

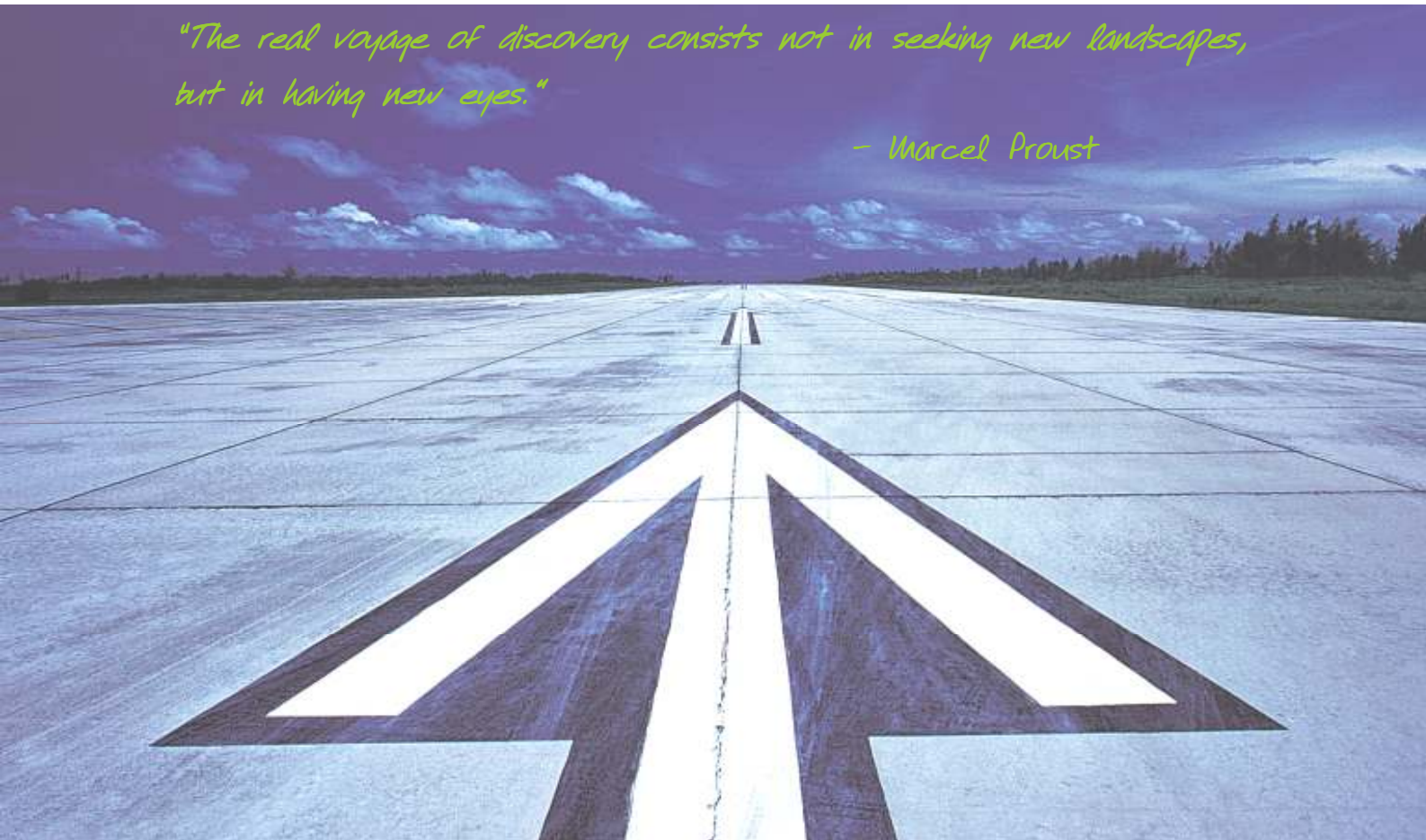
Deloitte.

Trends in Venture Capital in India

Findings from the Deloitte and Indian Venture Capital Association survey of venture capitalists in India.

*"The real voyage of discovery consists not in seeking new landscapes,
but in having new eyes."*

- Marcel Proust



About the Survey:

The survey was administered to Indian venture capitalists (VCs) as well as foreign based funds operating in India. This research was conducted in middle of last year, 2006 on a joint online platform of Deloitte and Indian Venture Capital Association (IVCA).

The survey questions were designed to evaluate the environment for venture capital in India focusing on the preceding and forth-coming quarters with a view to indicate the degree to which VCs are expanding their investment focus, identify areas they are targeting for expansion, and barriers to developing the VC environment to its full potential in India.

Better Economic Conditions Support Growth

VCs perceived the current economic environment conducive for their business and expected the same trend to continue into the fourth quarter. Majority of the VCs queried find the current economic conditions better than 2005 and anticipate the same to continue through last quarter of 2006.

