Grant Thornton

An instinct for growth™

The Fourth Wheel 2017

Private Equity in the Corporate Landscape

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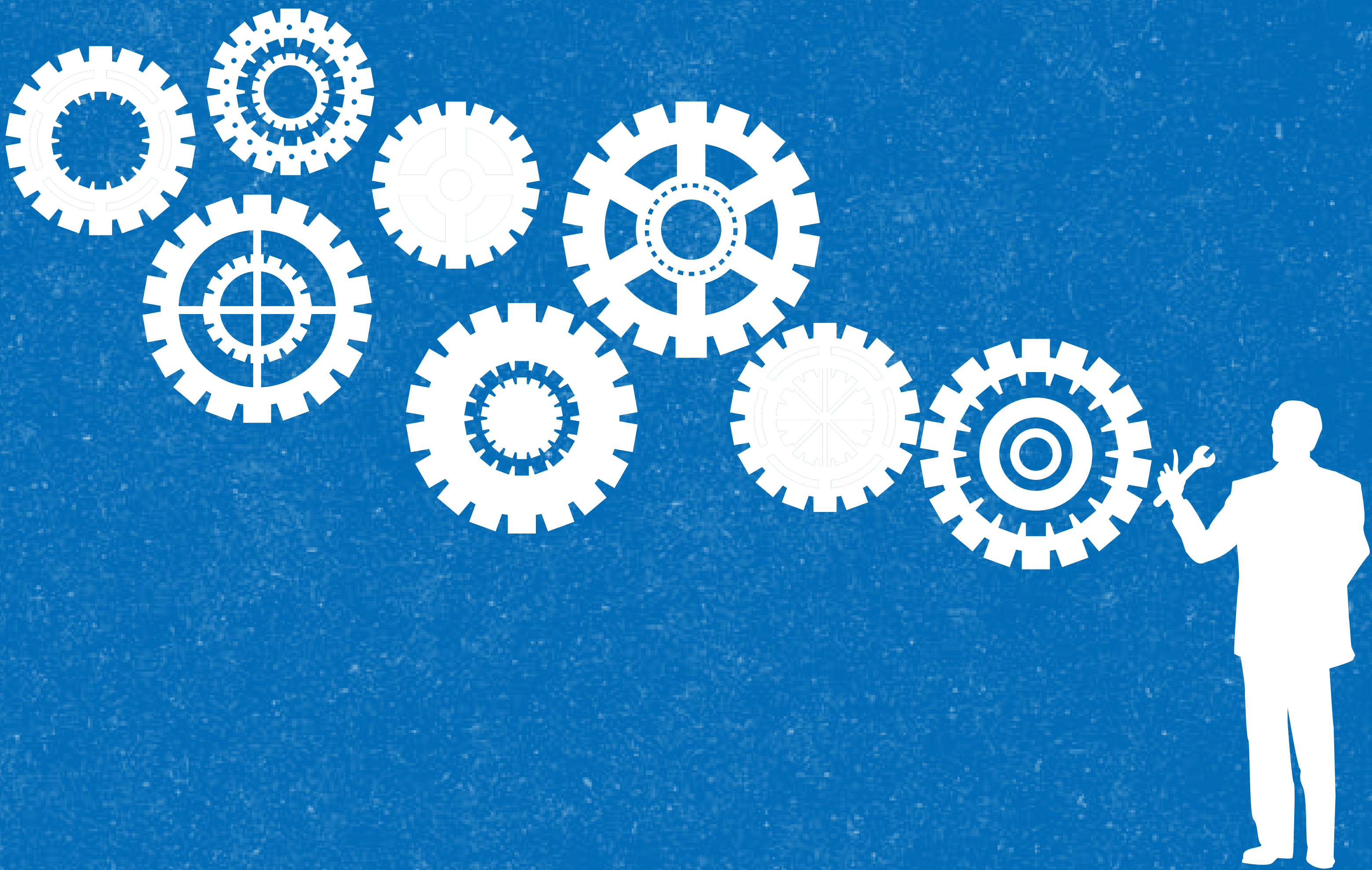


Message from IVCA

Gopal Srinivasan
Chairman
The Indian Private Equity and Venture Capital Association

Private equity, venture capital and angel capital are playing a vital role in India's economic development. Grant Thornton is taking the lead in this area by publishing this important report. The data and insights contained in this report will help spur the greater flow of private equity and venture capital in India.

IVCA would like to stress a few points.

Regulatory authorities like SEBI have helped lay the foundations of "Alternative Investment Funds" in India. SEBI's leadership in appointing and convening the Alternative Investment Policy Advisory Committee (AIPAC) is a major catalyst.

AIPAC has been at the forefront of making sound policy recommendations for the development of AIFs. The recommendations hace been very well received by stakeholders namely the Government, fund managers and portfolio companies.

It is a testament to these efforts that more new fund managers are entering India given the wide range of investment opportunities. Softbank and Lonestar are good examples. New domestic funds are being formed such as the successful fund raising by first time manager, Stellaris Capital. The Government's Rs. 10,000 crore fund-of-funds is a highly commendable initiative.

Finally, I would like to thank everyone at Grant Thornton and IVCA who worked tirelessly to produce and launch this invaluable report.

Foreword by Grant Thornton

Harish HV
Partner
Grant Thornton India LLP

We are pleased to present the next edition of the Fourth Wheel which we launched in 2011 that discusses the recent developments and trends in the private equity (PE) deal landscape. Over the years, PE investors have nourished the breed of entrepreneurs and helped businesses generate significant value. As a result, the Fourth Wheel (Private Equity in the Indian corporate landscape) has aligned with the three other Wheels (PSU, MNC and the Indian Private Sector) and has become an integral part of corporate India and I would argue its biggest wealth creator and has provided the capital needed for India Inc.'s new entrepreneurs to grow and scale up.

According to the data available with Grant Thornton, Private Equity and Venture Capital investors invested US$ 14 bn in 971 deals in 2016. The sectors in focus were startup, telecom, banking and financial services, real estate, IT/ITeS and manufacturing. These sectors contributed around 78 percent of the overall deal value in 2016. The transaction values and volume were lower than in 2015, wherein US$ 16 bn was invested in 1045 deals. This was partly due to the absence of some of the mega deals, particularly in e-commerce in 2015, which did not recur in 2016.

PE investors continued to show faith in startups where volumes remained more or less at par with the last year. However, increasing caution among PE investors prevented them from betting big this year. Unlike 2015 which witnessed more than 40 big-ticket investments (deals valuing US$ 100 mn or more), 2016 saw only 28 such deals. Investment values in startups declined by more than 50 percent this year, signifying rationalisation of investments and startup valuations. However, the Government's push on digitisation and initiatives under the Startup India plan are likely to lead to a rebound in this segment.

2016 also witnessed significant activity in exits especially through IPOs, which augurs well for the investor community. The IPO market showed phenomenal potential in 2016 by raising nearly US$ 4 bn across 25 issues. The coming year is also expected to show robust growth in primary markets, with SEBI approving 13 more IPOs, which are slated to hit the markets in 2017.

2017 could be the year of reckoning for the country where implementation of structural policies and reforms such as the GST and the recently announced measures in the Union Budget 2017 by way of massive push to the infrastructure sector, plans to integrate the transport architecture, renewed focus on affordable housing and a boost for ease of doing business will drive growth. Also, expected improvements in the banking sector, pick up in rural demand, post the effect of demonetisation, a robust primary market and improving capacity utilisations across industries are likely to drive domestic economic activity. Amidst global uncertainties arising due to Brexit, protectionist policies proposed by the US and a slowing Chinese economy, India continues to be the bright spot. India is likely to drive resilient growth in deal activity in 2017.

The Fourth Wheel 2017, now in its fifth edition is an effort by Grant Thornton in India in association with IVCA to highlight the PE activity in India. The study also provides an insight into the vibrant and dynamic entrepreneurship ecosystem in India. The data presented in the study is based on Grant Thornton's Dealtracker Report and views from across leading PE/VC fund houses. This makes the report abundantly rich with datasets and analysis.

I am hopeful that we see robust deal activity resulting in a healthier investment climate in coming months. I am thankful to all the people involved in preparing the report and trust you will find the report insightful. We thank you all for your continued support and look forward to your valuable inputs as we launch this year's publication.

Editorial

Prashant Mehra
Partner
Grant Thornton India LLP

We welcome you to this year's edition of The Fourth Wheel!

2016 reported a 43.5 percent y-o-y jump in transactions amounting to US$ 62.5 bn. The jump was primarily led by the resurgence of big-ticket M&A deals resulting in 2016 clocking the highest M&A deal value in the last five years.

In contrast, PE activity declined this year and registered its first decline in the last four years over increasing caution in investor sentiments. PE transaction values reduced by 12 percent primarily due to the absence of large ticket deals resulting in a marginal decline in the average deal size. Moreover, large part of the activity was concentrated on early stage companies where average deal sizes are relatively small. 2016 saw an uptick in follow-on funding rounds as companies focused on expansion and increasing scalability while the year fell short of recording growth capital funding.

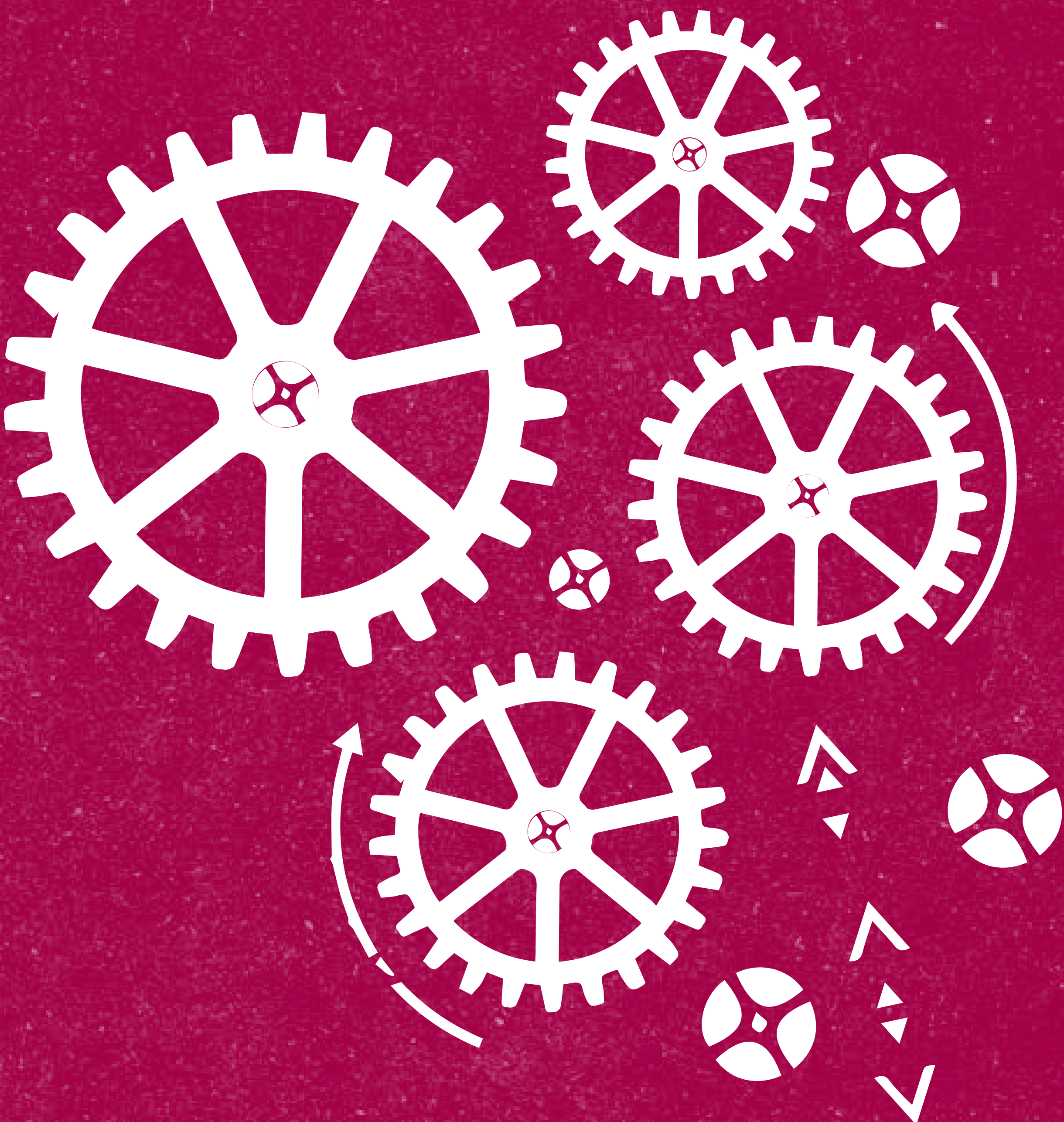
In terms of sector spread, startups continued to dominate both in terms of deal values and deal volumes contributing around US$ 2.5 bn and 70 percent to transaction volumes. Other major deal value contributors were core sectors such as telecom, BFSI and real estate capturing around 40 percent of values. The startup ecosystem in India witnessed rationalisation with funding getting tougher and investor's focus shifting to business fundamentals and scalability with realistic and justified valuations. Investors' ability to mentor and nurture startups will be the key to finding the right early-stage investment opportunities.

Indian assets are expected to remain in focus as inbound and domestic M&A accelerate on the back of a pickup in alternate buy out financing by PEs i.e. PE financed acquisitions. This may also result in the long-awaited big ticket transactions in the PE space. Government's actions on key policy issues and reforms such as GST, insolvency and bankruptcy code, rationalisation of tax regime, unblocking stalled projects, etc. should help improve the 'ease of doing business' that may further accelerate the transaction activity in India. With macro-economic scenario continuing to be positive, it is expected that PE investments will shift focus to the consumer and industrial sector to fund both organic growth and consolidation in the domestic industry.

The year 2016 witnessed a number of key reforms such as the roadmap to implementation of GST, demonetisation, income hike due to the seventh pay commission and one rank one pension (OROP). With more economic reforms on the anvil per the announcements in the Union Budget 2017, we can expect 2017 to be an action-packed year.

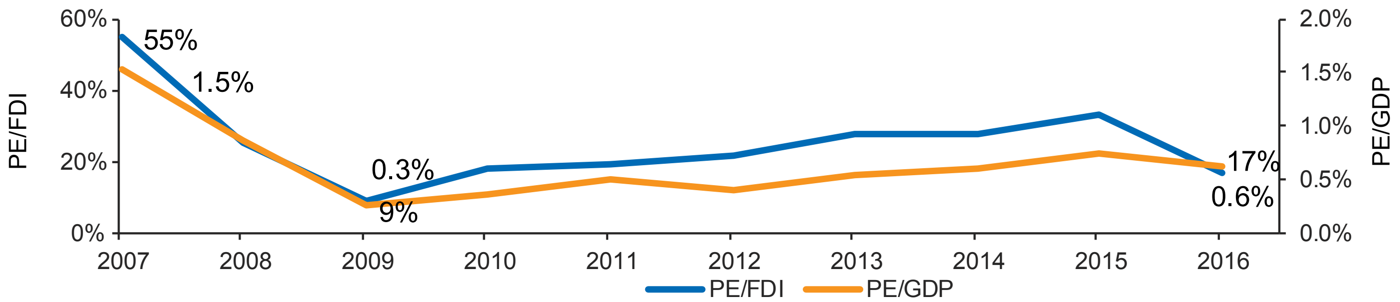
Having said that, challenges facing the banking sector, subdued private investments, rising crude oil prices and the uncertainty in the global markets are likely to be key concerns facing India this year. However, growth in domestic consumption (after the likely set-back post demonetisation), a strong IPO market (with nearly US$ 4 bn raised this year and over a dozen IPOs expected in 2017), infrastructure spending, banking sector reforms and a supportive policy environment are expected to keep India's growth resilient in 2017. Moreover, the recent budget announcements around conversion of preference shares (compulsory or optionally) to equity shares, proposal to abolish the FIPB, partial roll-back of long term capital gains, proposal to restrict the offset of foreign tax credits against MAT and AMT and concessional withholding tax benefit of 5 percent on ECB and Masala Bonds, should further encourage greater PE activity.

PE environment



2(a) PE Contribution to the Indian economy

Trend in PE Investments to Gross Domestic Product (GDP) and Foreign Direct Investments (FDI)



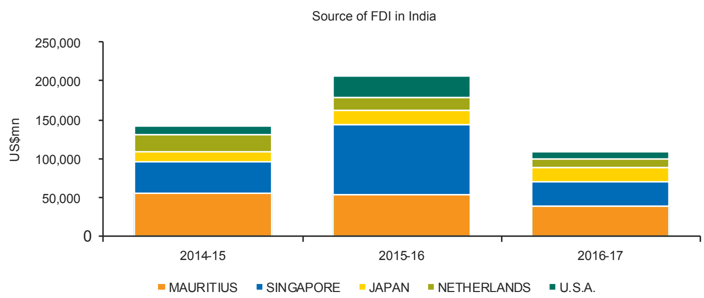
Source: International Monetary Fund, Foreign Investment Promotion Board

The Indian economy has been on an uptrend since the global economic downturn of 2007-08, with GDP picking up pace at the back of the various economic and political factors as well as structural reforms promoted by the Government over the last few years. This has led to a positive investment sentiment that has helped attract higher PE investments over the last seven years. This is evident from the increase in the PE to GDP ratio from a low of 0.3 percent in 2009 to 0.6 percent in 2016, suggesting the increasing contribution that the PE industry has made to the growth of the Indian economy. However, when compared to the PE to GDP ratio of developed markets, which is generally understood to be greater than a percent, the ratio of that of India is currently lower. Also, governed by India's experience of a high PE to GDP level of 1.5 percent in 2007, indicates that there is still scope for PE investments to scale up in India.

