Equity funds in India for the period – 2005-2008

**Table 4: Average value of deals categorized on the basis of investment in different stages of growth**  
(Amount in USD million)

Stage of Development	Company	2008	2007	2006	2005
Early Stage (Venture Capital)	Capital/Seed	5.92	5.5	4.08	5.35
Growth Stage		31.56	41.28	11.1	13.8
Late Stage		37.27	36.69	33.69	15.95
PIPE		47	52.62	23.87	15.57
Buyout		42.55	64.7	81.07	61.2
Others		90.4	118.2	41.4	-

**Source: India Private Equity Reports, Bain & Company, Indian Venture Capital Association**

The trend exhibited above indicates private equity companies in India, during 2005-2008 Period were focusing more on Late Stage deals in comparison to Early stage deals and thus on account of the same the number as well as value of Late stage deals increased substantially during the period. The total number of late stage deals, which were 40 in the year 2005 increased to 150 by the year 2007 and were 149 in 2008. Again in terms of value the late stage deals grew significantly during the same period. The value of such deals was 638 million USD in the year 2005 and the value of same rose to 5504 million USD in the year 2007 and it was 5555 million USD in the year 2008.

Within Growth/Late stage deals the private equity companies also focused on PIPE transactions (Private Investment in Public Equity). The volume as well as value of PIPE deals thus increased significantly during the above considered years (2005-2008).

It also emerges that even during this time period private equity companies were still investing less in the Early Stage deals in comparison to Growth Stage deals. As discussed earlier this may be on account of fact that Early stage deals in comparison to the Growth stage deals carry more risk.

It also emerged that private equity companies operating in India were not very interested in Buyout deals as a matter of investment strategy. The number of buyout deals has not increased substantially during the above considered period. The number of such deals was 5 in the year 2005, the same rose to 14 by the year 2006 but declined to 10 again by the year 2007 and was 9 in 2008. The value of buyout deals was 306 million USD in the year 2005; the value of the same increased to 1,135 million USD by the year 2006 but declined to 647 million USD by the year 2007 and was 383 million USD in the year 2008. Very few private equity companies like Navis Capital, ICICI Ventures, Infinity Capital, KKR, Actis, WL Ross, and Blackstone were interested in buyout deals. Largest buy out deal value, during the period was the buyout of Flextronics software by KKR and Sequoia in April 2006, followed by purchase of Sharekhan by Citi in Jan 2007 and Purchase of Gokaldas Exports by Blackstone in August 2007.

Period of 2004-2008 can be cited as second boom period of private Equity Companies operating in India. Between the periods 2004-2008, private equity companies started acquiring significant stakes in Indian Companies. During the period Private Equity Companies invested USD 50 billion in more than 1,500 Companies. This includes some of the largest enterprises today. Private Equity investments in India grew at CAGR of 72% between 2004 till 2008 that from an amount of USD 1.6 billion to an amount of USD 14 billion.

Some examples that can be cited here are Temasek Investment in Bharti Airtel (2007), IDFC investment in GMR (2004), Sequoia investment in SKS Microfinance (2006). The number of companies that received PE funding during the period (2004-2008) is as follows:

**Table 5: Private Equity Investments – 2004 till 2008**

Year	Companies receiving PE funding	Amount Invested (USD Billion)	CAGR of Private Equity Investment - 72%
2004	82	21.9	
2005	158	14.1	
2006	320	25.0	
2007	458	34.6	
2008	448	31.5	

**Source: India Private Equity Reports, Bain & Company, Indian Venture Capital Association**

**(iii) Phase III – 2009-2013**

Post Global Financial Crisis Private Equity investment also experienced slowdown India Specifically in the Year 2009. The CAGR of Private Equity investment in India was minus 68%. Following are the details of changes in Private Equity investments in some important Global Markets are as follows:

**Table 6: CAGR Changes in Select Global Markets**

Market	CAGR (2004-2008)	CAGR (2008-2009)
Korea	+21%	+64%
South-East Asia	+35%	-17%
Japan	-1%	-36%
Australia/New Zealand	+32%	+123%
India	+72%	-68%
Hong Kong /Taiwan	+61%	-70%
China	+39%	-12%

**Source: India Private Equity Reports, Bain & Company, Indian Venture Capital Association**

Signs of revival in the Private equity market started emerging from 2010. Following are the details of Private Equity investments in India for the period 2009-2013.

**Table 7: Private Equity investment details for the period 2009-2013**

Year	Number of PE Deals	Amount of Investment USD Billion	Number of Active Funds	CAGR Year on Year Basis
2009	251	4.58	181	-68%
2010	338	9.5	202	+111%
2011	531	14.8	238	+33%
2012	551	10.2	285	-18%
2013	696	11.8	314	+39%

**Source: India Private Equity Reports, Bain & Company, Indian Venture Capital Association**

Some reasons for changes in the private Equity investments for the above stated period are European Debt crisis, Concerns about returns being generated in India market (Stock Market indices did not indicate any positive movements in the years 2011 and 2012), Exit pressure on Private Equity companies and last but not the least macroeconomic environment in India. From the year 2013 onwards Indian PE market is witnessing third major boom period. This is on account of change in outlook associated with the Indian economy.

**CONCLUSION**

Private Equity investment is closely linked to stock market performances and outlook on economy. In India we have witnessed three major cycles till now and we are in the midst of third boom cycle now. Global Outlook on Indian economy is again becoming very positive and this may result in new investment

opportunities for Private Equity Companies in India. This cycle will again end with either change in Global market outlook, with changes in Indian Macroeconomic indicators or may be changes in Indian Stock Market indices.

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