

Understanding the Financing Challenges Faced By Startups in India

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Abstract

India is a country in South Asia. It is the seventh-largest country by area and the second-most populous country with over 1.2 billion people. Large population implies a large potential market in India; however, it also leads to heavy employment pressure in Indian society. In recent years the self-employment consciousness among college students are increasing and the students are less likely to rely on parents or schools or wait for opportunities. Instead, they tend to take initiative to look for new chances for themselves. This research aims to investigate the challenges of financing startups in India. This paper is intent to explore the main difficulties faced by startups in India, and discuss the financing resources of startups in India by Using a literature-based analysis.

1. INTRODUCTION

1.1 Definition of Startup

A startup company or startup or start-up is a young company that is just beginning to develop. Startups are usually small and initially financed and operated by a handful of founders or one individual. These companies offer a product or service that is not currently being offered elsewhere in the market, or that the founders believe is being offered in an inferior manner. In the early stages, startup companies' expenses tend to exceed their revenues as they work on developing, testing and marketing their idea. As such, they often require financing. Startups may be funded by traditional small business loans from banks or credit unions, by government sponsored Small Business Administration loans from local banks, or by grants from nonprofit organizations and state governments. "A startup is a company designed to grow fast. Being newly founded does not in itself make a company a startup [1-3]. Nor is it necessary for a startup to work on technology, or take venture funding, or have some sort of "exit". The only essential thing is growth. Everything else we associate with startups follows from growth

1.2 A LIFE CYCLE VIEW OF YOUNG COMPANIES

If every business starts with an idea, young companies can range the spectrum. Some are unformed, at least in a commercial sense, where the owner of the business has an idea that he or she thinks can fill an unfilled need among consumers. Others have inched a little further up the scale and have converted the idea into a commercial product, albeit with little to show in terms of revenues or earnings. Still others have moved even further down the road to commercial success, and have a market for their product or service, with revenues and the potential, at least, for some profits.

1.3 CONTEXT OF ECONOMY IN INDIA

The Economy of India is the seventh-largest in the world by nominal GDP and the third-largest by purchasing power parity (PPP). The country classified as newly industrialized country, one of the G-20 major economies, a member of BRICS and a developing economy with approximately 7% average growth rate for the last two decades [4, 5]. India's economy became the world's fastest growing major economy from the last quarter of 2014, replacing the People's Republic of China.

1.4 BACKGROUND OF GRADUATES' ENTREPRENEURSHIP IN INDIA

Large population implies a large potential market in India; however, it also leads to heavy employment pressure in India's society. According to statistics, there are approximately 700 universities and more than 35,000 affiliated colleges enrolling more than 20 million students, Indian higher education is a large and complex system. The structure of degree-granting institutions is cumbersome primarily due to "affiliation" and funding sources. More than 85% of students are enrolled in bachelor's degree programs with majority enrolling in three year B.A., B.Com. or B.Sc. degrees. One-sixth of all Indian students are enrolled in Engineering/Technology degrees. These results in an estimated 26.5 million students enrolled in Indian higher education in 2014-15 and 9 million graduates.

2. OBJECTIVES OF THIS PAPER

This paper is intent to explore the main difficulties facing startups in India, and discussing the principle financing resources of startups in India. More specifically, this paper tries to analyze challenges of Indian financing startups.

3. LITERATURE REVIEW

3.1 Main Problems Faced by Startups in India

➤ The Imperfect Education System and Conservative Lifestyle

The education system is one of hindrance for startups. In college, students are usually trained with advanced techniques but lack of marketing, sales and operational ability and leadership skills needed to advance their own enterprises. In addition, conservative lifestyle also contributes as one of obstacles. As a culture of family remains, family remains skeptical to change and prefer options that are able to provide a steady income rather than engaging risk. This places pressure on the budding entrepreneur who fall victim to the dichotomy of providing for the family instead of following some "whimsical" dream (Au & Kwan, 2009)[3].