Similarly, the PE fund inflow as a share of FDI has also been consistently increasing post 2008. The ratio was 17 percent in 2016 compared to 9 percent in 2009. India witnessed a high of 55 percent in 2007 indicating a potential for higher contribution going forward. The PE/FDI ratio showed a decline in 2016 due to lower PE investments and higher FDI inflows during the first six months of 2016 as compared to 2015.

Source of FDI in India

Singapore emerged as the top source of FDI in India in 2015-16, replacing Mauritius which was the top contributor in 2014-15. However, in 2016-17, Mauritius has regained the top spot during the first six months of 2016-17. Further, Mauritius, Singapore, Japan and Netherlands have been the leading contributors to FDI over the years. This was primarily because of the favourable tax treaties of these countries with India. Also, the primary reason for the higher FDI inflows from Mauritius and Singapore in 2016-17 could be attributed to the proposed change in India-Mauritius and India-Singapore tax treaties that offer grandfathering provision for capital gains tax benefits for investments made until 31 March 2017.

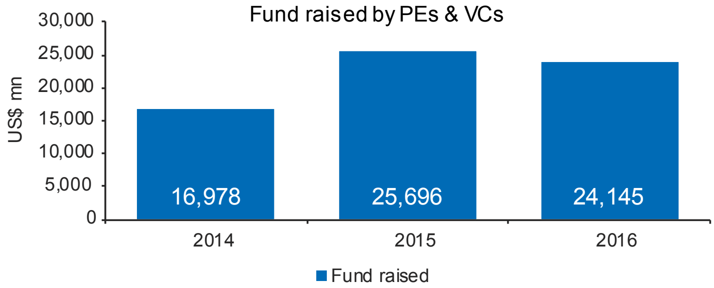


Source: Foreign Investment Promotion Board
Note: 2016-17 represents data for the period April to September only

2(b) Fund raised by PEs & VCs

Fund raising activity in the PE and VC space witnessed a decline of 6 percent in 2016. PEs and VCs raised closed to US$ 24.1 bn in 2016 as compared to US$ 25.7 bn in 2015. Majority of the funds raised in 2016 (US$ 14 bn) were raised by Brookfield Asset Management Inc., an infrastructure focused fund. Further, out of the total funds raised in 2016, approximately 20 percent were raised by India focused funds. On a cumulative basis, PE and VC firms have raised close to US$ 67 bn from 2014 to 2016. However, only about US$ 42 bn was deployed by them over the three year period, suggesting high levels of cash reserves (dry powder) with the PE/VC investors. This could also be one of the reasons for the marginal decline in fund raising activity in 2016 as fund houses are yet to invest a portion of the funds raised in previous years.

In 2015, technology startup focused PE/VC firms predominantly raised funds. These funds include YourNest Angel Fund, Global venture capital, Bessemer Venture Partners (BVP) - BVP IX, Trifecta Capital, SAIF Partners, Astarc Ventures, YouWeCan Ventures, Accel India IV-Accel Partners, Sequoia Capital, India Realty Excellence Fund II (IREF II)- MORE, Zodius Capital II, Edelweiss Financial Services Ltd- Special Opportunities Fund II (ESOF II) and others.

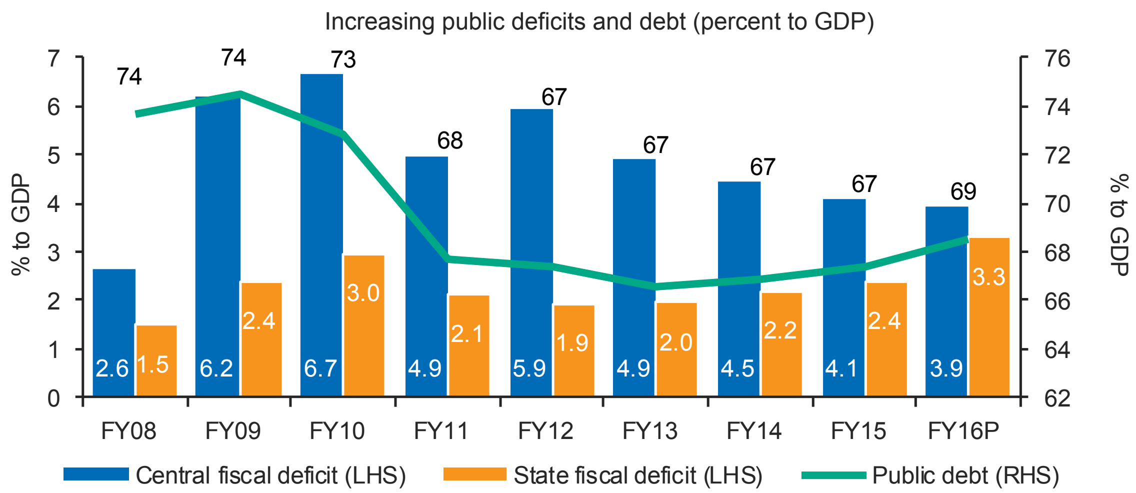


However, in 2016, majority of the funds raised were towards the infrastructure space. PEs also raised funds with a focus on sectors such as power, real estate, technology and startups. These funds were raised by ICICI venture, HDFC Limited, Kotak Realty Fund, Norwest Venture Partners, Accel Partners, Rocket Internet and others.

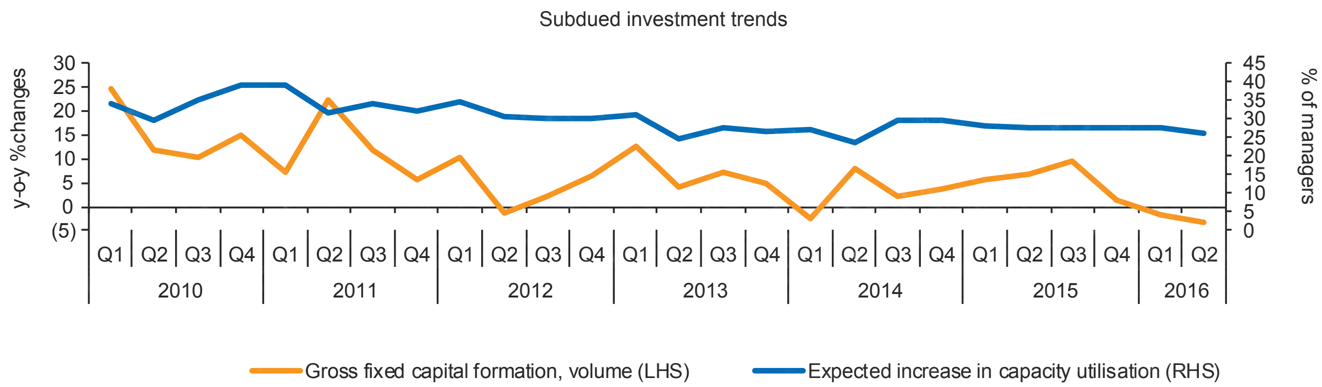
Further, over the past few years, corporates and multinational companies have been setting up funds to invest in smaller startups. Also, as a continuing trend in 2016, marquee entrepreneurs too are continuing to make investments in their personal capacity. Looking at the present scenario, there appears to be adequate funds available to be deployed; however, the challenge to identify attractive investment opportunities still remains.

2(c) Economic outlook

The IMF predicted a 7.6 percent GDP growth (in Oct-16) for FY17, making India the fastest growing economy in the world. However, the impact on GDP due to the demonetisation drive will need to be seen in coming months. India's growth story in 2017 will be driven by improvement in the investment climate, consumption growth and implementation of structural reforms.



Source: 1. Reserve Bank of India and Controller General of Accounts.
Notes: 1. Data for the fiscal year 2015-16 are provisional.



Notes: 1. percentage of managers interviewed expecting an increase in capacity utilisation.
Source: 1. Central Statistical Office 2. Reserve Bank of India

Signs of export recovery (percent year-on-year change)

Source: 1. Central Statistical Office. 2. Reserve Bank of India.

The year 2016 has been eventful for the economy with the last quarter seeing a lot of action with demonetisation, the Goods and Services Tax bill and the US presidential elections.

One of the most defining themes in the country, towards the end of the year, was demonetisation. The jury is still out on whether this move will have the envisaged impact on curbing black money and digitisation of the un-banked and informal economy. Transactional impact due to the cash deficit in the system is likely to have a negative impact on the economy in the short-term.

However, in the medium to long run, this move is expected to decrease borrowing costs, reduce inflation, improve tax collections and increase digitisation of the system.

While the global economic outlook appears uncertain after the Brexit and the US presidential elections, oil prices have been showing tendencies of a rise after OPEC and several non-OPEC countries announced production cuts. In this scenario, India, which till recently enjoyed the benefits of subdued oil prices, will face pressure on its import bill. Exporting companies, on the other hand, are likely to face challenges with reduced global demand for goods and services in the face of rising uncertainty in the global markets.

The banking sector, with gross non-performing assets estimated at Rs 6 tn as of June 2016, is reeling under bad loans and inadequate provisioning in the past. The sector is expected to continue to face challenges on account of weakness in the corporate sector performances, thereby increasing provisions and stressed assets. With nearly Rs 3.4 tn required for capital adequacy till FY19, capital raising challenges facing the sector, are likely to persist.

The investment climate in the country was impacted during the year due to weakness in global demand, overcapacity across sectors, higher leverage among corporates and high public debt levels. However, improvement in this regard is expected when sentiment relating to issues troubling private investment and the banking sector are resolved. Critical drivers of growth in 2017 will be domestic consumption growth and implementation of structural reforms such as the demonetisation, GST and seventh pay commission/one rank one pension among other economic reforms.

India outlook for 2017

The year 2016 has witnessed a number of key reforms during the year such as the GST, demonetisation, income hike due to the seventh pay commission and one rank one pension (OROP). With more economic reforms announced in the Union Budget 2017, we can expect 2017 to be another action-packed year. Having said that, challenges facing the banking sector, subdued private investments, rising crude oil prices and the uncertainty in the global markets are likely to be the key concerns facing India this year. However, growth in domestic consumption (after the likely set-back post demonetisation), a strong IPO market (with nearly US$ 4 bn raised this year and over a dozen IPOs expected in 2017), infrastructure spending, restructuring in banks and a supportive policy environment are expected to keep the country's GDP resilient in 2017.

Notable potential deals likely to be executed in 2017

CPPIB to invest over US$ 2 bn in commercial real estate space

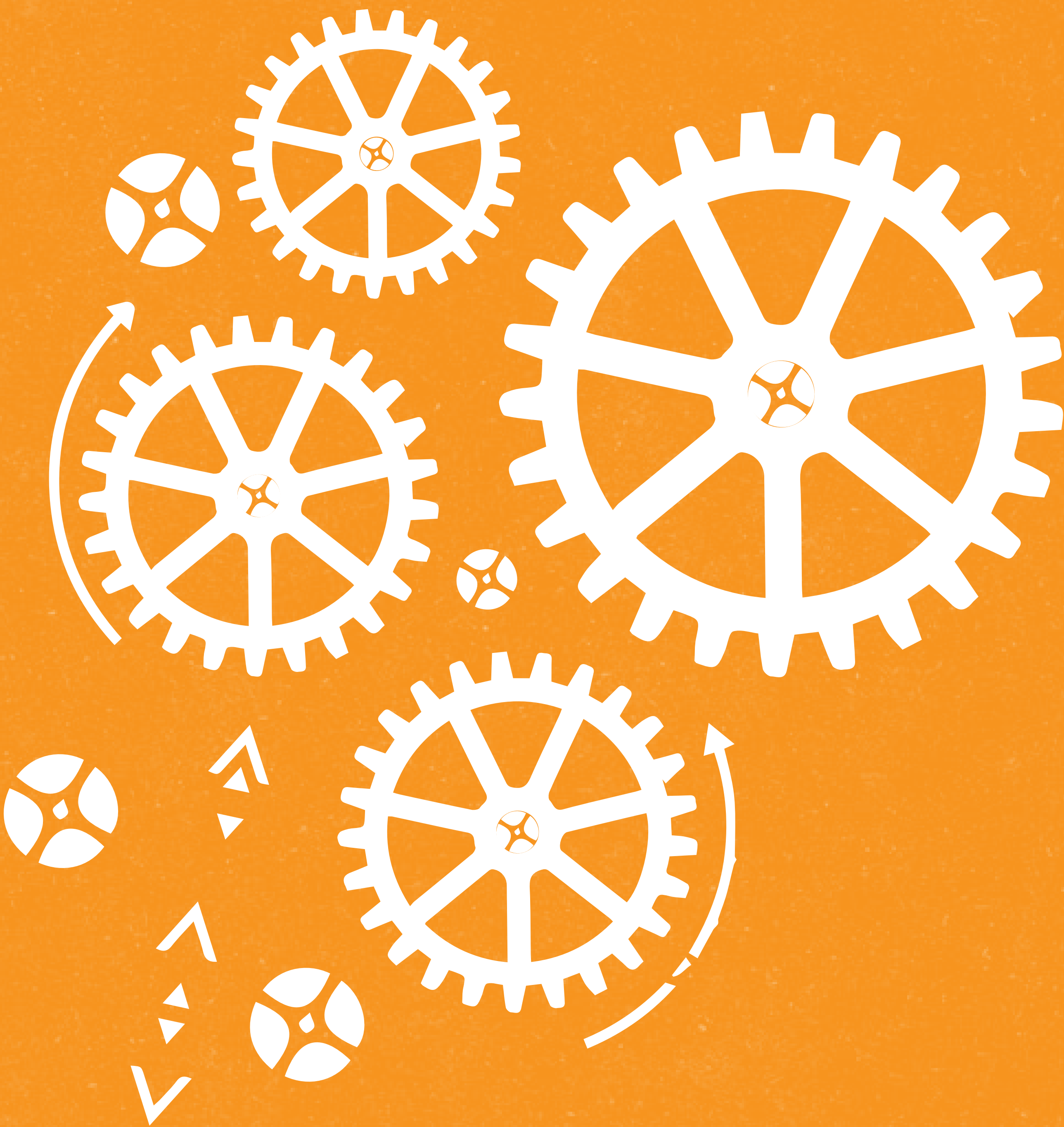
Canada Pension Plan Investment Board (CPPIB) is leading talks to acquire PE firm Everstone Group's industrial and logistics real estate development platform, IndoSpace, as a part of private real estate investment trust (REIT). Latest estimates of this entire transaction peg the value to be more than US$ 2 bn (Rs 15,000 crore). Reports indicate that in the first phase of the deal, CPPIB will acquire nearly ready development space of approximately 10 mn sq ft for around Rs 4,000 crore.

IndoSpace, a joint venture between Everstone Group and US-based Realterm, is developing another 30 mn sq ft across the country which will be developed and added to this portfolio and the payouts will be linked to that. According to reports, the term sheets have been signed and the deal is expected to be signed this year.

Paytm parent in talks to raise funds at US$ 5 bn valuation

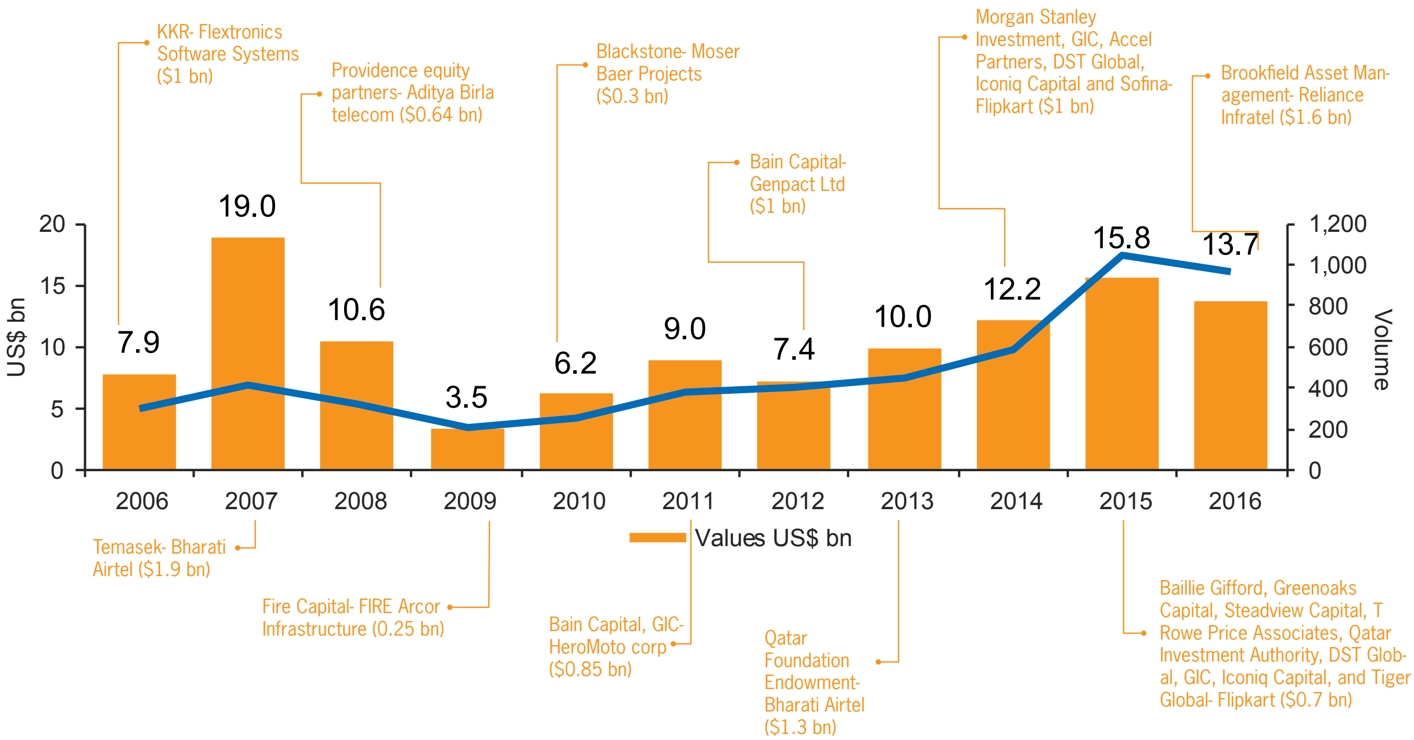
The company is in discussions with MediaTek, Singapore's Temasek, Goldman Sachs and others to raise US$ 350 mn; this deal will value Paytm at about US$ 5 bn, more than double its last reported valuation of around US$ 2 bn in June. Reports published in Aug-16 indicated that existing investors which include Chinese Internet giant Alibaba and its payments affiliate Alipay besides venture capital firm SAIF Partners, will also participate. The funds are expected to be deployed across all of Paytm's businesses — digital payments, online marketplace and the payments bank. If the transaction takes place, it will be the largest funding in India's broader technology and internet space this year.

