Startups- Taking India towards a Knowledge Economy
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Abstract: Start-up has become the new buzzword in the Indian business jargon. With its emphasis on innovation and technology, they are the future for India. However, their journey has been a roller-coaster ride. From being plush with funding, we are increasingly seeing investments to companies with sustainable models. Moreover, this trend is also moving in to Tier-2/3 cities. While most of them still suffer from the issue of profitability, we can expect that this will settle down in due course and usher a new phase in the economy.

Keywords: Start-ups, software, technology, funding and investment.

INTRODUCTION

What is a Start-Up? Eric Ries, the creator of the Lean Startup movement, defines a startup as a newly formed company, the purpose of which is to develop new, usually innovative products or services in uncertain circumstances. If it satisfies a new need, present in a broader area or even globally, it also has great growth potential [1]. There has been a phenomenal growth of Start-ups in India during the last decade. A typical adult spends most of their day around start-up products. If you are too lazy to cook, food is just a click away on Swiggy/Zomato. One can commute to their workplace using Ola. For booking hotel rooms to your next travel destination, choose from hundreds of options in OYO. Above all, paying for all the above services using PayTM! With a commitment to creating customized solutions, start-ups are easing the lives of people. What is most encouraging in all this is that all these companies are home-grown and thus, carving a niche for the nation globally.

In the present dispensation, only a handful of these companies have become successful and even fewer have generated profits, it is important for us to analyse the reasons for its, as well as their sustainability. Even the Government has realized the potential of this sector to India’s product market as well as job creation, given proper regulatory framework. Let us study these issues in detail.

Literature Review

Carl Dahlman and AnujaUtz [2] suggest that in the global knowledge economy of the twenty-first century, India’s development policy challenges will require it to use knowledge more effectively to raise the productivity of agriculture, industry, and services and reduce poverty. Start-ups can be seen as one of the outcomes in this direction.

Arora [3] traces the growth of the software industry in five emerging economies, including India. As per the study, India used the comparative advantage of a relatively low-cost, technically skilled (and English-speaking) workforce to develop strong export-oriented software industries. Moreover, Indian software firms grew by providing low-level software services to US firms, graduating over time to higher stages in the technology chain. Jain analyses the growth and prospects of Startup systems in India [4].

Prashantam [5] analyses how Startups in developing economies are addressing local problems through creative technologies and solutions. This is creating special challenges and opportunities for large global companies as well.

Baporikar [6] gives an overview of contemporary perspective on startups in India, enhancing understanding of startup ecosystems and recognizes the framework for social change taking shape due to Indian startups contribution to the national economy. The paper also attempts to understand the key success factors and provides commandments to further foster startups to optimize the social change. Kshetri [7] gives an in-depth study of the hindrances faced by Start-ups in India.

Funding Trends

Over 1000 tech start-ups were registered in 2017, taking the total to 5200 and making India the world’s third largest start-up ecosystem-according to a Nasscom-Zinnov Joint Report on the ‘Indian Start-up Ecosystem-Traversing the Maturity Cycle’. It is also employing close to 80,000 people [8].
As per the report, 40% of startups were in the Business to Business (B2B) segment. Fin-tech startups had a bonanza year in 2017, owing to demonetization in November 2016. With 360 companies, it witnessed at 31% year on year growth with over $200 million funding received in the first half of 2017, recording a growth of 135% since the comparable period in 2016. The healthcare technology vertical, another important focus area, saw a 28% annual growth, with an estimated base of 320 startups. The vertical also garnered a total funding of $160 million in the first half 2017, up by 129% since 2016.

The report also added that with over 60% startups, the Business to Consumer (B2C) technology startup segment focused on creating innovative business models and taking the vertical approach, securing close to 70% of the overall tech startup funding in the first half of 2017[9].

Table 1 below shows the number of Funding and Investment deals in the top sectors during the years 2015-17.

<table>
<thead>
<tr>
<th>Sector</th>
<th>2015</th>
<th>2016</th>
<th>2017</th>
</tr>
</thead>
<tbody>
<tr>
<td>Finance</td>
<td>300</td>
<td>250</td>
<td>300</td>
</tr>
<tr>
<td>Consumer</td>
<td>200</td>
<td>250</td>
<td>300</td>
</tr>
<tr>
<td>Healthcare</td>
<td>150</td>
<td>150</td>
<td>150</td>
</tr>
<tr>
<td>F&amp;B</td>
<td>100</td>
<td>100</td>
<td>100</td>
</tr>
<tr>
<td>EdTech</td>
<td>50</td>
<td>50</td>
<td>50</td>
</tr>
</tbody>
</table>

![Top Sectors- Number of Deals](Fig-1.png)

Multiple and easily accessible platform like Venture Capital/Private Equity, angel investors, incubators, financial institutes and even banks, are the driving force for the same[10]. What is further worth illustrating is the quantum of foreign investment in start-ups. The SoftBank Group of Japan has the largest list of ‘Unicorns’ (companies with a valuation of $1 billion) under its portfolio in India followed by Tiger Global (USA) and Tencent (China).

**Concentrated in the Metros**

Since technology has been the backbone of this boom, it is understandable that the start-up ecosystem is concentrated in the metros. In fact, 66% of Start-ups are located in three urban agglomerates- Bangalore, Delhi NCR and Mumbai, according to World Economic Forum [11].

With the markets nearly getting saturated in these cities, it is most likely that the next group of unicorns will emerge from Tier-2 and Tier-3 cities. Some encouraging trends from these cities are already emerging- Rajkot-based Balaji Wafers and Namkeen group, which started out as a home enterprise, is today worth Rs 4000 crore and holds a sizeable share in the Indian as well as the international snacks market.