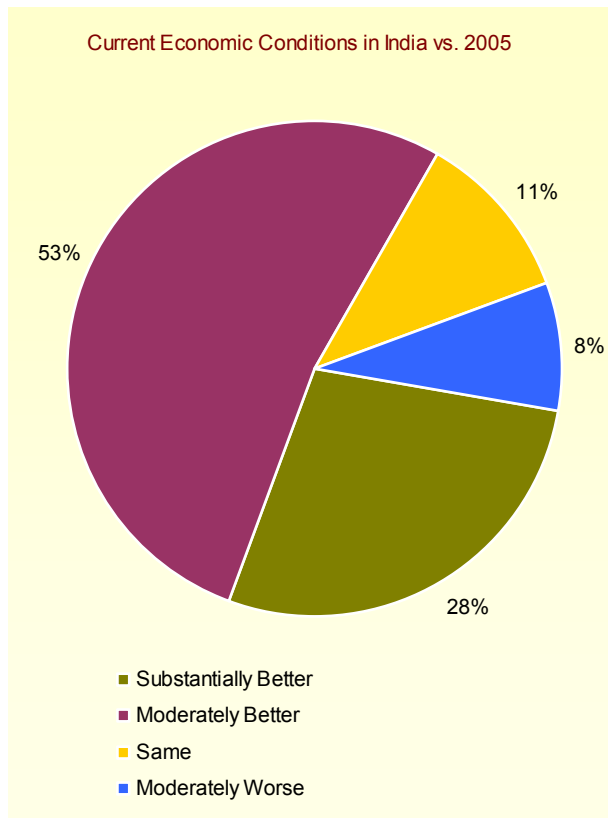


Figure 1

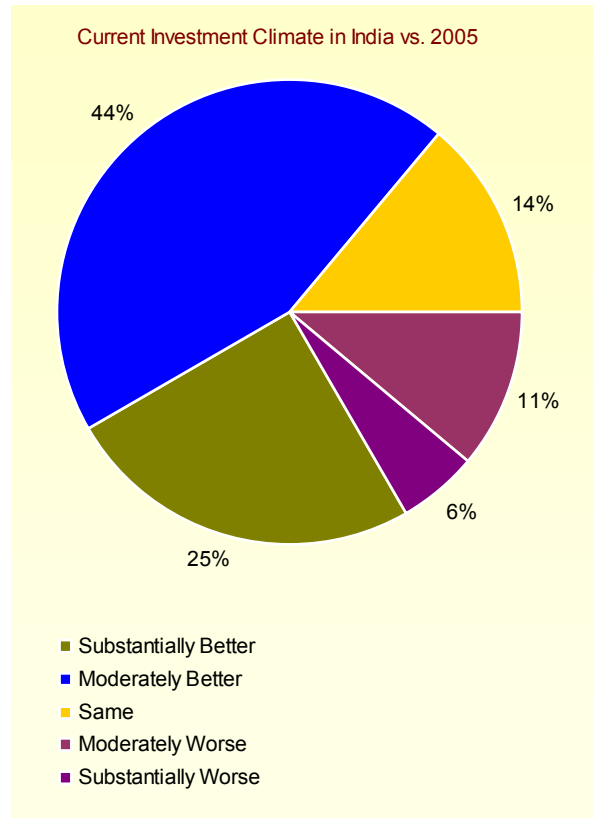


Figure 2

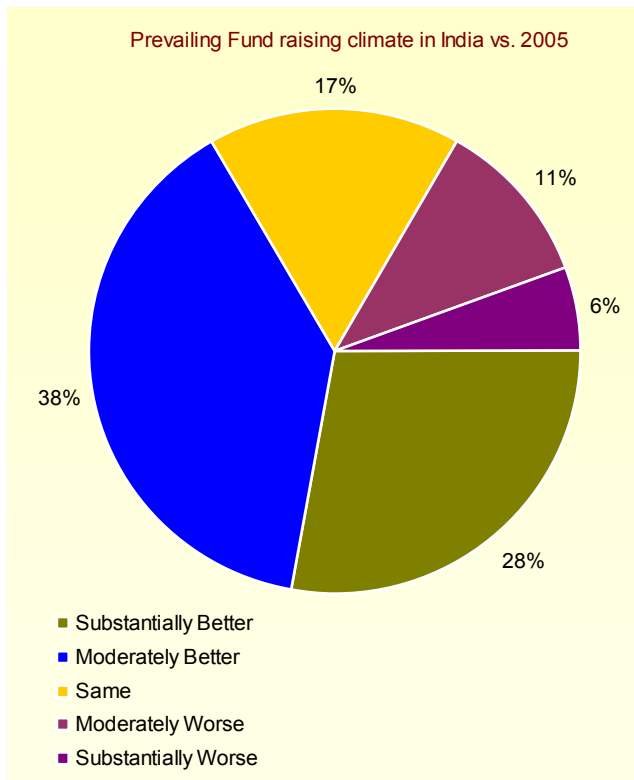


Figure 3

VCs Make Hay While the Sun Shines

India's economic growth rate accelerated to 9.2% in the period July-September from 8.4% in the same period last year on the back of a strong performance by the manufacturing and services sectors¹. This justifies, to a great extent, the ease in fund raising compared to 2005 as reflected in the survey. It also adds strength to the survey finding, that one of the major catalysts for increased investments in India, has been the growing economy followed by growth in the services sector.