PE deal scenario



3(a) Deal formations

I. Key PE deals in the last decade



II. PE quarterly trend chart since 2012

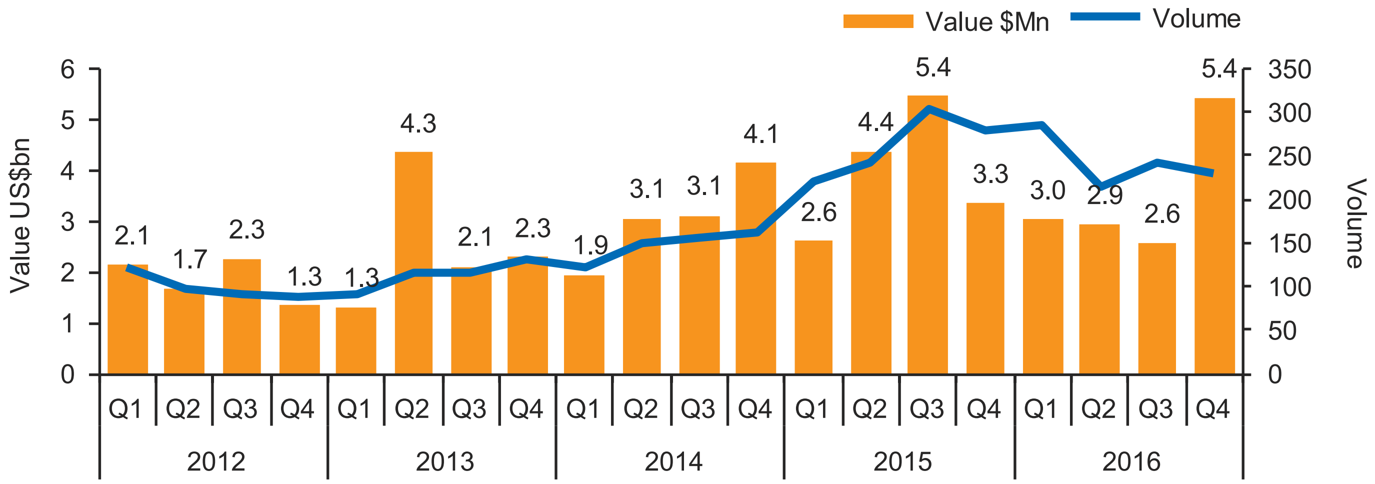
399 Deals
US$ 7.4 bn

452 Deals
US$ 10 bn

589 Deals
US$ 12.2 bn

1045 Deals
US$ 15.8 bn

971 Deals
US$ 13.9 bn



Top sector by value
IT & ITeS (18 percent)

Top sector by volume
IT & ITeS (16 percent)

Top sector by value
Pharma, Healthcare & Biotech (14 percent)

Top sector by volume
Startup (18 percent)

Top sector by value
E-commerce (19 percent)

Top sector by volume
Startup (37 percent)

Top sector by value
Startup(32 percent)

Top sector by volume
Startup(65 percent)

Top sector by value
Startup(18 percent)

Top sector by volume
Startup(69 percent)

III. Top deals

Top ten deals in 2016 accounted for

37 percent of total PE deal values

Acquirer	Target	Sector	US$ mn
Brookfield Asset Management	Reliance Infratel Ltd	Telecom	1,600
Brookfield Asset Management	Hiranandani Group-offices and retail space in Powai	Real Estate	1,000
Blackstone Group Lp	Mphasis Ltd	IT & ITeS	816
Fairfax India Holdings Corporation	Sanmar Chemicals Group	Manufacturing	300
Tamasek Holdings and KKR & Co	SBI Life Insurance Company Ltd	Banking & Financial Services	266
Naspers Group	Ibibo Group Private Limited	E-commerce	250
GIC and Abu Dhabi Ivestment Authority	Greenko Energy Holdings	Energy & Natural Resources	230
TPG, Morgan Stanley Private Equity Asia, Havells India, and Vallabh Bhansali and others	Janalakshmi Financial Services Pvt Ltd	Banking & Financial Services	210
Clouse SA, Ontario Teachers' Pension Plan, Iron Pillar and other investors	Jasper Infotech Pvt Ltd-Snapdeal.com	E-commerce	200
Tencent Holdings, Foxconn Technology Group, Tiger Global, Bharti Enterprises and Softbank Holdings Pte. Ltd.	Hike Ltd	Startup	175

This deal alone contributed to 11 percent of total PE deal values and 78 percent of total telecom sector.

According to Industry sources, this is one of the largest commercial real estate deals executed in recent years.

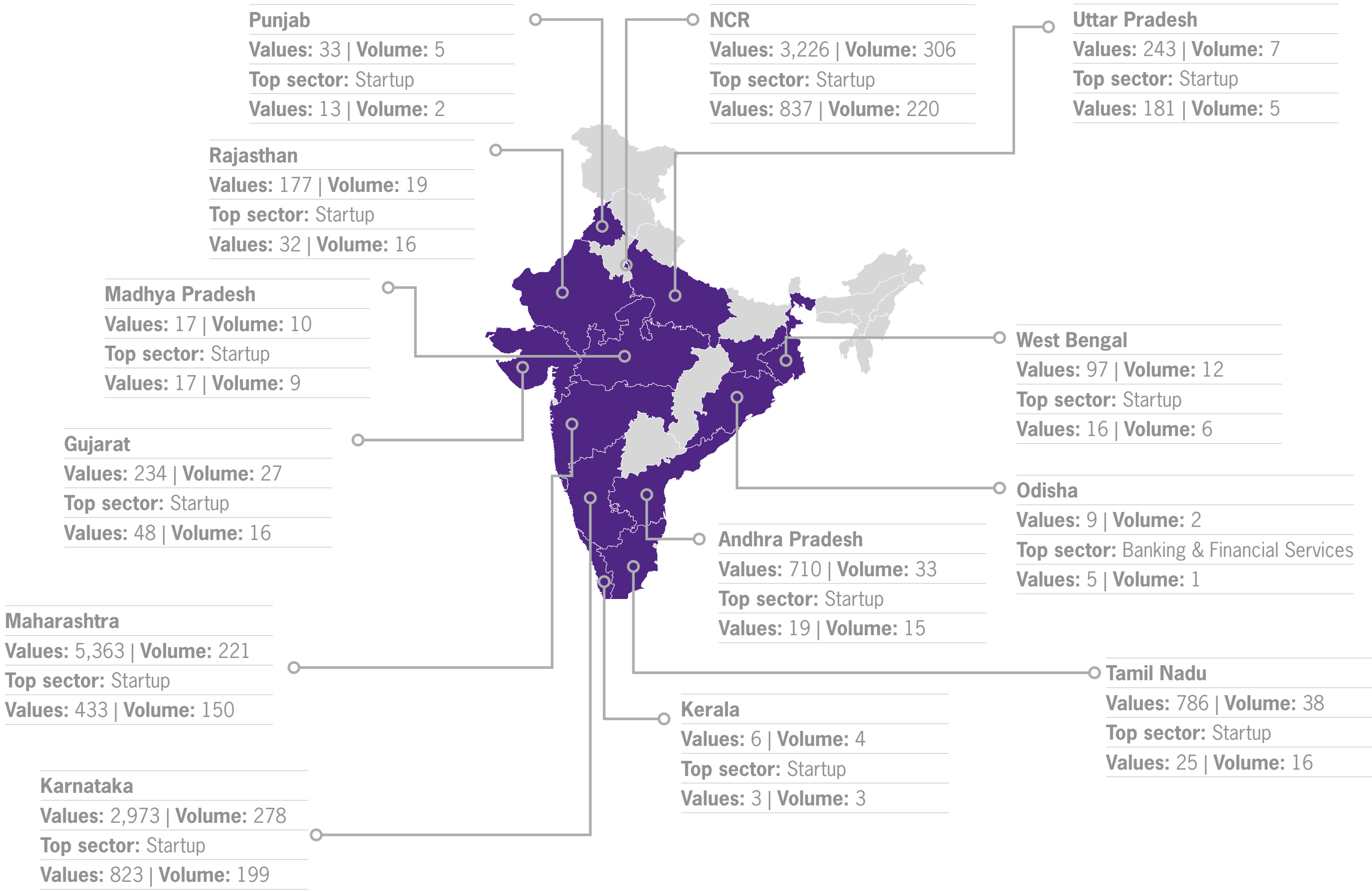
This is the highest investment made in the Insurance sub sector of Banking & Financial services in 2016.

This funding makes Snapdeal second highest valued start up after Flipkart.

The year witnessed Hike Ltd raise its Series D funding of US$ 175 mn and garner a bn dollar valuation adding to India's home-grown unicorns.

PE Investments in 2016 – statewise

NCR, Karnataka and Maharashtra received significant PE investment interest with nearly **83 percent** of total investments in 2016. The startup sector dominated investment volumes across 15 states.



Values are in US$ mn

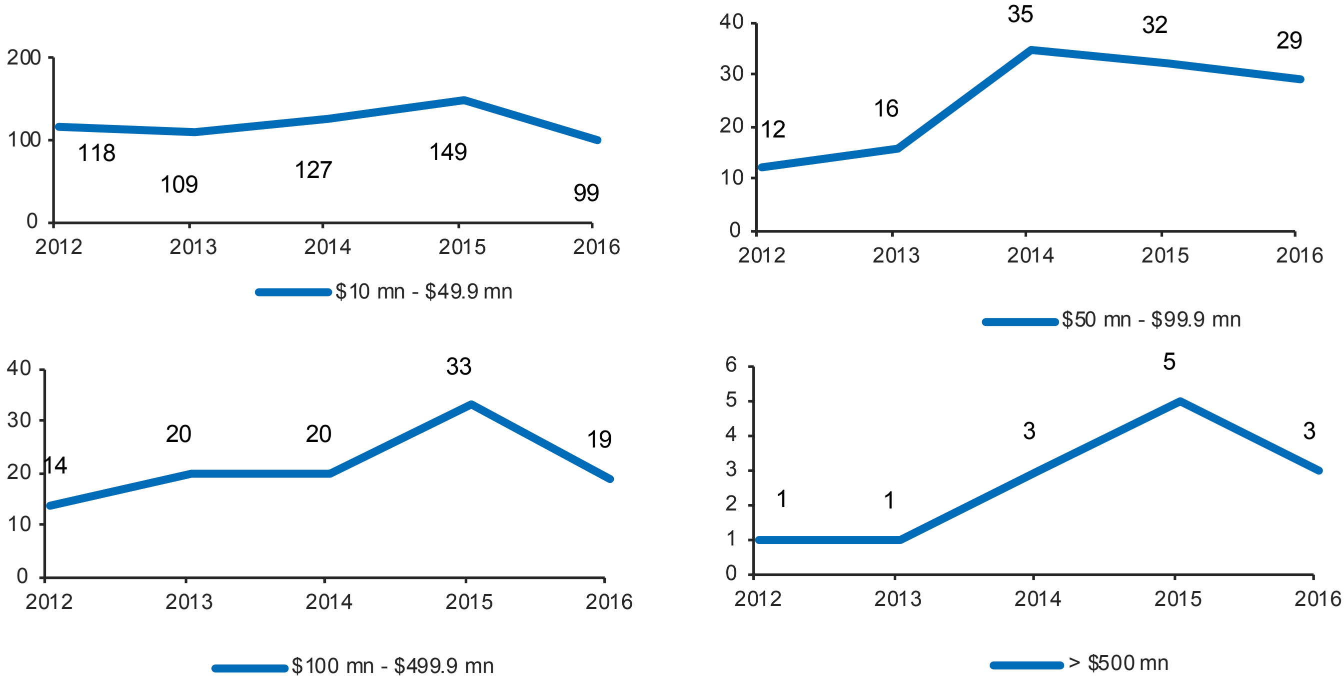
IV. How are PE firms investing (average deal size)

PE investments in 2016 saw decreased big ticket deals valued over US$ 500 mn each, a decline from 5 deals in 2015 to 3 deals in 2016. However, the levels are yet to match the big ticket investment levels in 2007.

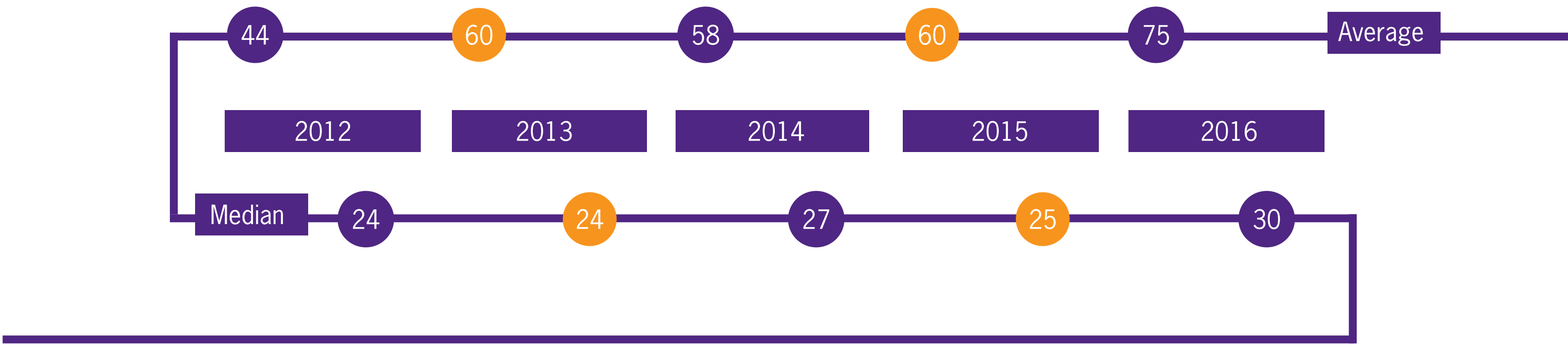
2016 attracted 150 investments valued at US$ 10 mn and above, a decline of 32 percent from the previous year, across sectors such as BSFI, startups, real estate, manufacturing, pharma, and retail along with upcoming e-commerce companies.

The median deal size of PE investments rose from US$ 24 mn in 2012 to US$ 30 mn in 2016, showing continued PE investors interest in India. One of the reasons for the increase in deal size is due to higher number of majority stake or control transactions in the year 2016. Given the investor sentiment, it is likely that there will be more big ticket deals in the next couple of years.

PE investments by deal size



PE investments by deal size (in US$ mn)



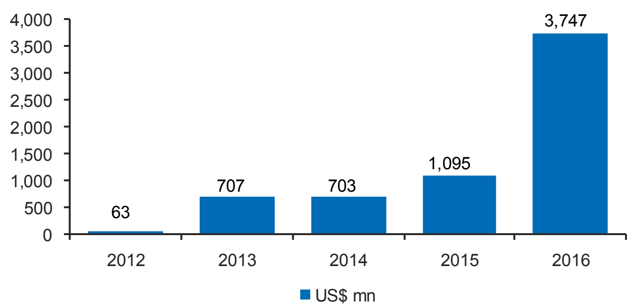
V. PE trends in relation to buyouts

Funds who have experience of investing in India for more than 15 years, are now seeking to attain majority stake/control over the investee companies. This arrangement gives them greater control over the investee companies, thereby, allowing smoother exits.

Buyout/control deals, which are common in the US or European countries, are gaining momentum in India in light of the above. The number and the value of buyout deals has increased significantly from 2012 to 2013-2016 with the value of buyouts clocking almost 4 times in 2016 when compared to 2015.

The top majority/buyout deals (value above US$ 100 mn), over the last four years are summarised in the table below. Sectors that saw the most buyouts include telecom, real estate, IT and ITeS, and banking and financial services.

