

INDIA'S STARTUP STORY

UNLOCKING TRUE POTENTIAL

India's startup ecosystem is not a recent phenomenon. It has been prevalent for over four decades. It has given rise to several industries and bolstered the Indian economy in its varied phases of evolution. In recent times, however, the startup ecosystem has garnered significant attention, not only because of the sheer number of entrepreneurial initiatives, but also given its strong angel investor network. With nearly \$20 bn of capital inflows and about 100,000 people, the Indian startup ecosystem today ranks amongst the top five in the world. However, the question that is foremost in our minds is whether this rapid growth is sustainable. What does India need to fully unlock the potential of startups and how best can it achieve this?

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The story of Indian startups is not just limited to the current century; in fact, it began over four decades ago. Through the 80s, a handful of pioneering IT service companies such as TCS, Infosys and Wipro placed India firmly on the global economic map. These companies invested in technology and leveraged the country's young, English-speaking workforce to provide cost-effective technology services to clients across the globe. The result is an industry that currently employs nearly four million people and generates \$150 bn in revenues.

The 90's witnessed the launch of Airtel, which today is India's largest telecommunications company, with over \$15 bn in revenues and more than 350 million consumers worldwide. Similarly, the 90's also witnessed the launch of ICICI, HDFC and Axis banks, which have gone on to rank amongst the top 10 banks in India as per balance sheet size (as of March 2016). In fact, ICICI and HDFC Bank rank number two and three respectively, after the State Bank of India. Most importantly, they have fundamentally reshaped every element of the Indian banking business model, leading to the betterment of the sector as a whole.

Cut to the present and India has seen a dramatic acceleration in both the quantum and the diversity of startups. Over the last 10 years, India has become one of the top five startup ecosystems in the world, alongside the US, China, the UK, and Israel. The country today is home to

a strong angel investor network with the sector witnessing active participation from every major Venture Capitalist (VC) or Private Equity (PE) firm. Over the same period, the startup sector has attracted nearly \$20 bn of capital inflows and today employs about 100,000 people, with that number doubling every two years. Furthermore, over 100 active incubators help entrepreneurs experiment with new ideas, by offering them functional expertise and resources.

This recent scale-up of the Indian startup ecosystem is the result of a confluence of multiple factors. On the demand side, there has been a massive explosion of consumers going online, driven by smartphone proliferation. The sheer number of these individuals and their ever-rising income levels, coupled with their desire for consumption, makes them a highly attractive captive consumer base. On the supply side, there has been a massive inflow of entrepreneurial and technology talent. The creation of marquee startups in India has made 'business' a highly lucrative career beyond the traditional mercantile community. Nearly 40% of India's startup founders and leaders come from premier engineering colleges and business schools, such as the IITs, IIMs and ISBs. This trend has reversed the nation's 'brain drain' by not only retaining the best and brightest in India, but also by attracting top quality talent of Indian origin back into the country. Finally, large capital inflows from global investors has helped catalyze the entrepreneurial



spark in our country. The vibrant startup ecosystem we see today, is the result of all these positively reinforcing megatrends.

However, some of the euphoria has subsided recently. Funding in 2016 has been much harder than the past couple of years. Investors are marking down the value of many startups. They are asking founders to stretch the current funding runway for longer by reducing cash burn, and asking tougher questions around the sustainability of business models as well as profitability. So, does this signal that the Indian startup ecosystem has hit a plateau? Quite the opposite, we think. If harnessed well, this ecosystem has the potential to change the face of the country over the next two decades.

All successful startups are based on a potentially disruptive consumer value proposition. Think about the convenience of an e-commerce marketplace, or the ability to call a taxi or book a room at the click of a button anywhere, while paying through a mobile wallet. Or consider the benefit of reducing turnaround time in logistics by 50%. What clearly comes through is a wide range of measurable as well as intangible consumer and business benefits.

But what is not so obvious is how the startups amplify the economic impact of technology at the grassroots level. For example, e-commerce companies such as Flipkart, Snapdeal and Shopclues etc. have put small businesses on an unimaginable platform. OLA and OYO have helped thousands of taxi drivers and hundreds of small

hotel owners achieve significantly higher productivity. Likewise, Rivigo is fundamentally improving the livelihood of its fleet pilots (i.e. truck drivers). It is this ability to inspire transformation at the ground level that gives Indian startups a truly unique character. If this innovation and energy can be directed to areas such as literacy, skill development, healthcare and sanitation, financial inclusion and natural resources, imagine what it can do for India!