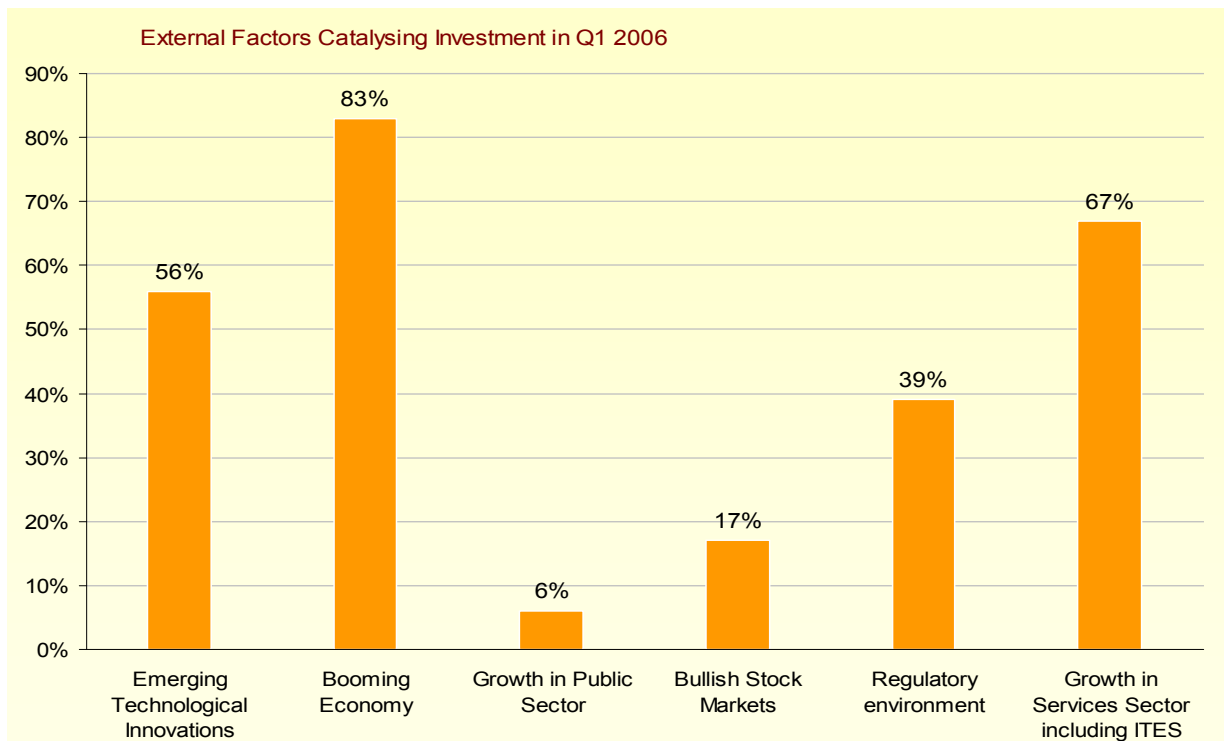


Figure 4

¹ "India's growth story just got better" – Business Standard, 01 December, 2006

VCs Have All the Reasons to Smile

In querying VCs about their expectations from last quarter 2006, more than half of them said that they either expected better or same economic conditions to prevail. Overall they were positive about the investment climate. Adding strength to their views, Mr. P. Chidambaram, the present Finance Minister said, “There is no limit to my expectation on GDP growth”² when asked to comment on the expected annual rate of growth.