Trend in large PE buyouts



Top buyout/control deals

Year	Investor	Investee	Sector	percent Stake (percent)	Investment Value in US$ mn
2016	Brookfield Asset Management	Reliance Infratel Ltd	Telecom	51	1,600
2016	Brookfield Asset Management	Hiranandani Group- offices and retail space in Powai	Real Estate	100	1,000
2016	Blackstone Group Lp	Mphasis Ltd	IT & ITES	60	816
2015	TA Associates and India Value Fund Advisors	Atria Convergence Technologies	Telecom	95	500
2015	JP Morgan Asset Management	Canaan Partners-portfolio in India	E Commerce	100	200
2015	KKR and Co. Lp	Avendus Group	Banking & Financial Services	60	105
2014	Capital Square Partners, CX Partners	Aditya Birla Minacs Worldwide	IT & ITES	100	260
2014	Xander Group	7.8 lakh sq.ft. commercial space - Infinity Tech Park	Real Estate	100	108
2013	Partners Group	CSS Corp	IT & ITES	80	270
2013	Blackstone	Agile Electric Sub Assembly Pvt Ltd- Igarashi Motors India Limited	Automotive	98	110

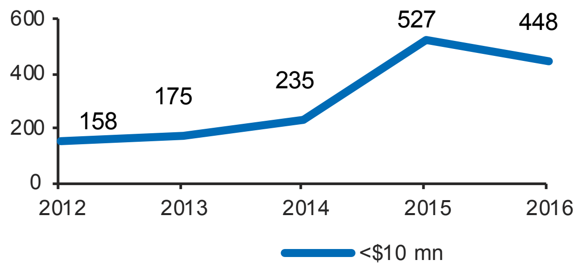
Note: For the purpose of analysis on buyouts we have considered the following criteria: All the transactions resulting in controlling stake of more than 50percent and are publicly disclosed are included.

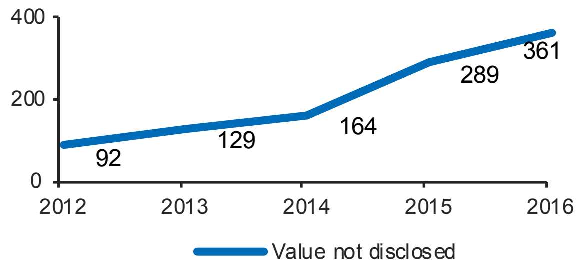
VI. VC investments by deal size

VC highlights

2016 saw a large number of investments in startups varying from angel, seed, growth, bridge, crowd, pre series A, series A and series B funding rounds ranging between a few thousand US$ to US$10 mn. 2016 investments were double the number of investments in 2014, clearly indicating an increased activity in the venture capital space in India.

While the number of deals increased from 399 in 2014 to 809 in 2016, the median deal size of VC deals decreased from US$ 2 mn to US$ 1 mn at the back of increased investment volumes.



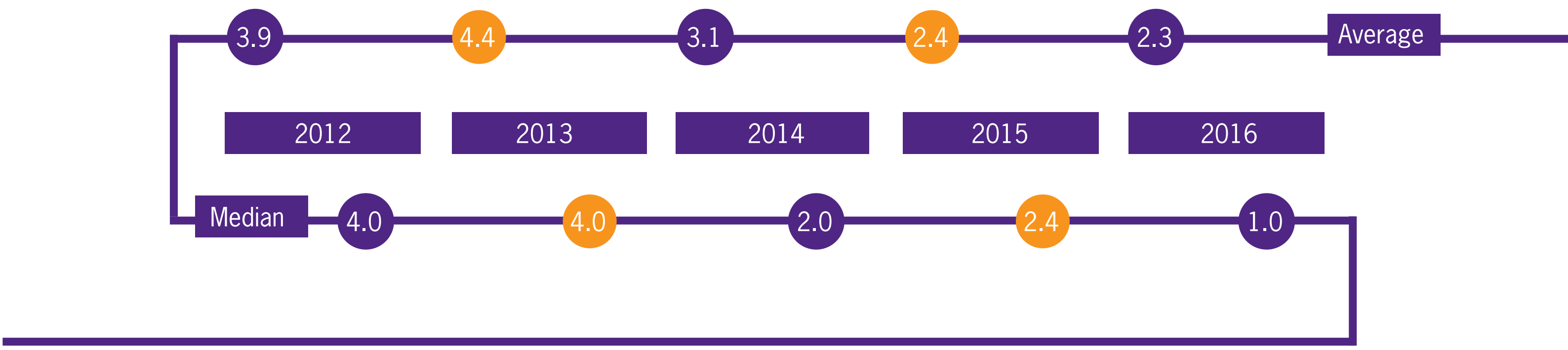


Trends in VC deal size

US$ mn	2012	2013	2014	2015	2016
Average	3.9	4.4	3.1	2.4	2.3
Median	4.0	4.0	2.0	2.4	1.0

Note: For the purpose of the above analysis we have classified investments above US$ 10 mn as Private Equity investment (PE)

Trends in VC deal size (in US$ mn)



3(b) Existing investment

I. Who are the active PE and VC firms

Key active PE/VC in 2015 and 2016 by number of investments

Rank 2015	Last year	Move	Investor	Count
1	1	↔	Angel investors	352
2	3	↑	Sequoia Capital	47
3	2	↓	Accel Partners	35
4	6	↑	Tiger Global	35
5	5	↔	SAIF partners	29
6	6	↔	Kalaari Capital	22
7	2	↓	IDG Ventures	21
8	3	↓	Helion Ventures	18
9	New	★	Indian angel network	17
9	5	↓	Nexus Venture Partners	17

Rank 2016	Last year	Move	Investor	Count
1	1	↔	Angel investors	526
2	2	↔	Sequoia Capital	29
3	3	↔	Accel Partners	27
4	9	↑	Indian angel network	25
5	New	★	Blume Ventures	24
6	5	↓	SAIF partners	19
7	7	↔	IDG Ventures	15
8	6	↓	Kalaari Capital	14
9	New	★	Venture Catalysts	10
9	New	★	Brand Capital	10

Startup investments have opened room for lot of angel investors who now provide startups with the required capital, typically at the seed round. The angel investors are more active now with the quantum of investments rising by more than 500 percent from 86 investments over a period of 2 years. This indicates the increasing investor appetite in the entrepreneurial startup ecosystem.

Sequoia Capital, Accel partners, Indian angel network and Blume Ventures have been the most active PE/VC investors in 2016.

The industry sources have projected the number of startups to increase from the current 4,300 to 11,500 by 2020 at the back of the impressive investment activity and also the general investor interest in India.

II. Sectors that attracted the most PE money

Investment values by key sector from 2012 to 2016 (US$ mn)

	2012	2013	2014	2015	2016
Start up	583	435	1,988	4,967	2,459
Telecom	1	1,260	110	500	2,055
Banking & Financial Services	747	1,109	1,257	1,924	1,878
Real Estate	722	954	1,731	1,187	1,509
IT & ITES	1,315	1,126	895	586	1,370
Manufacturing	226	507	314	864	984
E Commerce	116	456	2,364	1,838	975
Pharma, Healthcare & Biotech	907	1,391	586	981	653
Energy & Natural Resources	364	475	473	1,107	481
Transport & Logistics	425	81	207	132	436

III. Exits round up

2016 witnessed **90+** exits (38percent decline yoy) valued at around US$ 4.7bn (21percent increase yoy). Real estate was one of the most active sectors and open market transactions was the preferred exit route in 2016.

Notable PE exits

Sector: Automotive
Investor exited: KKR & Co. Ltd
Investee Company: Alliance Tire Group
Part/Full Exit: Full Exit

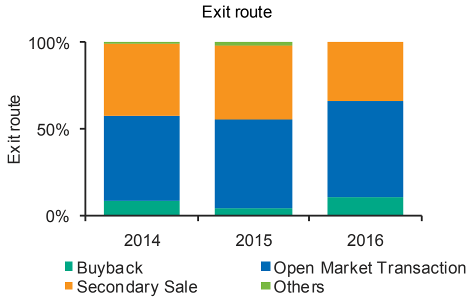
Sector: Telecom
Investor exited: Temasek
Investee Company: Bharti Telecom Ltd
Part/Full Exit: Full Exit

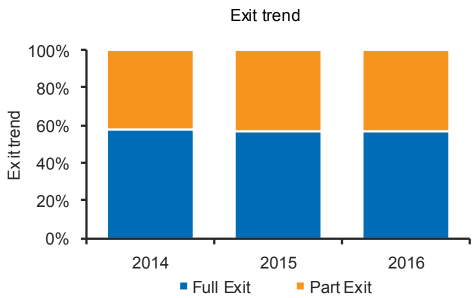
Sector: Pharma, Healthcare & Biotech
Investor exited: Advent International Corporation
Investee Company: CARE Hospital - Quality Care India
Part/Full Exit: Full Exit

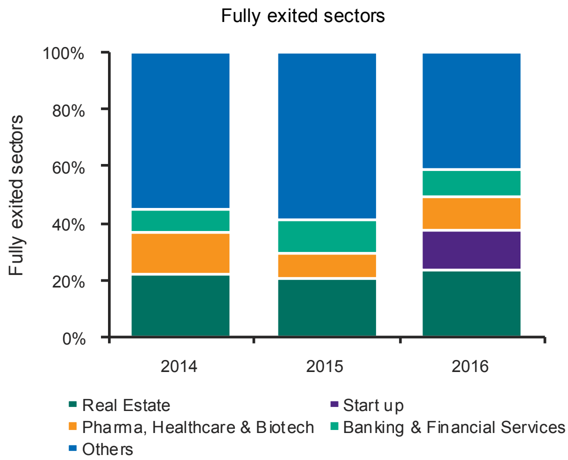
Sector: Manufacturing
Investor exited: Goldman Sachs Private Equity and others
Investee Company: Sigma Electric Manufacturing Co
Part/Full Exit: Full Exit

Sector: Real Estate
Investor exited: HDFC Property Fund**Investee Company:** Lodha Group's World Tower Project
Part/Full Exit: Full Exit

Exit volumes







3(c) Future investments/PE outlook

PE investments declined for the first time in 4 YEARS with nearly a 1,000 transactions contributing just below US$ 14 bn in values. Though the volume of transactions remained almost the same as 2015, the transaction values reduced by 12 percent due to the absence of large ticket transactions. This has resulted in reduced average deal sizes. 2016 saw smooth flow of follow on funding rounds as companies focused on expansion and increasing scalability while the year fell short of recording growth capital funding rounds resulting in reduced deal values.

In terms of sector spread, startups evidently continued to dominate both in terms of deal values and deal volumes contributing around US$ 2.5 bn and 70 percent to transaction volumes. Other major deal value contributors were core sectors such as telecom, BFSI and real estate capturing around 40 percent of values.

2016 struggled to witness large transactions in the PE space and this was perhaps because the focus for the last couple of years has been on the startup sector where transaction sizes have been relatively small. With macro-economic factors continuing to be positive and with reforms demonstrating early signs of economic growth, PE monies will shift focus to the consumer and industrial sector to fund both organic growth and consolidation in the domestic industry. PE will perhaps be visualised as an alternative means of financing consolidation for large and select corporates. This may result in the long-awaited big ticket transactions in the PE space.

Expert speak

Akshay Deshraj
Director
Grant Thornton India LLP

Cautious approach of PE investors

While the year 2015 witnessed a new peak for Private Equity (PE) investments in India, PE deal activity in 2016 demonstrated a more cautious approach. In 2016, total deal value declined by around 12 percent year-on-year. Average deal value also declined significantly, with only 22 PE investments above US$ 100 mn witnessed so far.

In spite of the cautious approach in large to medium investments, startup investments continue to be pursued aggressively by PE investors. Startup investments represent approximately 18 percent of all PE deals by value, though nearly 65 percent of such investments were in the Pre-Series A round of the funding. Mature e-commerce and fin-tech ventures, once the favourites of PE investors, have experienced subdued activity thus far. Institutional funding in Series A and above rounds was also less prominent this year. This has been due to a general slowdown in availability of growth capital and significant correction in valuation by global investors.

The recent uptick in investment activity in the third quarter is led by structured or debt deals in the real estate and renewable energy sectors. Though real estate was one of the biggest beneficiaries of PE investments, and had witnessed several high value deals this year, the recent demonetisation drive by the Indian government is expected to negatively impact PE investment activity in the real estate and housing financing companies in the short to medium term.

PE investment in core sectors however, continues to remain steady, with major deals taking place in the IT & ITes, BFSI and manufacturing sectors, which together represent around 30 percent of PE investment by deal value.

PE exits on a high

2016 set new records for PE exits through secondary sale. In 2016, PE exits totaled over US$ 2.8 bn through 31 secondary sale transactions, compared to 2015 that saw 63 exits totaling to around US$ 2.1 mn.

Strong performance of the secondary markets has provided PE-backed companies with an opportunity to provide their investors an exit through the IPO route. This trend is expected to continue, as a number PE-backed companies in the BSFI, consumer and retail sectors have upcoming IPOs in pipeline, or are actively exploring IPO based exit opportunities. Successful exits have strengthened PE investor confidence in the Indian markets, and are likely to promote big ticket investments over the medium to long term.

PE Outlook

PE investor continue to remain bullish over medium to long term

While short-term uncertainty remains on the overall impact of Government's demonetisation scheme on the consumer and retail sectors, PE investor sentiments continue to remain positive. The Government's push for digitalisation of economy is expected to have a positive and lasting impact.

Demonetisation has made a major impact on the investment outlook in all major sectors. The real estate, housing finance and luxury goods markets have been severely impacted in the medium term. FMCG is also adversely affected in the short term, though impact varies based on value of goods. This is expected to result in limited PE activity in these sectors over the medium term. E-commerce and fin-tech ventures, which witnessed reduced PE investments in 2016, are expected to make a comeback in 2017, capitalising on the digitalisation push.

Although investors remain bullish over the medium to long term, in the short term, investors are expected to be in "wait and watch" mode to assess the overall impact of changing regulatory policies on their current investments, before undertaking fresh investments.

Sector snapshot

4. Sector focus

Automotive		
207	132	436
10	8	8

E-commerce		
2,364	1,838	975
25	41	31

Real Estate		
1,731	1,187	1,509
43	32	18

Banking & Financial Services		
1,257	1,924	1,878
38	39	38

Startup		
1,988	4,967	2,459
219	680	666

Pharma, Healthcare & Biotech		
586	981	653
34	30	29

IT & ITeS		
895	586	1,370
61	44	52

Manufacturing		
314	864	984
18	17	19

Telecom		
110	500	2.055
2	1	3

Energy & Natural Resources		
473	1,107	481
14	12	7

Values US$ mn	2014	2015	2016
Volume	2014	2015	2016

Sector highlights

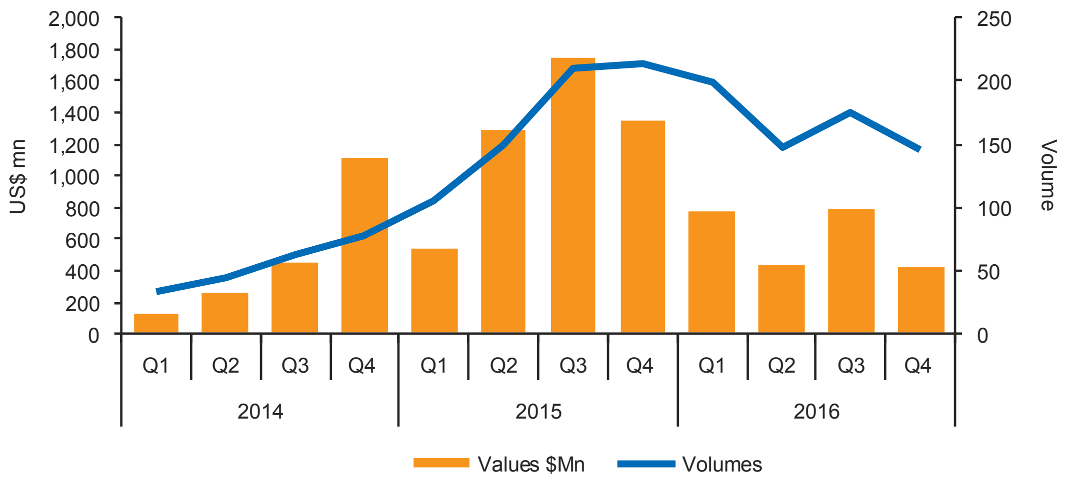
Startups continued to dominate investor interest with the highest contributions in investment values and volumes in 2016. Key sub-sectors which saw investment action were retail, logistics, enterprise infrastructure and application and discovery platforms.

Big-ticket consolidations among the domestic players in the telecom sector drove the sector's investment values in 2016. Banking and financial services was another top sector with the NBFC sub-segment alone garnering investments of US$ 888 mn contributing to 58 percent of the deal volume in the BFSI sector. Other sectors like real estate, IT & ITeS, manufacturing and e-commerce also witnessed big ticket deals valued over US$ 100 mn.

Retail & consumer and pharma & healthcare sectors are forming emerging sectors to attract private equity investments to support expansion of the established business operations.