Making this dream a reality will no doubt take significant effort, resources and resilience. More important, different stakeholders will need to play their part right, so as to achieve the desired results.

Founders must build startups that solve problems that are unique to this subcontinent, in addition to adopting proven global business models relevant to this part of the world. Startup teams in India are much younger than elsewhere globally. As a result, founding team members typically lack the experience of having worked in a mature organization, and believe in learning by doing. This entrepreneurial culture can result in startup teams making wrong choices with respect to organizational structures and roles, business processes, sales, marketing, and branding, often proving fatal for the venture. This is particularly crucial when they are transitioning from getting the 'product market fit' right to scaling up the business.

These teams have a lot to learn from Israel—widely known as the 'Startup Nation'. Like Indian entrepreneurs,



Startups have the potential to equip the semi-skilled population

their Israeli counterparts also want to build the 'next big thing'. But the latter are more successful in their pursuits as they do a few things differently. They spend a disproportionate amount of time on research and development (R&D), resulting in unique ideas with a global appeal. Further, they follow a 'lean-startup' strategy and carry out extensive market experiments before raising large amounts of capital. Apart from being typically older than their Indian counterparts, Israeli entrepreneurs also often have prior professional or military work experience. While some of these traits are cultural, many of them can be imbibed by Indian entrepreneurs to script their own success stories.

The startup journey also needs continual support from the government. Setting up a SIDBI-run Electronic Development Fund (EDF) that makes the Indian Government a Limited Partner (LP) in a fund for the first time ever, is a great example. However, more is needed. The country's administration needs to create a more progressive policy framework to nurture new ventures, especially encouraging them to address the country's unresolved problems. While the long-term commercial viability of any business is non-negotiable, startup businesses will likely have different maturity cycles depending on the sector they are in. For example, startups with a social impact bias may take longer to reach self-sustainability, but have the potential to create significant eco-social value.

Without an appropriate enabling environment, there will be disproportionate emphasis on near-term commercial viability, leading to crowding out of startups that want to focus on longer term innovation for social good. The government can provide higher incentives for investment in sectors that are most crucial for India. These incentives can take different forms, with several precedents such as generation-based incentives for renewable energy, tax and depreciation benefits, capital subsidies, priority sector banking norms etc., already been set. Consider an example: If the government creates norms mandating

partial allocation of priority sector lending requirements toward social impact startups, a massive amount of capital could be channeled to deserving sectors. Having said this, it is important to remember that subsidies alone cannot create solutions that are sustainable over the long term. Subsidies should be directed toward 'turbo-charging' startups in the social impact sector, while holding these new businesses accountable for creating long-term sustainability.

The government could also do more to foster the creation of a larger number of startup cities. While India has joined the league of the top five global startup ecosystems, only one Indian city (Bengaluru) ranks among the top 20 startup cities in the world. Therefore, much like the creation of Special Economic Zones (SEZs) to promote the growth of IT services, the government can facilitate the creation of five to ten startup-focused centers across the country. Indian academics can further provide a boost to this endeavor by contributing novel ideas based on their deep technical and functional expertise.

And finally, corporate India can play a big role in shaping the future of this landscape. They should fully embrace corporate venturing, providing new companies with the capital to compete on a global platform. There are clear early signs of this happening with companies like Infosys, Wipro etc. seriously investing in startups through VC funds. But a lot more can be done. Indian corporates are today sitting on INR 135 bn in cash. They all aim to embrace new digital technologies such as mobile, Cloud, Big Data and analytics to transform their existing businesses, but often lack the mindset and skillset to do this. The way around this challenge is for the firms to acknowledge this capability gap and use their capital instead to establish independent startups employing external talent.

Ultimately, the combination of progressive government policies, capital assistance from corporates, guidance from academics and the sheer brilliance of Indian entrepreneurs, cumulatively can create the secret sauce required to unleash the true potential of our startup ecosystem.

While India is a land of many unique problems, its greatest assets include its brainpower and resilience. By harnessing these, it can overcome a wide range of challenges through innovative solutions. Startups provide an excellent environment to nurture talent as well as to leverage the power and scale of latest technologies. In doing so, some of them hold the promise of transforming the country and potentially becoming the next set of Indian technology giants. Now is the time for all stakeholders to come together to make this vision a reality.

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