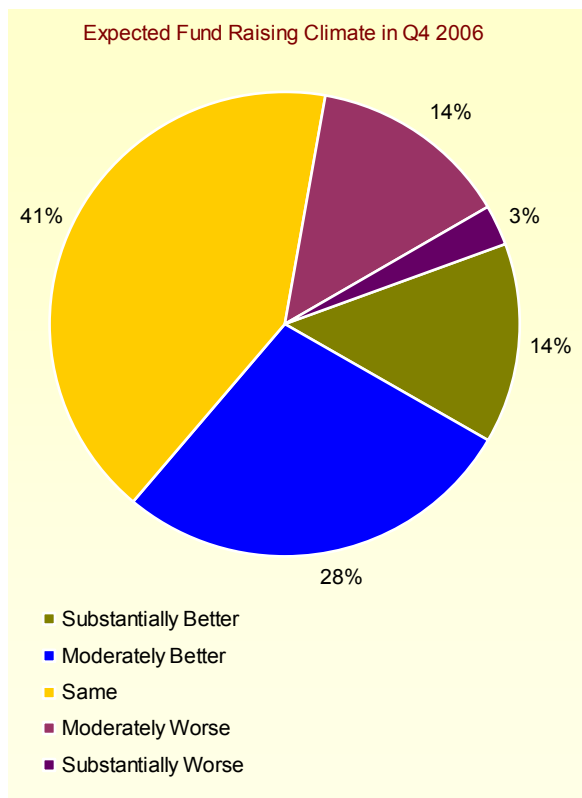


Figure 5

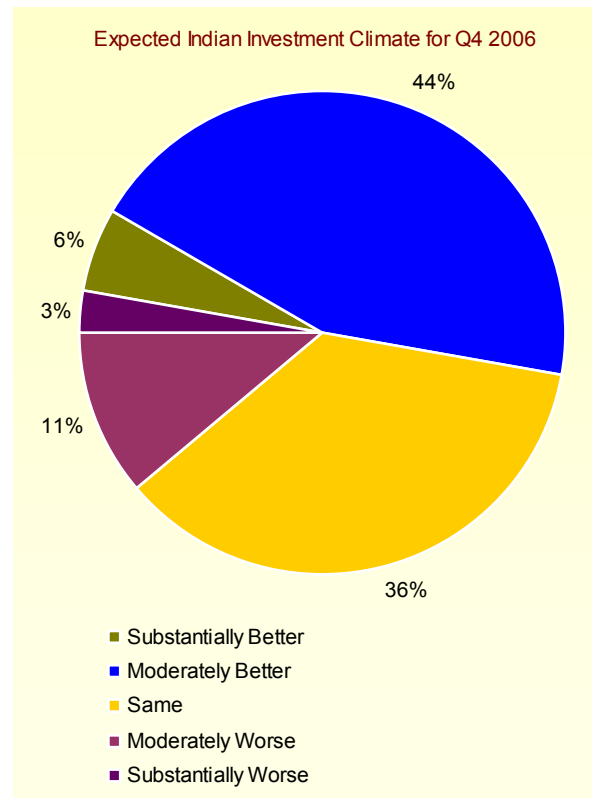


Figure 6

² “India’s growth story just got better” – Business Standard, 01 December, 2006

Performance Outshines Skepticism

Close to 70% of the respondents said that the portfolio results till Q3, FY 2006 were better than the 2005 performance results and they expected even better results in last quarter of 2006. Venture Capital and Private Equity firms have invested US\$1.9 billion in across 123 deals between January to November 2006.