I. Startup

Startup PE values declined by 50percent over 2015, volumes remained muted



Top sector by value
Retail (47 percent)

Top sector by volume
Enterprise Application and Infrastructure (18percent)

Top sector by value
Travel, Transport & Logistics (34 percent)

Top sector by volume
Retail (16 percent)

Top sector by value
Retail (26 percent)

Top sector by volume
Enterprise Application and Infrastructure (13 percent)

Top PE deals

Top five deals accounted for **22 percent** of total startup values

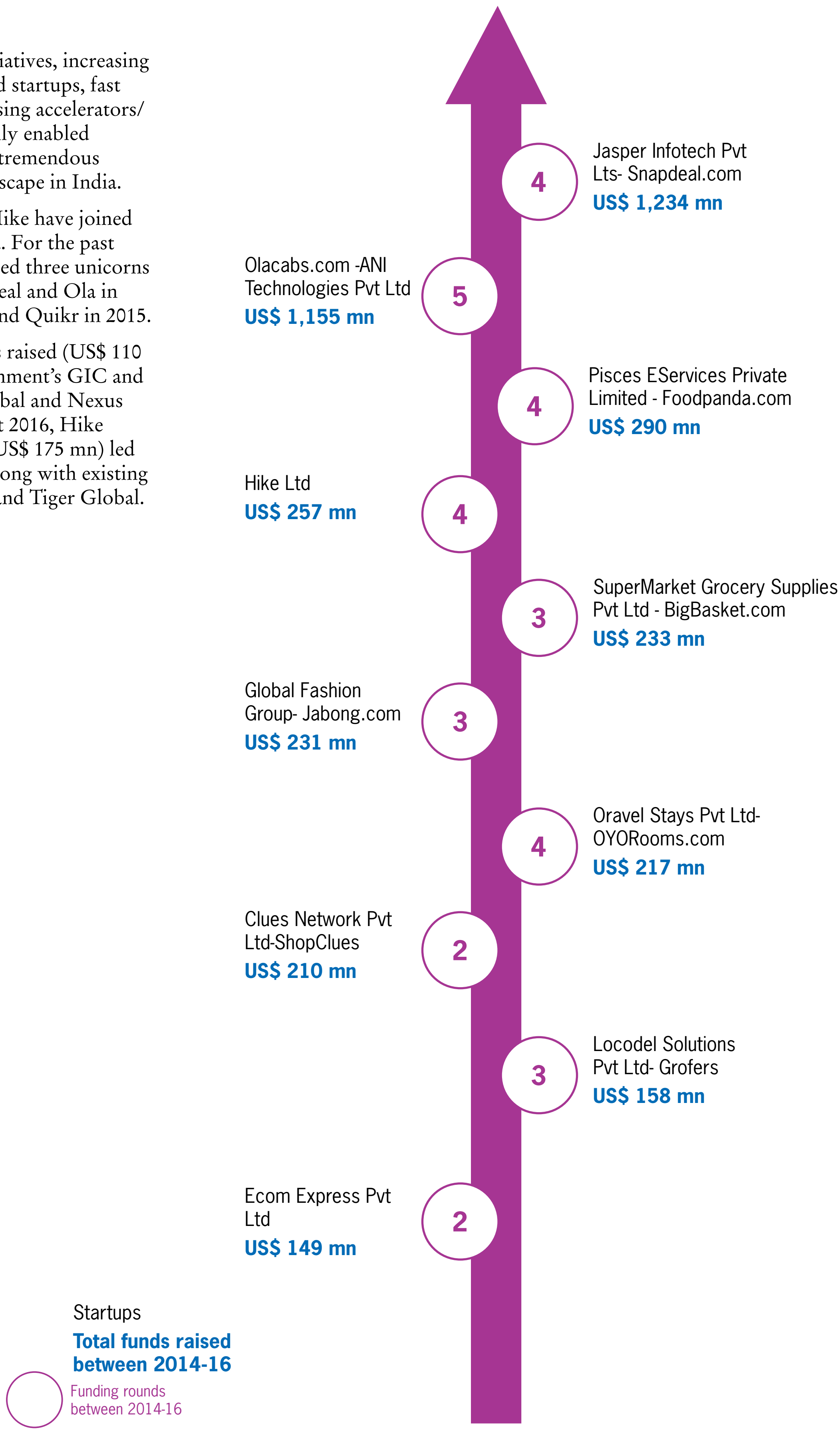
Investor	Investee	Sub sector	US US$ Mn
Tencent Holdings, Foxconn Technology Group, Tiger Global, Bharti Enterprises and Softbank Holdings Pte. Ltd.	Hike Ltd	Others	175
Helion Venture Partners and Zodius Capital, Ascent Capital, Abraaj Group, Bessemer Venture Partners, International Finance Corporation and Sands Capital.	SuperMarket Grocery Supplies Pvt Ltd - BigBasket.com	Retail	150
SoftBank Corp, Sequoia Capital, Lightspeed Venture Partners and Greenoaks Capital	Oravel Stays Pvt Ltd- OYORooms.com	Travel, Transport & Logistics	90
Warburg Pincus	Rivigo Services Pvt Ltd- Rivigo	Travel, Transport & Logistics	75
IFC, TPG Growth, Adveq Management, IDG Ventures and angel investors	Lenskart Solutions Private limited- Lenskart.com	Retail	60

Unicorns

Supportive government initiatives, increasing consolidation, rise in funded startups, fast maturing ecosystem, increasing accelerators/ incubators and rising digitally enabled consumer base have driven tremendous traction in the startups landscape in India.

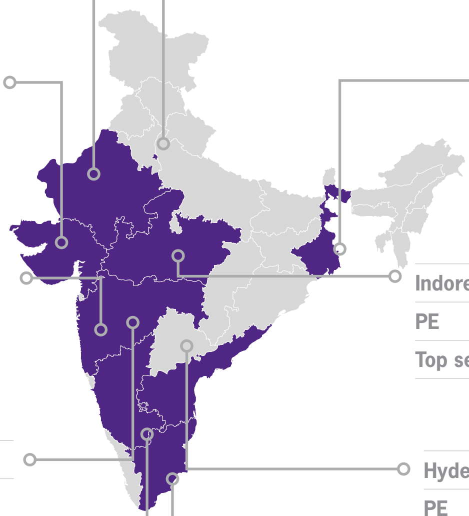
This year, ShopClues and Hike have joined the unicorn club from India. For the past two years, India has produced three unicorns every year – Inmobi, Snapdeal and Ola in 2014, and Paytm, Zomato and Quikr in 2015.

In January 2016, ShopClues raised (US$ 110 mn) from Singapore Government's GIC and existing investors Tiger Global and Nexus Venture Partners. In August 2016, Hike announced an infusion of (US$ 175 mn) led by Tencent and Foxconn, along with existing investors SoftBank, Bharti and Tiger Global.



Geographic representation by top cities

NCR, Bangalore and Mumbai lead in terms of PE startups with the three cities accounting for **79 percent** of the total number of startups funded in 2016. Pune, Jaipur and Chennai are the emerging cities which saw nearly 9% of total PE startup action this year.



Jaipur
PE | **Values:** 32 | **Volume:** 16
Top sector by volume: Retail

NCR
PE | **Values:** 837 | **Volume:** 220
Top sector by volume: Discovery platforms

Ahmedabad
PE | **Values:** 41 | **Volume:** 13
Top sector by volume: Food Tech

Kolkata
PE | **Values:** 16 | **Volume:** 6
Top sector by volume: Discovery platforms

Mumbai
PE | **Values:** 264 | **Volume:** 121
Top sector by volume: Retail

Indore
PE | **Values:** 20 | **Volume:** 9
Top sector by volume: Discovery platforms

Pune
PE | **Values:** 67 | **Volume:** 29
Top sector by volume: Enterprise Application and Infrastructure

Hyderabad
PE | **Values:** 21 | **Volume:** 15
Top sector by volume: On-demand services/ Enterprise Application & Infrastructure

Bengaluru
PE | **Values:** 824 | **Volume:** 201
Top sector by volume: Discovery platforms

Chennai
PE | **Values:** 25 | **Volume:** 16
Top sector by volume: Enterprise Application and Infrastructure

	US$ mn	Vol
Top 10 cities	2,459	666
Others	217	23

values are in US$ mn

Sector classification

The year saw a huge inflow of funds into B2C focused startups in the retail, discovery platform, logistics, health, education and fintech sectors. B2C verticals, within these sectors, that have had the maximum traction are food tech, on demand and hyperlocal services, discovery platforms and retail, which accounted for around 70 percent of the total investment flow in this space in 2016. Emerging sectors this year which saw a lot of action were fintech, edutech and healthtech.

B2B funding growth is coming in line with B2C, generating 23 percent of total PE deal values and 27 percent of deal volumes indicative of a growing ecosystem. B2B vertical witnessed investment activity in key segments such as enterprise application & Infrastructure, data analytics, logistics, and fin-tech.

Key verticals in 2015

Enterprise Application & Infrastructure
89 deals
Worth
US$ 198 mn

Data Analytics & AI
20 deals
Worth
US$ 66 mn

B2B
Recorded
172 deals
Worth
US$ 746 mn

Retail
102 deals
Worth
US$ 1,481 mn

Discovery platforms
78 deals
Worth
US$ 317 mn

B2C
Recorded
464 deals
Worth
US$ 4,079 mn

Health Tech
4 deals
Worth
US$ 10 mn

Discovery platforms
4 deals
Worth
US$ 25 mn

Both
Recorded
43 deals
Worth
US$ 139 mn

Key verticals in 2016

Enterprise Application & Infrastructure
78 deals
Worth
US$ 215 mn

Data Analytics & AI
25 deals
Worth
US$ 61 mn

B2B
Recorded
181 deals
5 percent
Worth
US$ 574 mn

Retail
68 deals
Worth
US$ 589 mn

Discovery platforms
67 deals
Worth
US$ 187 mn

B2C
Recorded
400 deals
14 percent
Worth
US$ 1,700 mn

Health Tech
12 deals
Worth
US$ 37 mn

Discovery platforms
11 deals
Worth
US$ 24 mn

Both
Recorded
78 deals
81 percent
Worth
US$ 172 mn

PE and VC investments in startups by sub sector

Unlike 2015, this year saw fewer big-ticket (US$ 100 mn) rounds of funding as investors tightened their purse strings. With only two startups raising above US$ 100 mn funding rounds and three startups with above US$ 50 mn investments.

One of the continuing themes was the PE interest in the retail sub-segment which attracted 26percent of deal value followed by travel & logistics (13 percent) and enterprise application & infrastructure (10 percent). In terms of volume, enterprise application & infrastructure contributed to 13percent of total volume followed by retail (12 percent) and discovery platforms (12 percent).

	Volumes			Values &mn		
Sub sectors	**2014**	**2015**	**2016**	**2014**	**2015**	**2016**
Retail	35	109	81	943	1,511	629
Travel, Transport & Logistics	19	88	59	386	1,700	321
Enterprise Application and Infrastructure	39	95	87	94	213	235
Discovery platforms	22	83	81	87	345	220
Fin Tech	13	47	52	37	197	163
On-demand Services	4	57	62	7	179	135
Health Tech	19	35	59	37	169	130
Food tech	5	44	28	91	310	130
Data Analytics & AI	7	22	29	13	69	67
Others	56	100	128	292	274	428
Grand Total	**219**	**680**	**666**	**1,988**	**4,967**	**2,459**

Expert speak

PE/VC performance in 2016:

PE/VC investments in start-ups have seen a significant drop in the total value of investments as compared to 2015. PE investments stood at 666 (US$ 2,456 mn), down from 680 (US$ 4,967 mn) in 2015, recording 51percent decline in deal values over 2015.

Start-up investments contributed to 18percent of the total PE values and 69percent of PE volumes in 2016. PE investments saw a declining trend in start-up while 92percent of the total investments were made by VC funds.

Top 5 deals accounted for 22percent of the total start up values, led by investment in Hike Ltd (US$ 175 mn) by Tencent Holdings, Foxconn Technology Group, Tiger Global, Bharti Enterprises and Softbank Holdings Pte. Ltd. This round also resulted in Hike joining the unicorn club.

2016 did not witness big ticket transactions as compared to 2015 which saw many blockbuster investments above US$ 100 mn including Ola cabs and Snapdeal, with an average deal size of US$ 223 mn, whereas, 2016 saw only 2 start ups (Hike and Big Basket) receiving funding of above US$ 100mn compared to 11 in 2015 – with average deal size dropping to about US$ 68 mn.

Sector insights

The only sector that saw increased investment in 2016 with US$ 235 mn as compared to 2015 US$ 213 mn was Enterprise Applications and Infrastructure with an increase of ~10percent even though it witnessed a fall in total number of deals during the same time

The top three sectors that cumulatively received funding of US$ 1.2bn include retail, transport & logistics and enterprise solutions, which together account for more than 33percent of the total investment activity. Other key segments that witnessed deal activity include discovery platforms (10percent of total investment value) and Fintech (8percent of total investment value).

B2C contributed to ~70percent of the total start up investment. Top 5 deals in this segment accounted for 34percent of total deal values in B2C –namely Hike, Big Basket, Shopclues, Oyo rooms and Lenskart.

In 2016, B2C segment garnered US$ 1,697 mn a 58percent fall as compared to 2015 (US$ 4,049 mn), while volumes declined by 13percent y-o-y.

PE investments in B2B segment fell by ~25 percent in 2016 (US$ 577 mn) as compared to 2015 (US$ 775 mn), however start-ups are starting to cater to both (B2B and B2C) verticals with 81percent increase in volumes of such start-ups.

Top 5 deals in the B2B segment accounts for 28% of deal values

B2C verticals, within these sectors, that have had the maximum traction are retail, travel, transport & Logistics, discovery platforms and food tech, which accounted for around 62percent of the total investment flow in this space in 2016

Enterprise infrastructure solutions & Transport and logistics sectors attracted over 55percent of the investment in B2B space – Rivigo owned by Ecom logistics stands out with the deal size of US$ 75 mn.

Data Analytics & AI: Innovations such as Google Allo, Amazon Alexa has expanded the boundaries of automation – with the increase in machine to machine learning, the Social, Mobility, Analytics and Cloud sector is witnessing new investments with across industry applications – this segment has seen 22percent increase in volume of deals totalling about US$ 67mn

Fintech: Fintech has seen 10percent increase in the number of deals although the value has fallen by 17percent. The increase in the volume of deals demonstrates the strength of fundamentals on the sector – un-banked sector and low penetration of financial products accentuated by the effect of demonetisation is bound to evolve into diverse and large sector across Payment wallets, Biometric authentication, Cyber security, Insuretech, Robo advisory and the rise of India stack.

Sector Outlook

The average deal size for VC funding stood at US$ 2.4 mn.

Funding rounds at series A and below dominated with 74 percent of the total start up volumes raising over US$ 1bn.

We observed angel/seed rounds to be as low as US$ 20000 and they went up to US$ 10 mn. Series A ranges between US$ 1 mn and US$ 20 mn. With the tax cut announced for less than Rs 50 crore turnover companies, lot of start-ups stand to benefit with the 5percent reduction as well as from the tax holiday extended upto 5 out of 7 years – added benefit for founders to dilute their stake to raise money even though they are loss making. Total number of M&A deals in 2016 were 146 (US$ 881 mn), up from 135 (US$ 885 mn) in 2015

The year witnessed a lot of traction with 662 round of investment raising around US$ 2.3 bn from VC funds

Although, PE investments saw a declining trend in start-up while 92percent of the total investments were made by VC funds . Notable is the 8percent increase in M&As, from 135 to 146 deals totalling about US$ 881mn.

Vidhya Shankar
Executive Director
Grant Thornton India LLP

II. IT & ITES sector

Sector Insights

The Indian IT & ITES sector has been witnessing the adaption of new technologies and has been focusing on developing enterprise solutions on the back of Social, Cloud, Mobility, Artificial Intelligence and Big Data. The rapidly growing start-up ecosystem in India backed by Government's initiatives, which are aimed at digitising India, have been driving the innovation in the industry.

As the sector is undergoing transformation, the PE deal space has also gained momentum since 2015 and continued into 2016. The key trends in the PE activity in IT & ITES sector are:

- While 2015 saw 43 deals with deal value of US$ 416 mn, 2016 witnessed 51 deals with deal value of US$ 554 mn, excluding the following two strategic deals
  - Blackstone's acquisition of MPhasis in 2016 ($816 mn)
  - Blackstone's acquisition of IBS Software Services in 2015 ($170 mn)
- In 2015, Software Development segment has driven the deal volume (19 with US$ 231 mn) followed by IT solutions (10 with US$ 65 mn) and Data Analytics & AI (5 with US$ 73 mn).
- In 2016, these three contributed similar deal values - Software Development (17 with US$ 174 mn), IT solutions (20 with US$ 175 mn) and Data Analytics & AI (10 with US$ 176 mn). 4 out of the 5 top deals in 2016 are from these segments.

