

6th annual edition

AVCJ Private Equity and Venture Capital Report

INDIA

2011

SAMPLE



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OVERVIEW

Macro gold, micro hurdles

As Indranil Pan, Chief Economist at Kotak Mahindra Bank, explained of India's strengths just as 2010 was coming to a close, "There is no doubt that India is one of the strongest [growth engines] in the global economy, and possibly just behind China. Obvious implications for this are that inflation is quite high. The last number reported on the WPI is about 8.5%," he said, later noting that the Reserve Bank of India and other regulators "are looking at driving the inflation down to a medium-term target of 6.5%."

"From the investor's perspective, it could still look to be on the attractive scale."

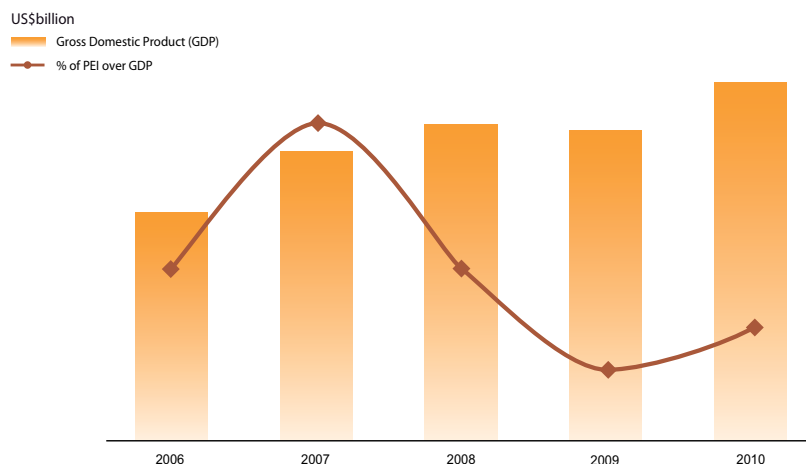


Other factors and... growth... domestic consumption, strong demand for domestic... services, banking, air traffic, freight and agricultural... concluding with a... on GDP. "Interest rates going upward... to slightly firmer, which could have a bit of a sobering... in terms of the GDP, also given because we're looking at a... growth year in 2011," Pan said. "Overall, from the current 8.4 to 8.5%... the Indian economy could actually slow down to around to 7.8-8%. But on a... scale in terms of where the globe is, I think that's still quite a healthy number, and from the investor's perspective, it could still look to be on the attractive scale."

CHALLENGES IN THE DETAILS

Unfortunately, with all of these positives as a backdrop, India has not reached its potential as a result of issues like corruption, the lack of critical infrastructure, sectors closed to foreign investment and regulations which vary from state to state. Punit Shah, Executive Director & Head of Financial Services & Private Equity Tax Practice at KPMG, adds that uncertain

FIG 1.1
INDIA - GROSS DOMESTIC PRODUCT VS. PRIVATE EQUITY INVESTMENT



*GDP data refers to fiscal year (April 1-March 31) and Private Equity Investment data refers to year-ended on December 31
Source: International Monetary Fund, AVCJ Research

FUNDRAISING

Funds (not) raised in a difficult market

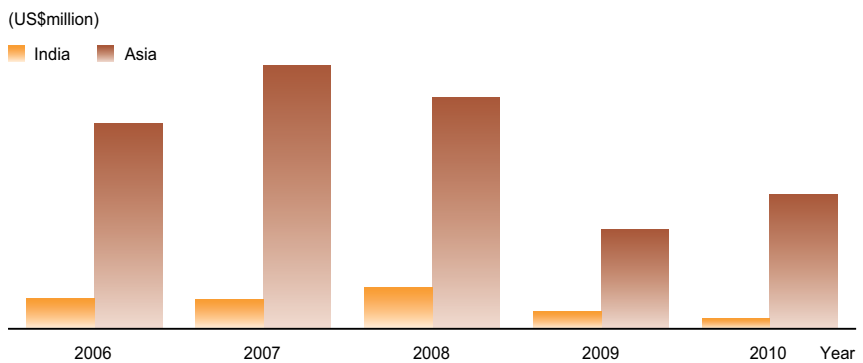
“The fundraising process has become more arduous, particularly in light of slowing returns.”

The returns that macro conditions in India would not yet materialized. Puneet Bhatia, Managing Director & Co-Head, T... in 2002-2003, before the India fundraising boom, the “10x re... it’s next to impossible to find and manage... raising an India-dedicated fund is more than... takes... a check signed, the number of meetings, the num... is quite simply more arduous.



...201... was raised in Asia-Pacific. Of that, just \$2.4 billion went to... 38.5% drop in fundraising and a 22% drop in the number of funds who... only saw commitments.

FIG 2.1 INDIA - TOTAL PRIVATE EQUITY FUNDS RAISED (US\$ MILLION)



*Excluding real estate & global funds
Source: International Monetary Fund, AVCJ Research

TOTAL PRIVATE EQUITY FUNDS RAISED (US\$ MILLION)

	2006	2007	2008	2009	2010	% Change 2009-2010
India	\$X,XXX	\$X,XXX	\$X,XXX	\$X,XXX	\$X,XXX	-XX.X%
Asia	\$XX,XXX	\$XX,XXX	\$XX,XXX	\$XX,XXX	\$XX,XXX	XX.X%
% India over Asia	XX.X%	XX.X%	XX.X%	XX.X%	X.X%	-X.X%

*Excluding real estate & global funds
Source: AVCJ Research

INVESTMENTS

Rising valuations thwart investments

“They will probably get 2x, which is not necessarily anything to write home about.”

Investments are problematic for one reason: valuations. Tan, Managing Director of Squadron Capital said bluntly, “India has been the most expensive and remains the most expensive in the current cycle... If you invest in an average portfolio, profit growth is 15-20%; if you compound that over five years, a median portfolio, they will probably get only 2x, which is not necessarily anything to write home about.”

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Still, exits (to be discussed later in this report), it was also a record for the deployment of capital. \$7.7 billion in capital was deployed in the first half of the year, well outperforming the five-year low in 2009 of \$1.1 billion. The number of deals transacted only rose by 16.9%, which begs the question: are firms still paying too much?

STAGE BY STAGE, A GROWTH STORY

“GPs are moving into the growth space, learning how to influence entrepreneurs without a controlling stake.”

The numbers would seem at the outset to indicate that larger deals and potentially more buyouts are being done. However, the opposite is true. Buyout is up just 38.5% while growth is up 133% and venture is jump 176%. A total of \$5.4 billion was deployed in growth capital, while buyouts were worth only \$735 million. A stark contrast for a country that private equity had hoped would be a bastion for the Asian buyout story. With growth comes a completely different skill set, part of which has to do with patience and persuasion, as opposed to control and a forcing of the hand.

Mark Silgado, Senior Managing Partner, IL&FS said, “Private equity in India needs to be more patient. [Minority investments] may be small but they are valuable. Quick deals where you make money fast may not be high value, but if you wait for factors that take time, you may see higher valuations.”