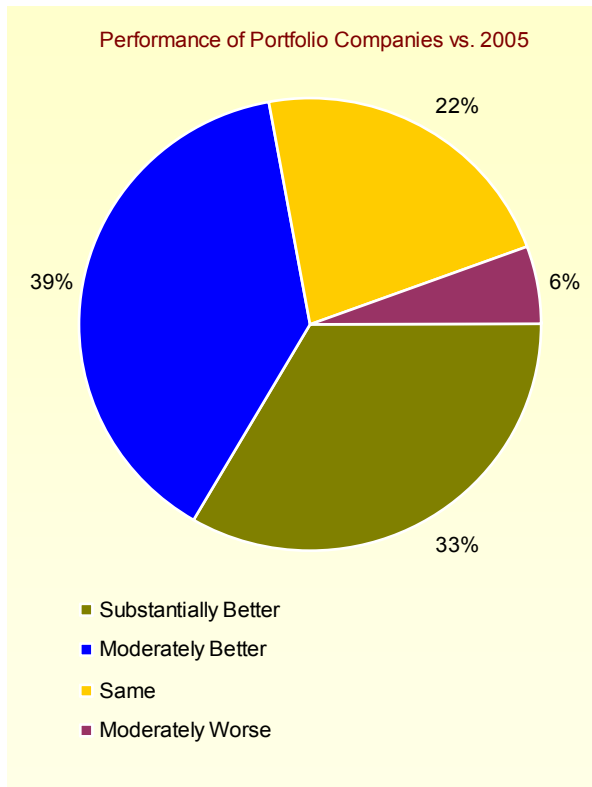


Figure 7

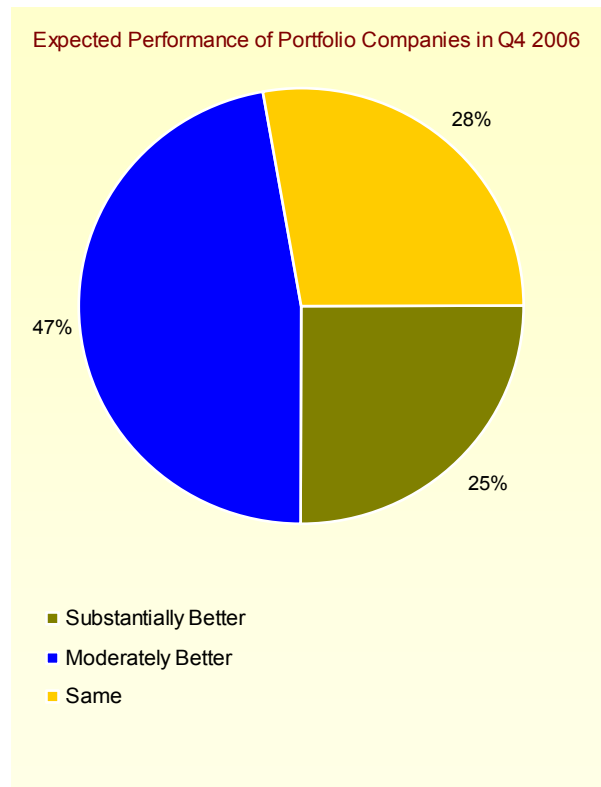


Figure 8

VCs Set Their Eyes on East

VCs realized the potential of the eastern states, and plan to increase their investments in the region. Towards the end of 2006, we can expect a shift in the investment towards eastern and northern regions. Of the fresh investments set out for the last quarter, the eastern region would likely witness an increase of almost 67% followed by the northern region with an increase of 40%. Since the queried venture capital professionals do not plan any fresh investments in the western India, the overall share of the west zone in their investment portfolio is expected to fall to 26%. South India fails to charm VCs for fresh investments.

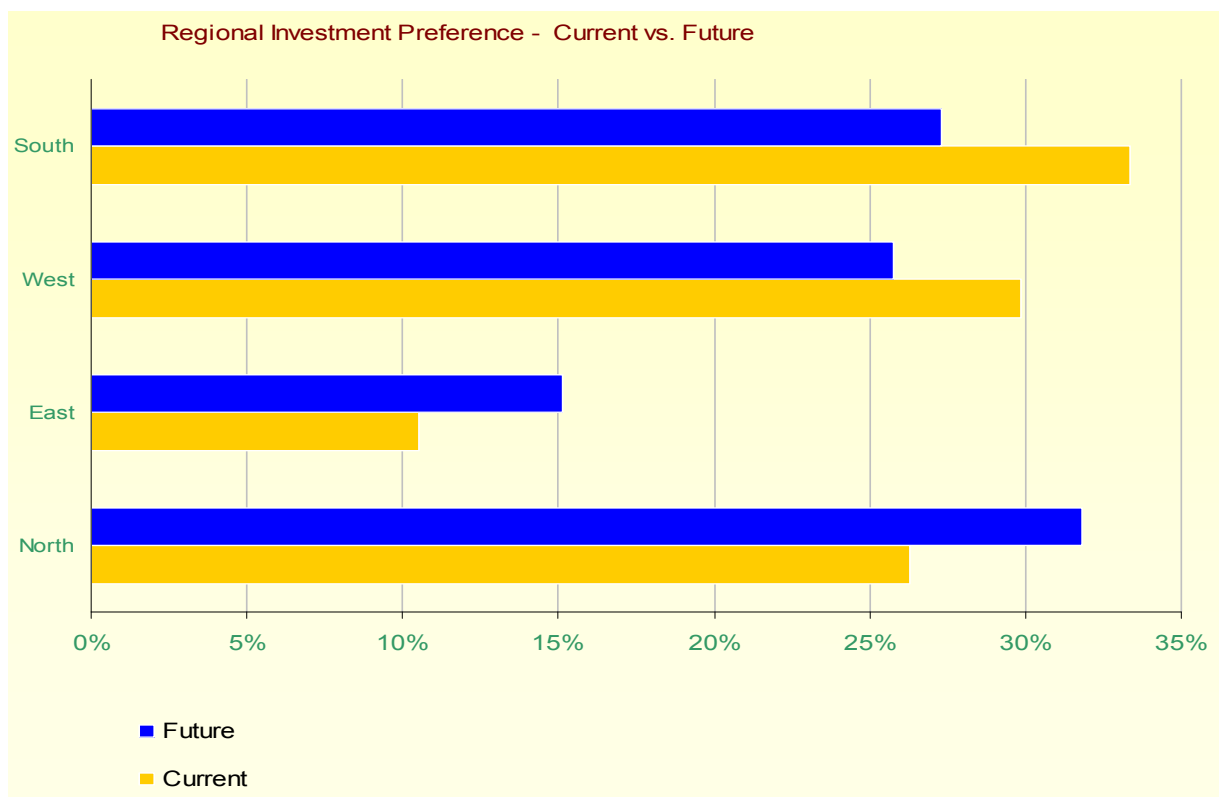


Figure 9

Star Performers – Construction and Bio Technology

The survey very clearly brought out the two sectors which interest VCs - construction & real estate and bio-technology. Till Q1 2006, of a total of 91 investments made by the survey respondents, 20 were in the construction industry and bio-tech was close at heels with 17 investments. The investments, though accounting for less than 10% of total investments made by the queried VCs, clearly indicates the future trends of where the cash would flow. The survey seems to suggest that investments are distributed across the various sectors, and VCs have a well balanced portfolio and are ready to venture out beyond IT services and BPO/KPO industry.