IT&ITeS	2015	2016	2015	2016
BPO/KPO	2	1	10	816*
Cloud Technology	4	3	33	25
Data Analytics & AI	5	10	73	176
IT Solutions	10	20	65	175
Mobile VAS	2	1	3	4
Others	1		2	
Software Development	20	17	401*	174
Grand Total	44	52	586	1,370
Less: Strategic deals *	1	1	170	816
Total	43	51	416	554

*** indicates strategic deals**

Acquirer/Investor	Target/ Investee	Sub-Segment	$' mn
Blackstone Group Lp	Mphasis Ltd	BPO/KPO	816
Khazanah Nasional Berhad	Fractal Analytics Ltd	Data Analytics & AI	100
Capital Square Partners	Indecomm Global Services (India) Private Limited	IT Solutions	90
Accel Partners and Sequoia Capital India	FreshDesk Technologies	Software Development	55
EDBI, Blue Cloud Ventures,Hercules Capital, Sequoia Capital, NTT Finance, Nexus Venture Partners and Tenaya Capital	Druva Software Pvt Ltd	Software Development	51

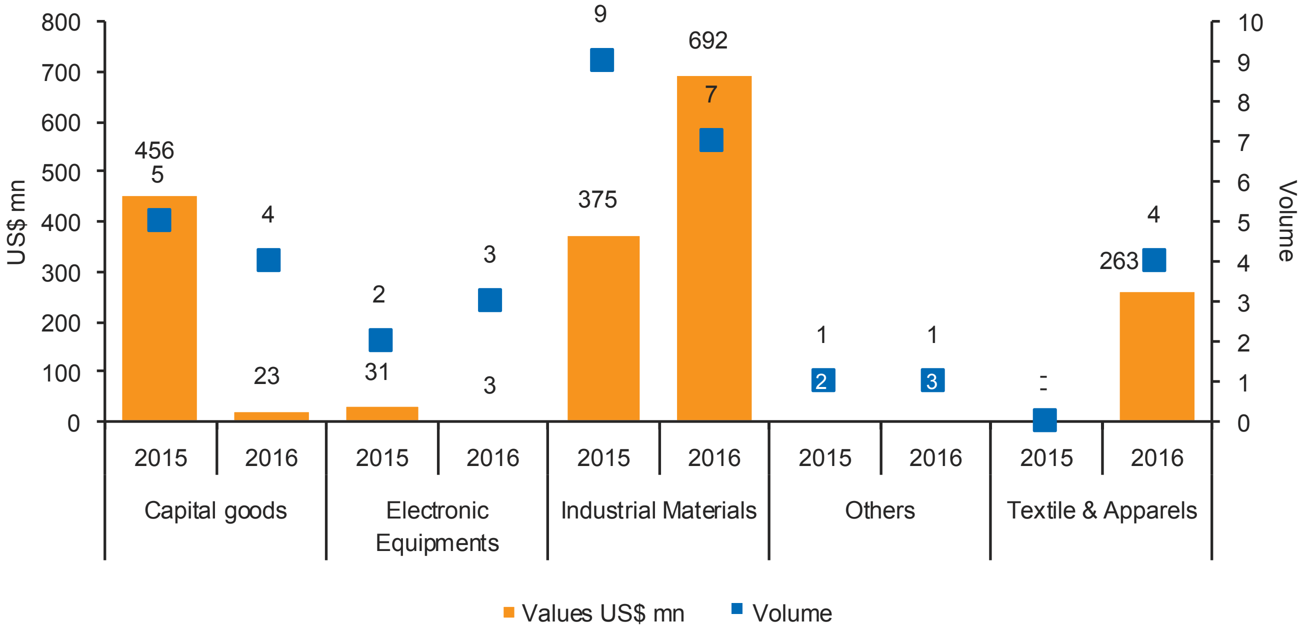
Sector Outlook

Indian IT & ITES sector is focussing on adding capabilities and reskilling the existing workforce in order to adapt to the changes necessitated due to the rapidly developing technologies, emerging solution offerings and transforming business models. This would continue to generate opportunities for the start-ups driving the innovation in the industry and working on niche solutions. While, the overall industry outlook may be dampened by the risks emerging from the recently introduced restrictions on the US immigration laws, the outlook for PE investments in the industry is positive and 2017 is expected to witness levels similar to 2015 and 2016, if not more.

Shanthi Vijetha
Director
Grant Thornton India LLP

III. Manufacturing sector

Sector performance/insights



The PE deal space in the manufacturing sector has never been as popular as in the M&A space. PE deals in the sector accounted for less than 2 percent of the total deals in 2015 and 2016, accounting for around 5.5 percent and 7 percent of the total PE deal value during 2015 and 2016 respectively. The deal activity remained fairly consistent with 19 deals (US$ 984 mn) announced during 2016 as compared to 17 (US$ 864 mn) during 2015. The largest deal announced was Fairfax Holdings investment of US$ 300 mn in Sanmar Chemicals Group. The other large deal announced during 2016 was Argand Partners LP's acquisition of 100 percent stake in Sigma Electric Manufacturing Company for US$ 225 mn. The average deal size remained fairly consistent around US$ 50 mn over these two periods.

With the manufacturing sector being considered a key sector in India's growth story and the positioning of India as the fastest growing economy in the global outlook, the sector is expected to see more traction in the coming years. With the current government focused on improving the investment and operational climate in the country and the economic and regulatory reforms on the anvil, most investors would be realigning their outlook and approach to investments in India.

Sector Outlook

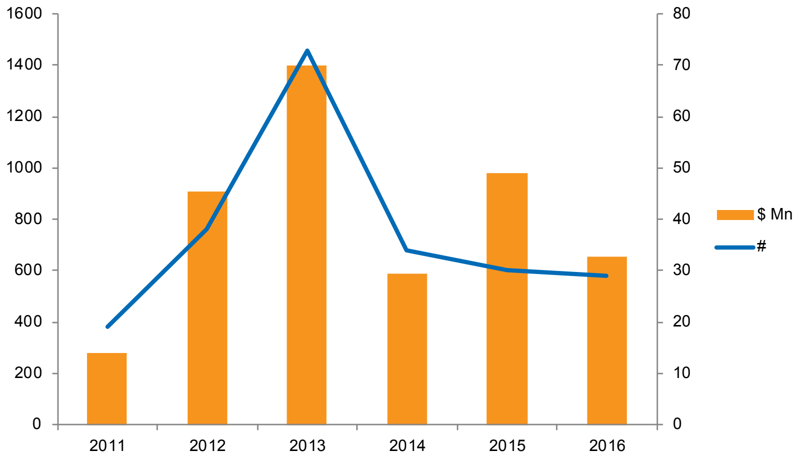
Deal activity is expected to pick up within various sub sectors like Capital Goods, Auto Components and Industrial Materials on account of various factors like enabling policy support, on-going consolidation, FDI inflow, technical collaborations, restructuring of businesses, development of industrial corridors offering concessions and benefits, development of smart cities and infrastructure, etc. In our view, the extended support being offered by the government and related bodies to the business environment in general should boost up the PE and VC investments in India in the coming years.

Anirudh Gupta
Director
Grant Thornton India LLP

IV. Pharma, Healthcare & Biotech

PE activity in 2016 has seen a decline of 33percent in values while volumes remained constant, indicating a drop in big ticket deals in the year. 2015 witnessed 5 hundred mn dollar deals while 2016 had just one. While 2015 witnessed large pharma deals in Capital International – Mankind Pharma (US$ 205 mn), Temasek – Glenmark (US$ 151 mn), 2016 PE landscape has clearly favored the hospital segment.

Overall Pharma, healthcare sector PE deal values and volumes



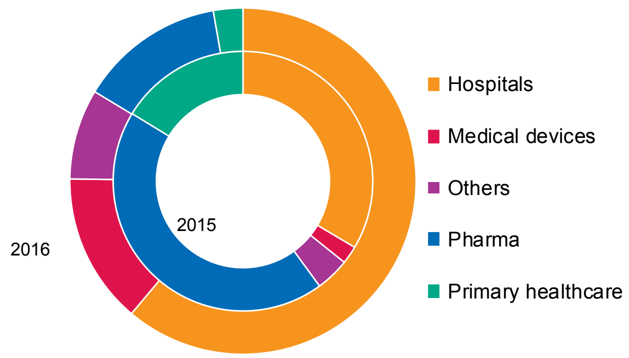
Sector performance/insights

Pharma sector in 2016 witnessed a 80percent decline in values and a 22percent decline in volumes over 2015. This can be attributed to the lack of big ticket deals in the pharma space in 2016. While the fundamental strategy of consolidation, gaining access to global markets in generics continues to remain intact, the lack of big ticket deals in 2016 is possibly a temporary trend and can be expected to revive in 2017 on the back of a globalisation of pharma industry and the quest for cross border presence.

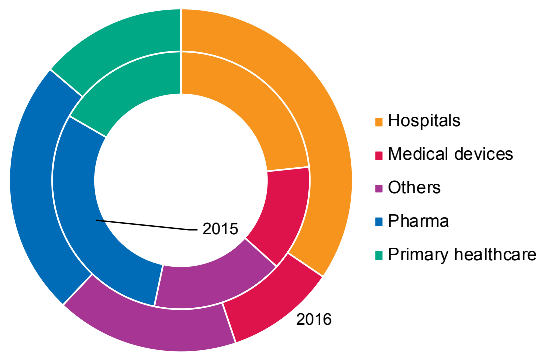
Hospital segment witnessed a 42percent increase in volumes and 21percent increase in values over 2015. The top PE deals in 2016 has largely been in the hospital space with global PE majors such as Abraaj, TPG, IFC eyeing attractive hospital assets in the country. It is also interesting to note the revived interest in single specialty space both in the form of primary infusion (TPG- Cancer Treatment Services) and through secondary exits as can be seen in the ADV – Dr. Agarwal Eye hospital deal, TPG – Rhea healthcare deals. We expect this segment to continue to witness heightened interest and premium valuations in 2017 on the back of a huge demand supply gap in Indian healthcare, growing focus on tier 2 hospital chains and increasing preventive healthcare awareness and affordability.

Medical technology segment is starting to witness innovations in high end technology as compared to the traditionally low end consumables driven segment. However, the sector faces challenges in the form of an uncertain regulatory environment, pricing pressures etc. 2017 is expected to see the hospitals introduction of several reform measures targeted at easing investments and creating a separate regulatory body for the segment through the proposed Draft Medical Devices bill. While the segment is nascent in India and will take a while to attract big ticket investments and investor interest, emergence of e-health/m-health platforms spanning the spectrum of healthcare services, digital access to information and advanced technological tools signals a higher level of deal activity in the deal start up space going forward.

Split of deal values by subsector



Split of deal volumes by subsector



Top PE deals in the sector

Investor	Investee	Seller	percent Stake	Padded Amt*
Abraaj Group	CARE Hospital - Quality Care India	Advent International Corporation	N.A.	195.00
International Finance Corp	Apollo Health and Lifestyle Limited	N.A.	29 percent	66.18
Kedaara Capital	Sutures India Pvt Ltd	CX Partners	13 percent	59.70
ADV Partners	Dr. Agarwal's Healthcare Ltd	Evolvence India Life Sciences Fund	N.A.	45.00
TPG Growth	Cancer Treatment Services International	N.A.	65 percent	33.00
TPG Growth	Rhea Healthcare Pvt Ltd- Motherhood	N.A.	N.A.	33.00
Everstone Group	Rubicon Research Pvt. Ltd	Kotal Private Equity	70 percent	33.00
Sequoia India, Sands Capital Ventures, RA Capital Management, Accel Partners and Tata Capital Innovations Fund	Mitra Biotech Pvt Ltd	Karnataka Information Technology Venture Capital Fund (KITVEN) and India Innovation Fund	N.A.	27.40
Samara Capital Management Ltd	Sahajanand Medical Technologies Pvt Ltd	N.A.	N.A.	25.00
Samara Capital Partners Fund II Ltd	Adcock Ingram Healthcare Pvt. Ltd	Adcock Ingram Holdings Ltd	100 percent	22.00

Sector Outlook

PE backed transactions will continue to see traction in healthcare. Cross border integration activities in pharma will largely be driven through financing by banks and PE players. While VC's will remain on the lookout for newer technologies and service solutions across all subsectors, PE involvement in the sector will continue in the medium to large transactions across pharma and healthcare delivery.

Vrinda Mathur
Partner
Grant Thornton India LLP

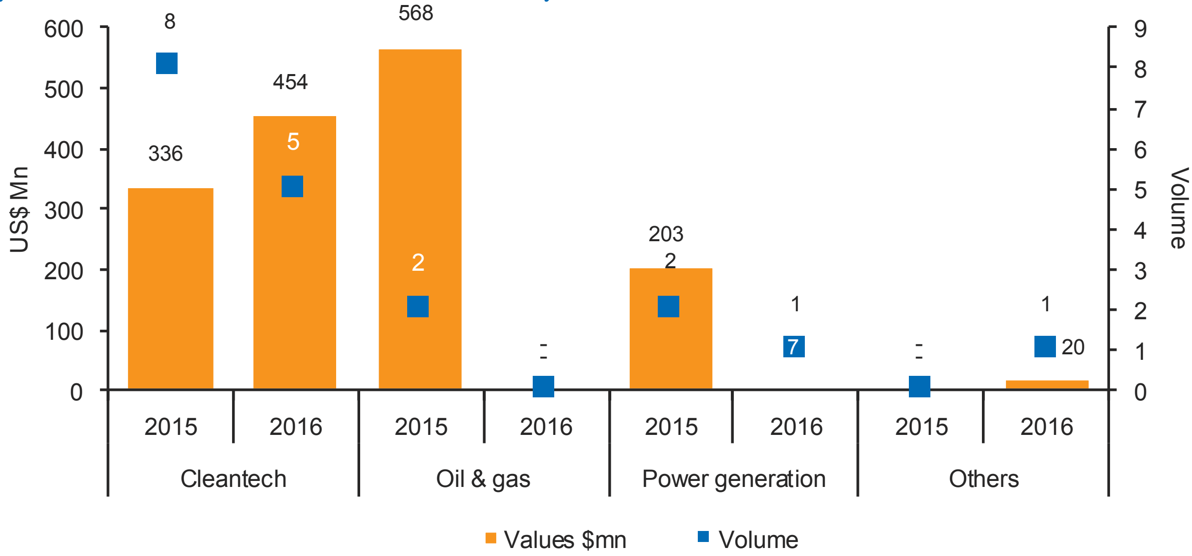
V. Energy and natural resources sector

Sector performance

Energy and Natural Resources Sector - Transactions summary

	2015	2016
Volume	12	7
Value US$ mn	1,107	481

Energy and Natural Resources Sector - Transactions by sub sector



Plain reading of the deal statistics in the Energy and Natural Resources sector would indicate low-levels of interest of the PE/VC fraternity in the sector. However, comparison of the prior year transactions with the current year transactions by sub sector highlights the following trends:

1. Cleantech continues to interest the PE/VC players. Aggregate value of transactions in the Cleantech segment grew from US$ 336 mn in 2015 to US$ 454 mn in 2016. Despite decline in the number of transaction from 8 in 2015 to 5 in 2016, the average deal size more than doubled (2015: US$ 42 mn; 2016: US$ 91 mn).

2. 2015 witnessed 2 transactions aggregating to US$ 568 mn in the Oil and Gas sub-sector, which included US$ 500 mn invested by Carlyle Group in Magna Energy Limited. This sub-sector remained silent in 2016 with no reported transactions.

3. Power generation sub-sector witnessed 2 transactions aggregating to US$ 203 mn in 2015, which included US$ 122 mn investment by Macquarie Infrastructure & Real Assets in Ind Barath Energy Utkal Ltd unit - Ind Barath Power Infra Ltd. Only one transaction of US$ 7 mn was consummated in the sub-sector in 2016.

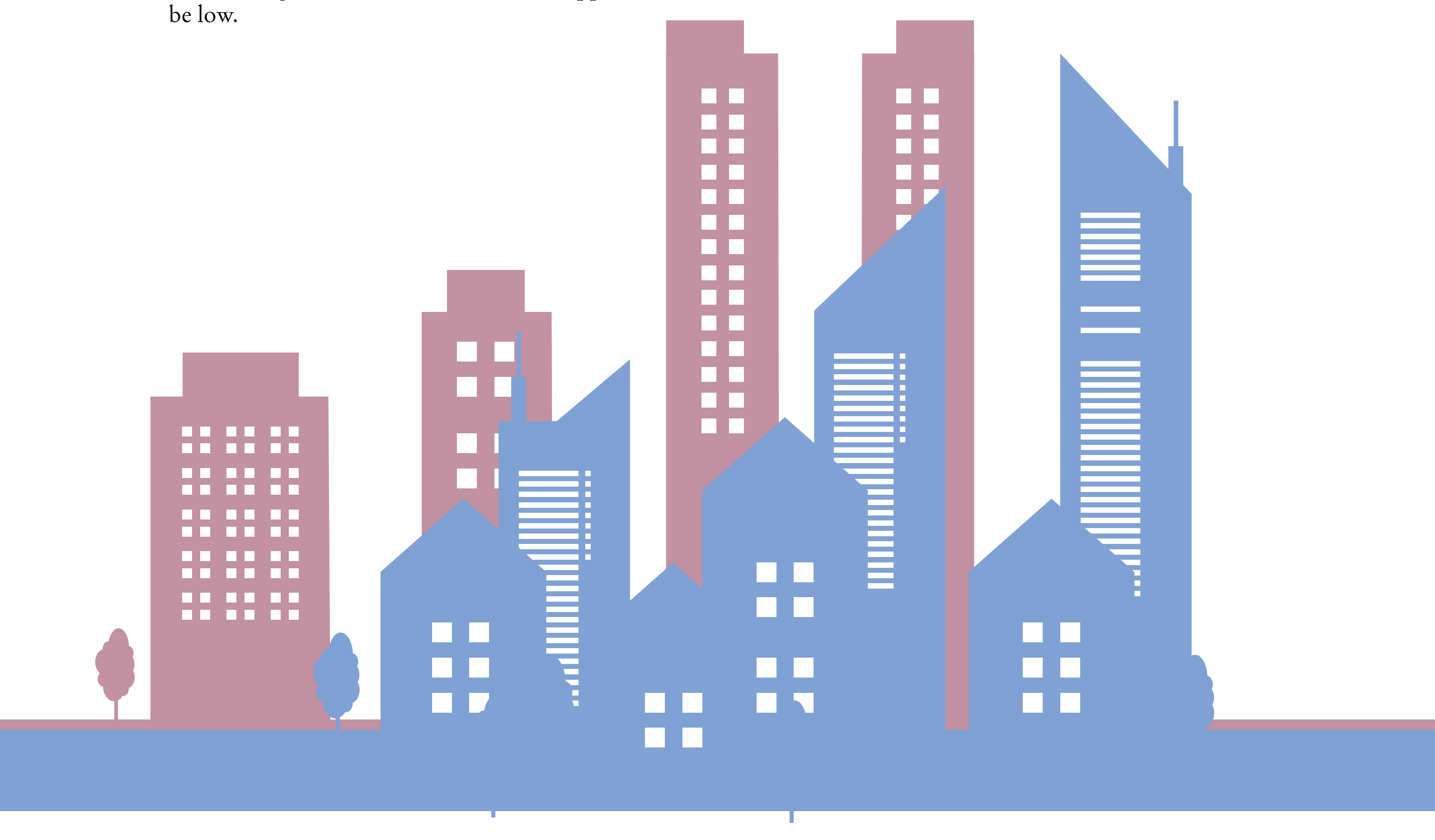
Key insights for transactions consummated in 2016

1. Only few selective PE/VCs have been active in this sector in 2016. Reported 7 transactions involved 4 PE/VCs, which included 2 transactions each by Piramal Enterprises and IDFC Alternatives.
2. 5 of the 7 transactions reported in 2016 were in the Cleantech sub-sector. 2 transactions of US$ 100 mn+ were consummated in the sub-sector, which included GIC and Abu Dhabi Investment Authority investment in Greenko Energy Holdings (US$ 230 mn) and Piramal Enterprises Ltd and APG Asset Management investment in ACME Cleantech Solutions Pvt. Ltd (US$ 132 mn).
3. Majority of the transactions involved India based PE/VCs and similarly majority of the Target investments were Cleantech companies owned by traditional companies which have significant presence in other sub-sectors of the Energy and Natural resources sector. The aforesaid trend indicates that execution capabilities increase the confidence of the PE/VC fraternity for consummation of transactions in the sector. Interest of the foreign PE/VC firms in the sector appears to be low.

