Our Views

Start Ups still attractive albeit with a new start

Most Indian start-ups which got listed on bourses in the last couple of years are trading at a discount ranging between 5.0% to 75.0% to their offer price. This market performance of the listed new age digital companies is a true reflection of how investor sentiments in the public market are perceiving the negative bottom-lines and higher valuations of start-ups. These factors, coupled with macro-economic headwinds including the liquidity tightening, has left start-ups who are still burning cash at a crossroads. So, what is different about the public market investor sentiments from the private investors? Well, while public markets investors want start-ups to be more disciplined in their spend, private investors take a long-term growth perspective of business and are more patient.

Now, the rational perspective of the public market valuation has spilled over to the private market as well. Consequently, private capital too has become scarce. Large Private Equity and Venture Capital funds (PE-VC) have also become more conservative given the investment environment in the recent quarters. While 2021 was a banner year for the Indian start-up ecosystem with ~220% growth in PE-VC investments over 2020, the outlook for 2022 has not been very attractive thus far. Our start-ups received ~$11bn in CY2020 which increased to ~$35bn in CY2021. However, 2022 is witnessing a dramatic slowdown with year-to-date flows of ~$20bn. Deal values witnessed a decline of ~76%, with late-stage deals taking a major hit. In general, early-stage start-ups can still raise capital more easily as they are typically insulated from fluctuations in the public markets. Almost 750 start-ups got funded in CY2020. This number increased dramatically to 1000+ in CY2021. However, CY2022 has seen a significant reduction with ~800 transactions year to date.

As the start-ups are preparing to dodge the ongoing slowdown globally, India is expected to be doing relatively better compared to its peers. However, Indian start-ups should also read the message from the public market. Investors are willing to sacrifice growth for a clear path to profitability. I do think though that market is still open to provide sufficient financing to start-ups particularly those who have the right business model and are using deep technology or digitisation as a tool for solving a problem. The other underlying message from the public market is to tighten the belt. As the supply of money so far was easy, a bit of fat has been built up which can easily be restructured. So, with some focus on getting lean, start-ups can reduce the cash burn, conserve cash, and turn profitable sooner than their present estimated timeframes.

In these difficult times, one could also consider alternative funding plans. Venture Debt is emerging as an alternative for providing short-term finance. Though the high-risk perception of start-ups has been an obstacle for entrepreneurs to raise such debt capital, to facilitate this and to continue to boost the start-up industry, the Government of India has recently launched **the Credit Guarantee Scheme for Start-ups (CGSS).** The aim is to improve the availability of collateral free loans for start-ups through credit guarantees on loans extended by member institutions (MIs) to eligible start-up borrowers. CGSS can be a significant catalyst for start-ups who need immediate funding or liquidity to flourish. The scheme is an excellent support to start-ups. However, the current limit of a maximum of 10 crores per start-ups could be a dampener for start-ups who are in the late-stage category and require large funding support.

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All said, the feedback from public market will result in a more reasonable start-up valuation and will shift the focus from fast growth to sustainability. On the brighter side, the availability of a significant dry powder with PE-VC funds, significant growth and constant support from the government are an indicator that our start-up ecosystem will continue to thrive albeit with **a new start!**

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