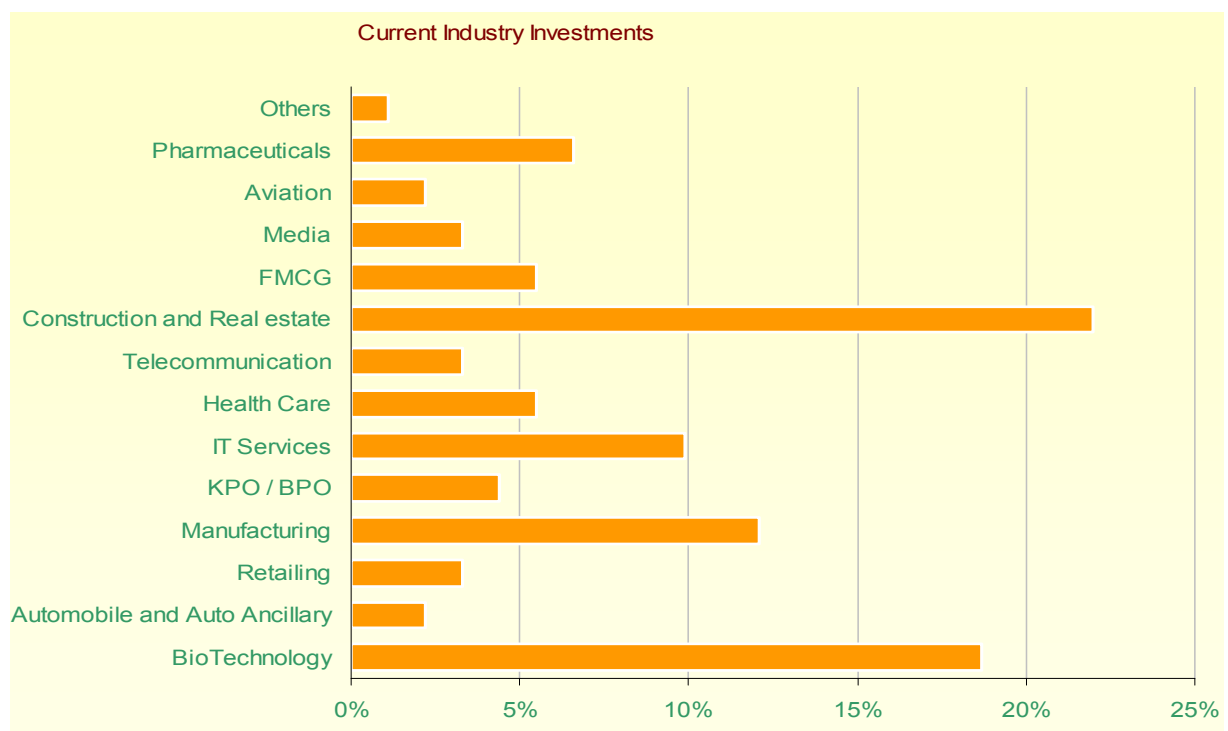


Figure 10

Construction and Manufacturing – The Future

Construction and real estate along with manufacturing industry saw an increase in investments in FY 06. The VCs are expected to continue focus on these two sectors with fresh investments taking place in industries like consumer products, energy sector, IT mobile space and specialty chemicals.