Sector Outlook

Government's reforms in the laws regulating this sector, focus on cleantech and incentives rolled out to encourage investment in the sector are expected to increase deal activity in the sector. Technological innovations and integration of big data analytical tools in the technology based products for the sector will encourage start-ups in the sector and thereby make room for increased participation from PE/VC investors.

Pankaj Chopda
Director
Grant Thornton India LLP



VI. Emerging sectors

Banking and financial services

Key insights for transactions consummated in 2016

Khushroo Panthaky
Director
Grant Thornton Advisory Private Limited

2015	2016
US$ 3.7 bn	US$ 3.8 bn
62	72

The Financial Services Industry is one of the most dynamic industries and is highly instrumental in the development of any economy. The growth and progression of this industry significantly impacts other industries and vice-versa. Financial services industry has various segments, such as banking, insurance, funds, asset management, NBFC, home finance, micro finance, micro housing finance, capital markets, and to a great extent fin-tech as well, and it is therefore difficult to conclude on the overall performance of this industry effectively. It is pertinent to analyse the growth and development under each segment of this industry, as its performance in calendar 2016 has been concerning. On an overall basis, technology remains the key under every segment of this industry, since a significant chunk of this industry is operated on the best platforms of information technology. Even from a regulatory perspective, this industry is one of the best regulated, as compared to others. Also, India is second to none as far as the regulatory oversight on this industry is concerned.

The Indian Banking sector is well capitalised and highly regulated. Indian banks have withstood the global downturn and have shown resilience as far as the liquidity, market and credit risks are concerned. New banking models such as payments banks and small finance banks have been rolled out in the system. As per RBI, in-principle approval has been awarded to 11 payments banks and 10 small finance banks and such initiatives and other measures undertaken by RBI would be very instrumental in providing a facelift to the banking industry in India. The Indian Banking Sector has witnessed an overall healthy growth rate. In its continuous endeavour to effectively and efficiently grow, the Indian Banking sector has adopted improved risk management practices, encouraged technological innovations, diversified its revenue streams and has been focussing on financial conclusion. It continues to increasingly look out at the opportunities for consolidation, developing innovative financial products and instruments, such as derivatives and risk management products. As per RBI Deputy Governor, the Central Bank has collected over US$ 185.81 bn in demonetised notes from various branches of the banks. The impact of demonetisation was also obvious, as the bank credit reduced by 0.8 percent. From 8 November 2016 to 25 November 2016, US$ 9.85 bn were paid by the defaulters. The banking sector underwent vital reforms with the introduction of Insolvency and Bankruptcy Code, 2016. The code is expected to empower the judicial system to handle corporate defaults and winding-up petitions. Further, new RBI guidelines on stressed assets would reduce the burden of bad loans on their balance sheets. Proposed mechanisms for asset resolution, including the Bankruptcy Code, will help speedier recovery. Further, RBI's initiative of making it mandatory and having no exceptions for complying with the standards on Know Your Customer (KYC) have enabled all the banks to ensure that there is a comprehensive policy framework in order to prevent money laundering activities. RBI has worked over the past three years on the financial inclusion plan, wherein, it encourages self-set targets for opening rural brick and mortar branches, employing business correspondents, covering un-banked villages through banks' branches and other means and opening no-frills accounts to provide opportunities to the financially excluded segments. This step would ensure that banking is available at every doorstep.

In the Insurance industry sector, there have been key changes in the regulatory framework in India, with foreign partners increasing their stakes in the Indian joint ventures, in consequence to the Foreign Direct Investment limit being allowed to increase from 26 to 49 percent. The reinsurance industry has also witnessed a significant change with foreign insurers allowed to set up branches in India. The insurance industry has moved into the next phase with initial public offerings made and proposed to be made by the large private insurance players. Technology forms the edifice for this transformation, as its role changes from a mere ancillary function to being graduated to a core competency for insurance businesses. The increased internet and mobile connectivity will digitalise the role of insurance across the value chain with real time access to policy data and virtualisation of processes. The private sector insurers continue to discourage cash transactions. There are checks and balances against cash transactions, such as tax deduction certificates. For instance, in case of health insurance, if premium is paid by cash, then it is not entitled for tax deduction under Section 80D of the Income Tax Act. Agency-driven policies will be impacted the most, as the agents tend to collect premiums in cash. The problems faced by the agency channels appear to be short lived. Eventually, this would expedite the process of general public switching from cash to plastic and using online wallets and banking and in turn will provide a boost to the consumer internet business. The country also witnessed a major consolidation in this sector, wherein, two large private life insurance players are in the process of getting integrated to emerge as a challenging player in the market place and to also reap other benefits out of the integration, such as integration synergies, cost effectiveness from a consolidated business and a widespread geographical coverage. Further, the traditional insurance products have once again started becoming popular in comparison to the unit linked products.

In the mutual funds sector, the Securities and Exchange Board of India (SEBI) has been proactive with introducing regulatory changes, investor protection measures (especially in the context of recent mutual fund portfolio liquidity risks/mutual fund distribution, through electronic platforms), exploring ways to broad-base the retail funds market and thereby widen the pools of capital available to mutual fund asset managers (AMCs). With a significant increase in the level of bank deposits, which has been particularly witnessed during November and December 2016, the fixed deposit rates would be adversely impacted and therefore the depositors will be looking forward to other alternate channels of investments within the organised sector, such as mutual funds etc. as against investments in real estate and gold. This would result into significant money being channelised into the mutual funds industry, which in turn would positively impact the growth in the debt and equity markets of the nation.

NBFCs had a good year indeed, until they were hit by the demonetisation. Although there has been a growth in the income of the upper middle class and there is a better potential to save and spend in comparison to the past, there is an increased tendency to avail loans for different purposes and this is one of the major reasons as to why NBFCs showed a good amount of growth, until the demonetisation. Increased awareness of the benefits of availing credit and easy credit being available at affordable rates from the Points of Sale are growth drivers in the NBFC lending space. Subsequent to the demonetisation, the business of NBFC has been adversely impacted and the share prices of listed NBFCs have significantly reduced on account of the reduced demand for loan disbursements, which is directly linked to the slowdown in the economy and the health of the loan book, as the ability of the borrowers to pay the installments on time is also adversely impacted.

Micro finance and micro housing finance companies witnessed growth during 2016, until the announcement of demonetisation. The micro lending concept has picked up well on account of a huge segment of our population being middle class and lower middle class, which leads to an inclination and an endeavour to own a business venture in a modest manner or own a small affordable home to live in. The concept of nuclear family has gained a good amount of momentum in India and there is an increased demand of affordable housing, which leads to availing loans, payable over a long period of time and in smaller installments. Even from a micro finance perspective, there is a focus to encourage lending for the development of the SME sector and therefore entrepreneurship within the middle class and lower middle class has considerably emerged. There is hardly any incidence or a very low incidence of NPAs in case of micro lending which has been one of the reasons for the emergence of many lending houses during 2016 in the space of micro finance and micro housing finance. Over a period of time, our nation will also witness significant growth in micro lending for the purposes of buying second hand vehicles and motor cycles. Subsequent to the demonetisation, this segment has been adversely impacted as the borrowers, who are primarily emerging entrepreneurs or low income earners are adversely impacted by the after effects of demonetisation, which has reduced their ability to pay off the monthly installments on time and therefore the government has rightly announced certain relaxation measures, so as to ensure that delays in payment of loan installments do not constitute defaults.

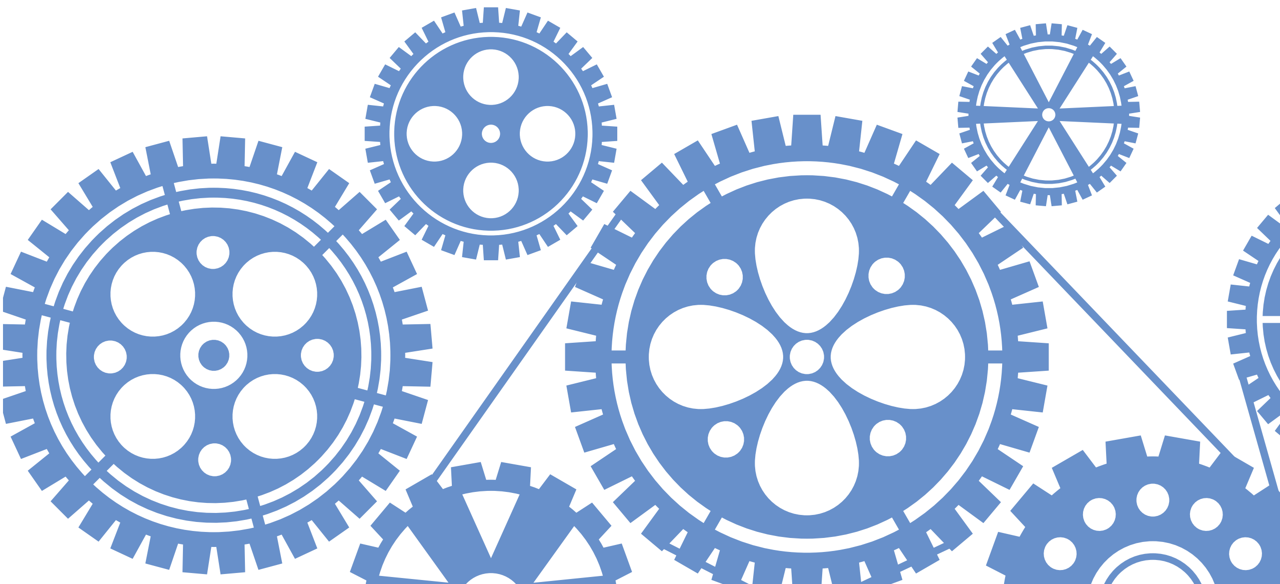
Fintech is the buzz word in our economy and within the FS industry and is known for its disruptive and contemporary nature. It ensures convenience and ease in executing financial transactions under the assumption of having in place a world class technology. The e-wallets, mobile banking and other electronic modes of payments and wallets have caught a lot of momentum this year and subsequent to the demonetisation, the use of electronic modes of payments has substantially increased. The government and the regulatory authorities have worked very hard to facilitate the availability of safe and secured electronic modes of payments by strictly ensuring layers of security, both at the service providers' end and at the users' end. Substantial awareness is created across the country and in particular, in the rural areas, as regard to the benefits of getting adapted to electronic modes of payment. The announcement made by the Government to provide discount on payments made through electronic modes is well received and is in the larger interest of the economy, as it leads to having less paper money in circulation. Fintech companies will continue to play a vital role in providing top class security and ease in processing financial transaction. The fin-tech companies and regulators would continue to enhance the awareness of the society to encourage execution of transactions through electronic modes.

The central bank has allowed 100 percent foreign investment through the automatic route to the regulated financial service companies, other than banks or insurance companies, and has simplified rules for easier entry of venture capital funds to startup ventures. It has also eased external commercial borrowing regulations. This has been of significant help to the industry.

To conclude, the financial services sector has witnessed a year of good, innovative and challenging times during 2016. Further, Ind-AS, the new set of Indian Accounting Standards, would be applicable to many sectors of this industry, effective 01 April 2018 and would result into a new financial reporting framework. This could significantly impact the manner in which the net worth and profitability are currently determined. The multiple regulators overseeing the industry are conscious about the various economic developments and are doing their best to ensure that the health of the financial service companies and conglomerates remain in check. The single largest factor which has caused fear and disruption within the sector is the impact of the demonetisation, which would take some more time to put this industry back into top gear.
However, the government will continue to effectively regulate the industry in the wider interest of the shareholders, stakeholders, investors, borrowers, lenders and others, who have a role to play.

Secured and tested technology platforms would remain to be the top priority for this industry, as it constitutes the backbone of operations. Therefore, the industry and the regulators would leave no stone unturned in ensuring appropriate and adequate investments to have a world class IT infrastructure in place. The landscape of India's financial sector is changing and will continue to evolve. One should no longer be talking about 'digital transactions' but transactions in a 'digital world".

Sources of limited referencing made to compile this write up: Indian Banking Association, Reserve Bank of India, Tech Sci Research, CII publications, newspapers etc.



Digital payments

Prashant Mehra
Partner
Grant Thornton India LLP

2015	2016
$1,102 bn	$584 bn
70	73

With the rise in internet penetration (especially through mobile data) and growth of the economy as a whole, the digital payment industry is set to flourish in India. This, coupled with the thrust of economic reforms by the government, whether it is the startup initiative, policies encouraging bank account opening or the recent demonetisation of high denomination notes will altogether drive the economy from cash transactions to digital payment solutions and will penetrate not just in the urban but also the rural and semi-urban regions in India. The private sector too, is doing its bit by creating new and better platforms for this mobile data penetration.

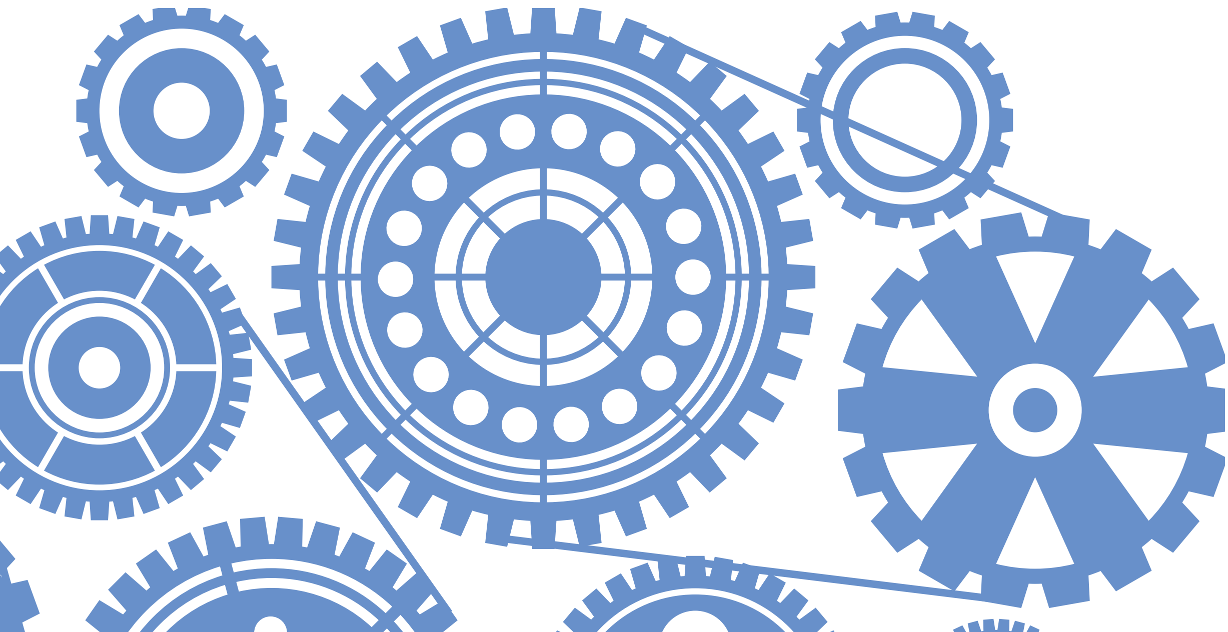
E-commerce

Triven Gupta
Director - Global Research Centre
Grant Thornton Advisory Private Limited