➤ Lack of Support Networks and Entrepreneurship Ecosystem

One of the major challenges is that there is severe shortage of startup support networks and entrepreneurship ecosystems. In many western countries, there are special institutions serve as incubators, startup accelerators, startup competitions for entrepreneurs to put their ideas to test and obtain necessary guidance. In India, incubators, startup accelerators, and startup competitions are slowly making their way into the first tier cities, but there truly are not enough to go around. As a result of this shortage, many startups fail at the "idea" stage of their business. The ecosystem usually does not directly provide funding to start-ups; they just serve as platforms that link investors and entrepreneurs so that entrepreneurs can obtain necessary funding to test out their ideas. The lack of these facilities makes it more difficult for entrepreneurs to find investors. In return, investors are more difficult to find entrepreneurs as well.

Even if entrepreneurs are able to find investors, they will face an entirely different set of challenges. Indian culture inherently does not promote entrepreneurship. Conversely, it encourages stability, employment at large state-owned or private organizations and, above all, teaches people to be risk averse. Even if young Indian individuals have intention to start their own business, their family usually places a considerable amount of negative pressure on them to forget entrepreneurship and look for a "stable job" instead.

➤ **India lacks enough angel investors to fund start-ups**

Unlike the West, India does not have an adequate number of angel investors who can fuel the growth of the country's thriving start-up ecosystem, industry body Nasscom has said. "For a successful start-up ecosystem there is a need for enough angel investors who can support budding entrepreneurs from an early stage. But this is not happening in India and there is a serious lack of it," Nasscom Vice-President Rajat Tandon told PTI. "High net-worth individuals and corporate executives, among others, should come forward and participate in this growth story," he said. A recent report by Nasscom had said India ranks third among global start-up ecosystems, with more than 4,200 new-age companies. Tandon said, "The case is very different in countries like the US. People are just waiting to invest in good companies. We should also have something like that." "Mainly, investors (in India) are afraid because there is a high risk of failure in these investments and also there is a lack of policy on such investments," he added. "Why will investors put money in such companies? They need tax benefits and a number of other things to put in their money. We have already written about these things to the Government and I am sure we can expect something by the year-end," he said. In his Independence Day speech, Prime Minister Narendra Modi had announced a new campaign „Start-up India; Stand up India" to promote bank financing for start-ups and offer incentives to boost entrepreneurship and job creation in the country.

"At Nasscom, we are not only encouraging investors but also asking people to mentor start-ups. Like someone has a design business, they can help start-ups develop UIs and guide them in the process. In return they take some equity," he said. "And there are people like Ratan Tata and Azim Premji, who are making a slew of investments and helping these young entrepreneurs. They are the inspiration," he said. Ratan Tata has invested in a number of companies including Ola, Snapdeal, Paytm, Urban Ladder, and Bluestone. Wipro boss Azim Premji has funded companies such as Myntra and Amagi, among others, through his investment arm Premji Invest [4].

➤ **Human Talent**

Compared to large mature enterprises, small startups are in an exponentially more difficult dilemma and encountering much severe challenging in recruiting due to the reason that it cannot pay high salary to its employees or offer any career development opportunities aside from building their business from the ground up. What is worse is that working for a startup in China is far less glamorous than working for a startup in the west due to culture differences. It is a disaster for a company who needs to execute on their business plan with minimal errors to just survive the month.

4. Conclusion

Many businesses start with a dream, but it takes more than just a dream for them to grow into successful businesses—including the tenacity to overcome the many challenges facing startups today. Startups take time, effort, and energy. Funding is a major concern for startups and small businesses. When the economy tanked, it made it harder to convince investors and banks alike to part with the cash that's essential for growth in the early days of a business. Credit today is tight, and it's not clear precisely when it will become more readily available. Plus, there's a growing trend of smaller initial investments in early stage startups. Intensifying the challenge of raising funds, major leaps in technology have led investors to raise the bar in terms of how much legwork entrepreneurs are expected to do before even pitching their companies.

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