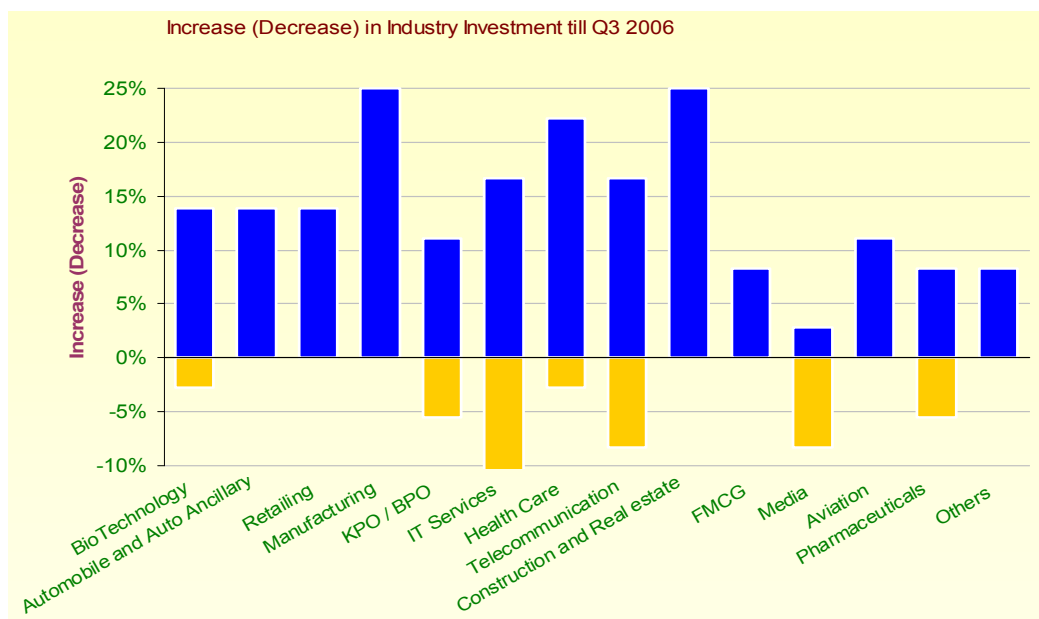


Figure 11

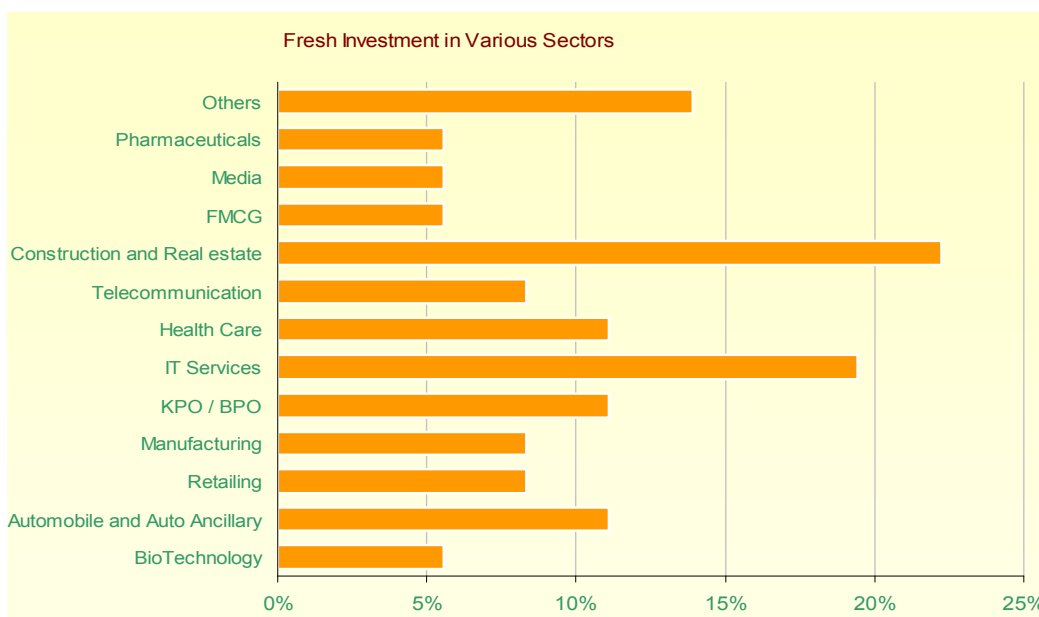


Figure 12

Entry and Exit Options

The survey very clearly suggested that second stage financing remains the most preferred stage for VC investment. The early stage financing along with startup and seed investments have attracted few VCs but have failed to generate enough confidence in the VC community. With the economy booming and VC professionals world over taking a note of India, one can expect higher investments for the start ups and seed stage financing.

To exit the deals, VCs have various options but IPOs seem to be the preferred exit route. Buy back by promoters also proves to be a good exit option. With the stock indices heading north, exit through stock market has also become a favourite route to exit deals.