Kolkata-based Wow! Momo is on a similar growth curve. The startup registered a turnover of Rs 50 crore in the 2015-16 fiscal, and is now planning to go international. Odisha-based dairy start-up Milk Mantra, which has more than 43,000 farmers from 800 villages as a part of its network has raised $10 million and became profitable in FY 2015-16[12].

Various factors have contributed to this rise in smaller towns, which will be discussed later. Moreover, these firms are rooted in the communities they belong to, and are therefore more attuned to the requirements and demands of their target audiences. With more than 60% of the country’s population currently residing in the semi-urban, tier-2/tier-3, and rural geographies, ventures operating out of smaller towns and cities have easier access to promising business opportunities and resources.

**Emergence of the Ecosystem**

Various factors have led to this emergence of Start-ups in India. First and foremost is the virtual elimination of ‘barriers to entry’. One can walk into a co-working space which provides all the amenities, without spending too many resources in creating the infrastructure. Information Technology (IT) has become a cheap commodity, and one can get reliable server space for a few thousand rupees per month. Moreover, it’s possible to get freelancers to build the required product, which means one can operate with a lean structure [13].
Secondly, there is enormous liquidity in the markets. As already mentioned, foreign funders (like SoftBank) find India to be lucrative investment opportunity. Government flagship initiatives like ‘Start Up India’ and ‘Digital India’ have eased finance from banks and other institutions. Even entrepreneurs like Ratan Tata, Nandan Nilekani, Sachin Bansal, Binny Bansal, Rakesh Jhunjhunwala, etc. are turning into investors. A host of others are becoming mentors for the next generation of entrepreneurs.

Thirdly, lots of accelerators and incubators have now sprung up, which are helping students to create a business, by teaching them how to craft business plans and to pitch to investors. The emergence of Tier-2/3 entrepreneurs can be attributed to this.

The Spectre of Profitability

<table>
<thead>
<tr>
<th>Company</th>
<th>Losses (2015-16)</th>
</tr>
</thead>
<tbody>
<tr>
<td>Flipkart</td>
<td>Rs.2,306 Cr</td>
</tr>
<tr>
<td>Snapdeal</td>
<td>Rs.3,516 Cr</td>
</tr>
<tr>
<td>PayTM</td>
<td>Rs.1,549 Cr</td>
</tr>
<tr>
<td>Ola</td>
<td>Rs.2,313.3 Cr</td>
</tr>
<tr>
<td>Zomato</td>
<td>Rs.492.3 Cr</td>
</tr>
<tr>
<td>Oyo</td>
<td>Rs.363.7 Cr</td>
</tr>
</tbody>
</table>

Table 2: Cumulative losses of Indian Unicorns (2015-16)

2017 saw $13.7 billion being invested into the Indian startup ecosystem. The value of investments is significantly higher this year compared to 2016 and 2015, when funding was at $4.06 billion and $8.4 billion respectively. Despite all the investments and massive valuations, it doesn’t imply profitability. In the drive to get a larger market share, all of them are burning huge cash. The continuous spree of losses is creating a shortage of funds within these organizations, putting in jeopardy their viability. Of the top 10 Unicorns, only two are currently profitable: Data analytics firm Mu Sigma has made annual profits for three years while InMobi, an advertising technology platform, posted profits in the fourth quarter of 2016. Biggies, including Flipkart, SnapDeal[14], PayTM, Zomato, Ola[15]and Oyo[16]-all incurred losses. Table 2 gives a summary of losses.

However, it is worth mentioning that the revenues of these companies are also rising, and are expected to rationalize their business models in due course.

More disturbing is the number of promising start-ups that have failed- Data from venture capital research firm Tracxn shows 277 shutdowns in 2017. Not surprisingly, ecommerce accounted for the largest number of shutdowns, followed by food-tech. Despite the fast growth in smartphone usage, monetization has proved hard in the consumer internet space. While the likes of Amazon and Flipkart can absorb losses with a long-term view, smaller players are forced to shut shop when the funding tap is closed [17].

All of this is making investors more cautious and are deploying capital with greater caution and focus on evaluating long-term sustainability of businesses. Thus, although the number of deals in 2017 was 820, it was less than 2016 and 2015 which saw 1,034 and 913 deals respectively.

CONCLUSION

Startup has been the flavor of the season from the past few years. But, taking money from VCs is not a startup. Startup is about being innovative, finding innovative solutions to existing problems or it means to launch an idea which has never seen before. They are made to handle innovation [18].

Over the past few years, India’s growth has been jobless-big companies are not generating as many jobs as required. Moreover, the economy is moving away from agriculture-based to knowledge-based. Hence, Start-Ups can fill this space by transforming the nation from one of job-seekers to job-creators by tapping ambitious innovative entrepreneurship. Moreover, Startup companies are the most dynamic economic organisations on the market, since they provide additional competitiveness to the economic system. This means that the economy stays healthy, vital and diligent.

Nirmala Sitharaman, MoS, Commerce and Industry, said “Entrepreneurship is no longer being condemned as jugaad” during the launch of the Startup India Action Plan on January 16, 2016, by PM Narendra Modi. In the past 18 months, the Indian Government has come up with a wide array of startup schemes and startup funds to encourage launch and growth of startups in the country. However, of the many initiatives, only a few such as Fund of Funds, Tax exemption, gain hype across the startup community [19]. Despite the above-noted positive trends, entrepreneurial activities are hindered by business unfriendly labor laws, adverse corporate bankruptcy regulations and the
lack of clear property rights [20]. Moreover, many Indian entrepreneurs still struggle with a culture that looks down on capitalism and is indifferent to hard work, improvement and innovations [21]. Other challenges include a big entrepreneurial financing gap [22] and the country’s poor R&D and innovation performance [23]. It is imperative that the Government be in full realization demographic dividend.

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