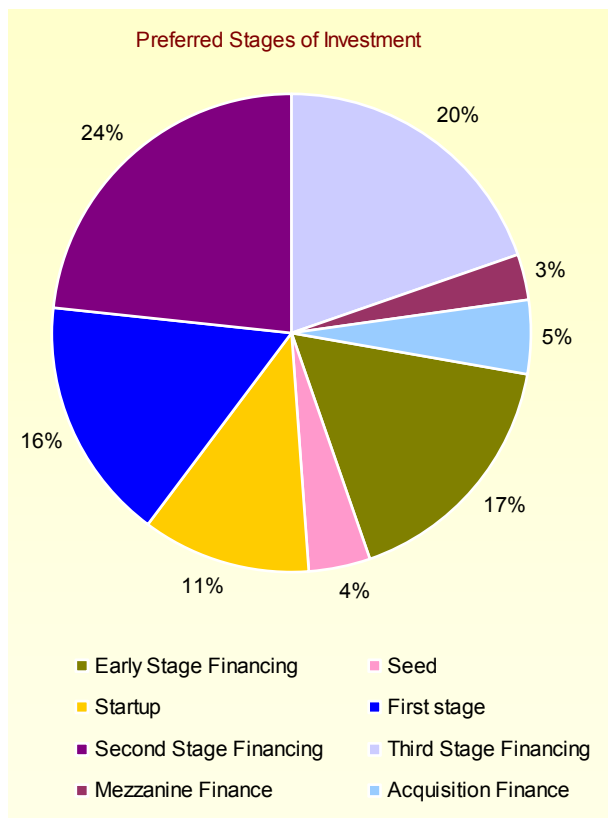


Figure 13

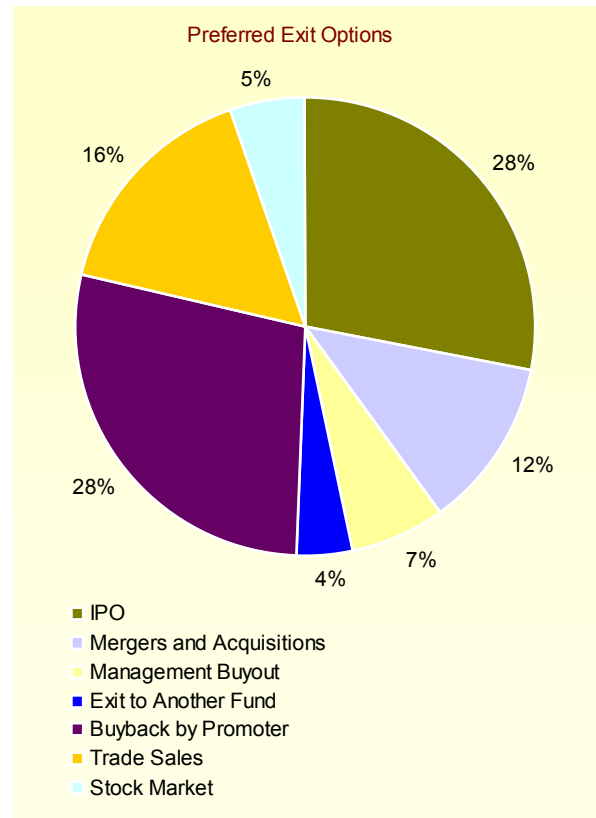


Figure 14

Impediments to Investing

The Indian opportunity is no doubt promising, as evidenced by the VCs' responses. Nonetheless, the market is challenging for successful investment. In terms of impediments to expansion, lack of quality deals was a major concern amongst respondents. Beyond administrative delays in documentations and approvals, the respondents identified a number of other concerns that varied as per different sectors.

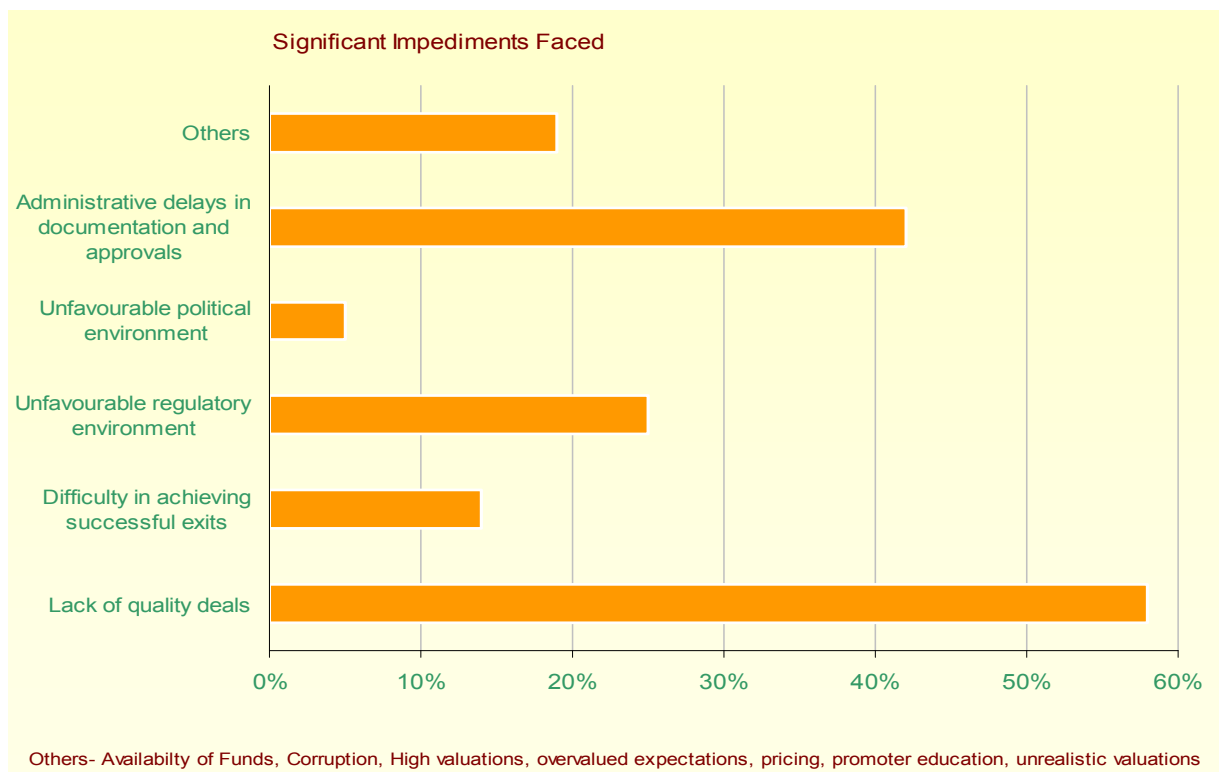


Figure 15

Summary

The survey suggests that the maturing of the still nascent Indian venture capital market is imminent. VCs have taken notice of newer avenues and regions to expand. VCs have moved beyond IT services but are cautious in exploring the right business models, for finding opportunities that generate better returns for their investors.

In the study, VCs gave a positive assessment of current conditions, both in terms of the overall business climate and the climate for fund-raising specifically, also predicting a continuation of these conditions into the next quarter.

VC professionals remain positive and confident about conditions for their business in the short to medium term: assessing the past quarter favorably and giving encouraging predictions for the quarter to come. Survey respondents were also upbeat about the attractiveness of the India as a place to do business.

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