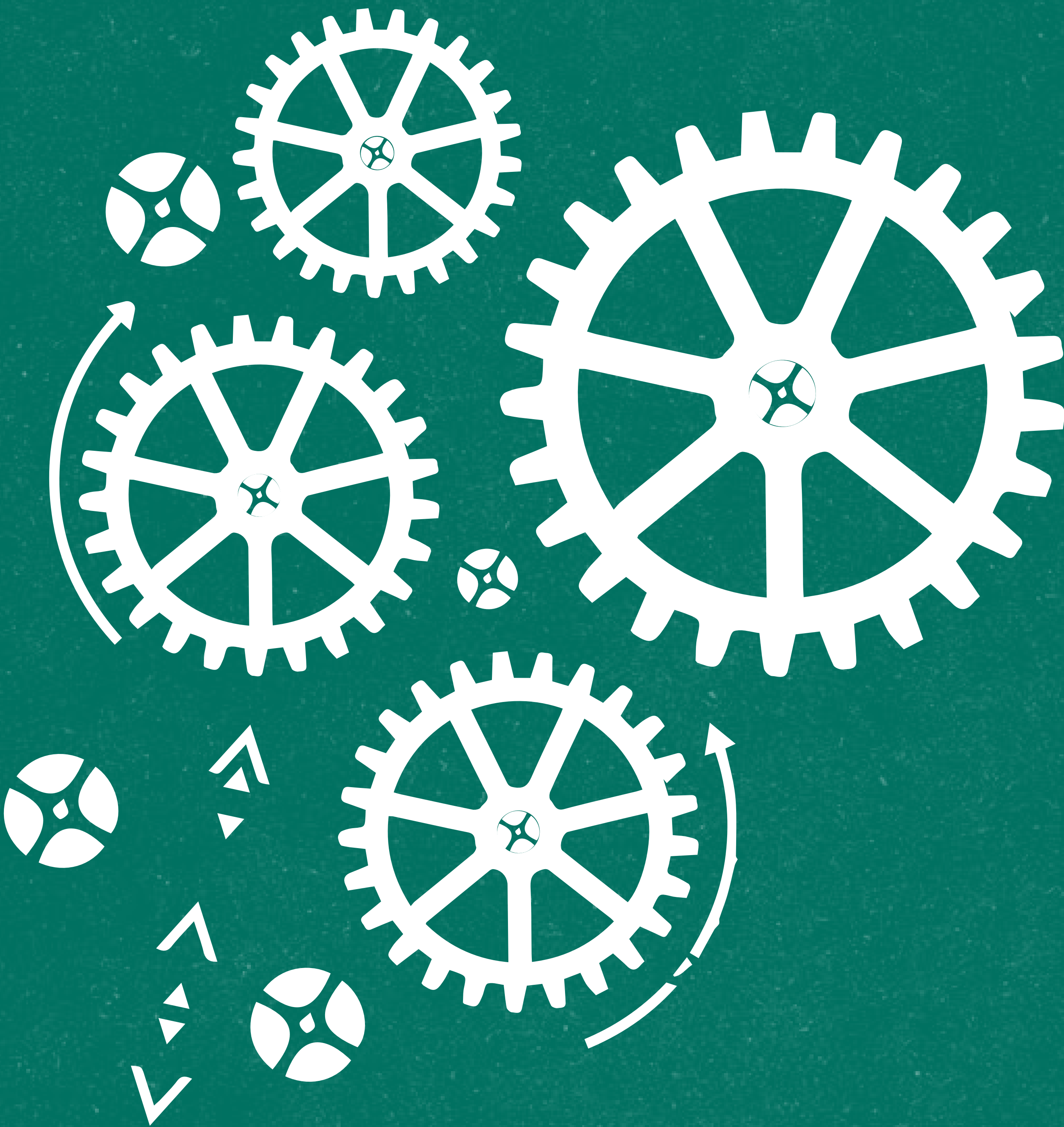
2015	2016
US$ 3.7 bn	US$ 3.2 bn
60	69

The performance of the Indian e-commerce industry is fueled by robust investment in the sector and rapid increase in internet users. The outlook remains stable yet positive.

The focus continues to be digital payments, customer-centric strategies and efficient systems. Consumer products and enterprise technology will be key areas for venture capital and private equity. However, some uncertainty may exist in the near-term due to continued economic and political uncertainties in India and the global markets. With investor sentiment remaining robust, ongoing banking reforms, and restructuring, the deal activity is anticipated to gain momentum towards the latter part of 2017.



Industry insights/ Investor speaks



Investor speaks

Shivani Bhasin Sachdeva
MD & CEO
India Alternatives Investment Advisors

1. What are your views on the PE investment activity in 2016 as compared to 2015? Volume and value reduced in 2016 – does the trend depict a cautious approach adopted by PE/VCs?

The fund raising environment in 2016 was tough that resulted in a drop in the PE/VC investment activity in 2016 as compared to 2015. The tough environment is mainly attributed to PE investment activity in early and late stage companies. These two stages have seen a sharp y-o-y decline of around 25 percent each in 2016. The growth stage, where we at India Alternatives focus on, has not seen much of a change with deals close to US$ 4 bn being executed in both 2015 and 2016.

High valuation expectation was one of the key challenges in 2016 that resulted in a lower number of deals being consummated. We expect valuations to become more realistic going forward.

In 2015, investments were made at unjustifiable valuations. In 2015, investments were made at unjustifiable valuations. Given the recent write-downs and fresh capital being raised through down-rounds, investors will remain cautious going forward. Finding the right investment opportunities across stages and sectors at a fair value will be a focus for PE/VCs this year.

2. What are the key challenges and opportunities (e.g. valuations, business scalability, profitability, regulatory changes, etc.) for the PE industry in the near term?

The consumer buying sentiment over the last few months post-demonitisation has become subdued and this has reflected in the financial results of leading consumer product companies and lending institutions. In order to revive consumer demand and achieve scalability, profitability may have to be sacrificed marginally in the first half of 2017. This shall have an impact on the performance of portfolio companies of numerous PE funds.

The budget speech for FY18 aimed at the revival of the rural economy and giving more disposable income in the hands of the middle class. With reduction in income tax rates for middle class and mass market consumers as well as for smaller corporates, we believe that there will be improvement in demand for mass market products and will lead to exciting investable PE opportunities in the mass market consumption segment.

3. What are the key sectors that can provide attractive investment opportunities for PE funds in India in the next 12 months?

With a push for a cashless economy, numerous sectors in India will experience higher growth in the organised market. A rise in disposable income, on account of various proposals made in the budget for FY18, shall increase domestic consumption spending and benefit multiple segments such as apparel, packaged foods, sanitary ware etc. Backing innovative, differentiated and quality-focussed companies in the domestic consumption space can prove to be a rewarding investment decision.

Another sector that is exciting from a PE perspective is the Indian defense sector. Continuous focus on indigenisation in the Indian defense space, a push for inclusion of private players, and multiple technology focused players being able to provide innovative and differentiated products, has resulted in the creation of fast growing companies in this space.

4. As a strategy and way forward would you prefer fresh funding in companies for organic growth or financing strategic acquisitions for companies in your portfolio?

India Alternatives operates in the mid growth space in India. It is that stage when a company has proven its competitiveness to a smaller target set and looks to replicate the business model to a larger audience. The organic growth potential for these companies is immense. In such a scenario, when there is a larger opportunity to capture and improvements are possible in terms of profitability, innovation, product offering, and delivering a superior customer experience, we would prefer fresh funding in companies for organic growth.

5. What are the major challenges faced by you in managing relationships with promoters and how are you addressing the same?

We back entrepreneurs who are aligned with us in terms of growth and governance and haven't yet faced any challenge in managing relationships with them. As I always say, "If the chemistry works, the math will follow."

6. What are the typical challenges faced while exiting portfolio companies? Also, has the investment horizon for PEs extended given India's long term macroeconomic outlook?

PPE funds typically prefer exiting portfolio companies through an IPO. Some large Indian companies have been successful in providing an exit to PEs through this route. However, the IPO route for mid-size companies remains challenging. Liquidity in Indian SME exchanges is inadequate to attract large investor interest and this restricts value maximisation for a PE fund. Even some of the larger consumer technology firms, which have disruptive business models, prefer listing on international stock exchanges such as the NASDAQ. Given the opportunities, the Indian capital market needs to grow fast in terms of width and depth by creating more awareness, acceptability and participation.

7. What are your top three asks from the Government/Regulatory perspective to help boost participation of the PE/VC industry in India's economic growth, and why?

1. Expedited clarity from the Government on Goods & Services Tax (GST). This should ideally come before the financial year end, in order to make reasonable business and financial projections.
2. Achieving a parity in terms of taxation on exit from listed and unlisted companies. The additional burden of tax for unlisted companies is one of the impediments for attracting capital.
3. Increased domestic institutional participation in PE funds. The Chinese PE market has grown tremendously on the back of strong government funding and the Indian PE market has the same growth potential if additional institutional funding support is provided. Also, to take the Startup India movement forward, the early stage companies will keep on requiring additional rounds of funding as they grow and this funding will be provided by growth stage PE funds

8. Any other matters to comment?

None

Investor speaks

Neeraj Seth
Head of Asian Credit
Blackrock

1. What is your outlook for alternative investment opportunities (such as private credit) for India?

Private credit is set to play an important role in India's growth story over the next few years. Government's pro-growth reforms will require financial sector's support in the form of credit creation. Bank credit, however, appears constrained at the moment because of capital scarcity and risk aversion – country's loan-stock-to-GDP is at its twenty-year lows versus the long-term trend. At the same time, NBFCs may face near-term headwinds due to their customers' reliance on cash transactions. In such a scenario, we expect private credit platforms to play a meaningful role in extending credit to worthy borrowers in the country.

2. What are the key challenges and opportunities for the private credit industry in the near term?

Capital expenditure by private corporates has been sluggish over the past few years due to demand side factors, and in part due to a weak banking sector. We expect government's measures such as the new Goods & Services Tax code to be supportive of demand recovery, which should drive new investments. At the same time, we expect alternative funding sources such as BlackRock's Private Credit platform to help provide flexible financing solutions to meet corporates' needs. We look forward to a successful implementation of the GST in the coming months.

From investors' perspective, the lengthy debt resolution process has historically been a challenge for credit investor in India. We expect that to change with introduction of the new Insolvency and Bankruptcy Code. The code lays out a time-bound debt resolution process and we view it as a significant positive reform for credit investors. With the first few cases filed under the new code already underway, we will be monitoring courts' interpretation of the code, and the actual time it takes for resolution.

3. What are the key areas that can provide attractive investment opportunities for private credit in India in the next 12 months?

We are seeing demand for growth capital from companies looking to invest domestically, spread across growing industrial sectors (such as renewable energy) and essential goods & services (such as education and affordable housing) where there is a lot of pent-up demand. Separately, we are also seeing demand from Indian companies pursuing overseas acquisitions. These companies typically have successful business models in India, primarily in the services space, and they are now looking to expand their footprint outside India.

4. As a strategy and way forward would you prefer fresh funding in companies for organic growth or financing strategic acquisitions for companies in your portfolio?

Not applicable

5. What are the major challenges faced by you in managing relationships with promoters and how are you addressing the same?

Indian promoters are making fast progress on institutionalising governance. This is supportive of these businesses reaching out to a global investor base, and pursuing global M&A. At BlackRock, we have supported our partner promoters to formalise standard operating procedures for key functions, and to implement proper Management Information Systems (MIS).

6. What are the typical challenges faced while exiting portfolio companies?

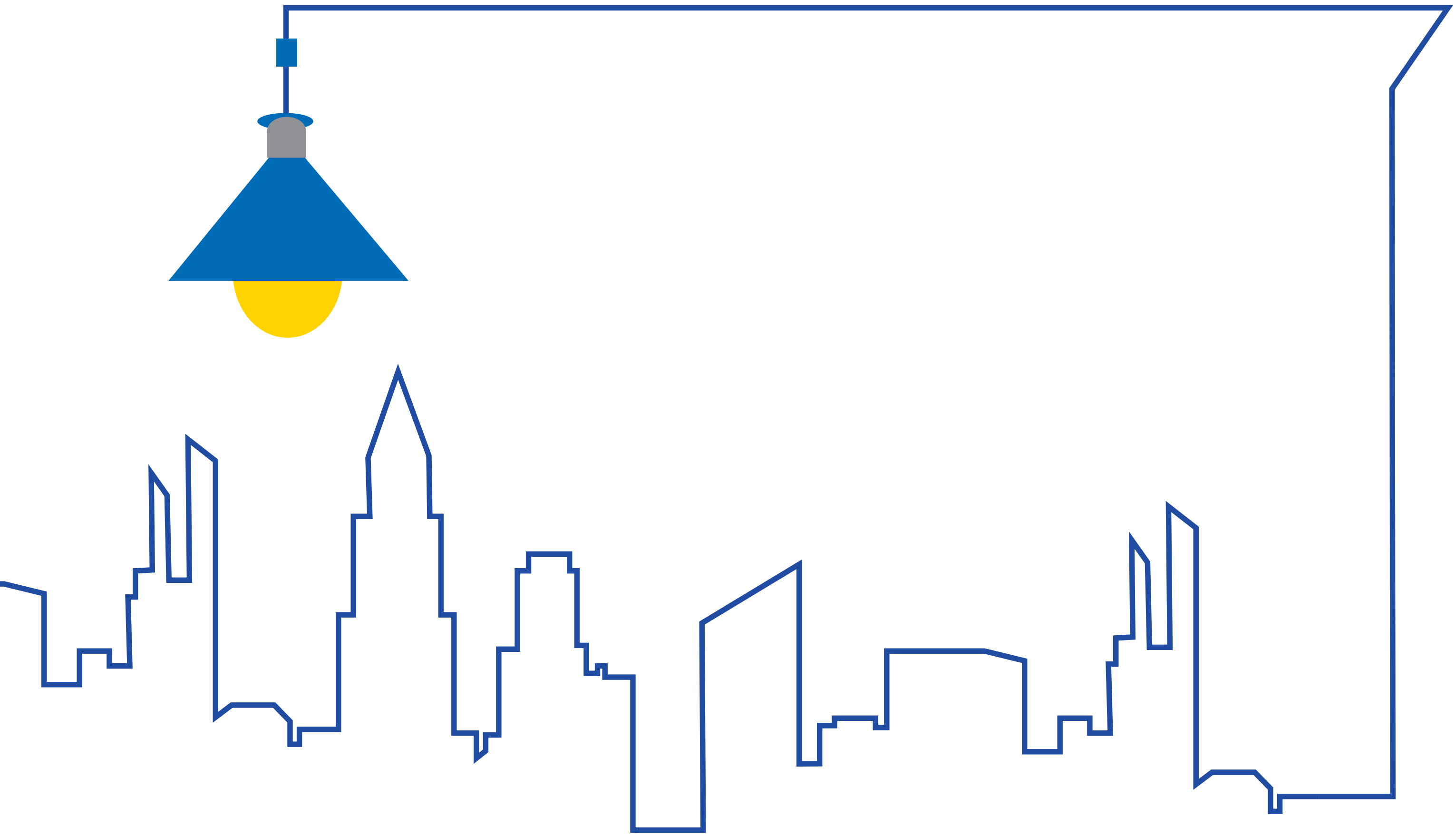
Exits may get delayed due to a number of reasons such as challenging market or industry conditions, or a delay in execution of management's plans, among other reasons. To mitigate such risks, at the outset we keep a meaningful margin of safety which acts as a buffer in challenging times. Our financing solutions are flexible and should a company's plans not work out as anticipated, we actively engage with our partner promoters to achieve the best possible outcome.

7. 7. What are your top three asks from the Government/Regulatory perspective to help boost participation of alternative credit providers in India's economic growth, and why?

We expect the momentum in growth-friendly reforms such as GST to continue, and we hope for a speedy implementation of such reforms. We expect the new Insolvency & Bankruptcy Code to meet its objectives of providing a timely outcome to debt resolution in India.

8. Any other matters to comment?

None



Investor speaks

Jinesh Shah
Founding Partner
Omnivore Partners

1. What are your views on the PE investment activity in 2016 as compared to 2015? Volume and value reduced in 2016 – does the trend depict a cautious approach adopted by PE/VCs?

a. 2016 signifies an important change in the approach by PE/VCs, as there is an increased focus on reducing the cash burn and get a roadmap for being cash break even. It seems that the industry is going back to basics to focus on sustainable growth i.e. fast growth but not accompanied by predatory loss making approach. However, I do believe that it depicts cautious approach, but an approach which is optimal and sustainable.

b. Besides, the investors have also started focussing on other sectors beyond e-commerce and food delivery, which is helping the overall ecosystem.

2. What are the key challenges and opportunities (e.g. valuations, business scalability, profitability, regulatory changes, etc.) for the PE industry in the near term?

a. Near term challenges for PE/VC sector is sustaining the valuations on the investments already done. It is increasingly becoming difficult to justify the higher valuations, especially in the light of the fact that quite a few of marquee investments have seen valuation downgrade.

b. Business profitability is becoming extremely difficult, as most of the investors followed herd mentality and there is very little differentiation in the investments made. However, this looks to be changing and the growth now seems to be following a good approach.

c. Valuation down round though is a challenge, it is an opportunity for investors who have not invested till now and this provides an opportunity to invest in good companies at a better valuation. In addition, this is forcing investors to look beyond the obvious investment areas, as it is creating a healthy portfolio diversification.

d. Regulatory changes especially with lack of clarity on GST is creating an area of uncertainty for all stakeholders. However, this is still better than what the industry has seen in the past..

e. With the US Government focussing on reducing the H1B immigrants, this will provide an opportunity to get better talent for Indian start-ups and probably, a chance to create good product tech companies.

3. What are the key sectors that can provide attractive investment opportunities for PE funds in India in the next 12 months?

a. Food and AgTech, especially precision agriculture focused on big data and IoT

b. Healthcare

c. Fintech

d. Supply chain and logistic tech

e. Education

4. As a strategy and way forward would you prefer fresh funding in companies for organic growth or financing strategic acquisitions for companies in your portfolio?

a. We would prefer fresh funding for organic growth.

5. What are the major challenges faced by you in managing relationships with promoters and how are you addressing the same?

a. Managing expectations and pushing the entrepreneurs to bring fresh managerial talent is the biggest challenge. Entrepreneurs are sometimes anxious of hiring talent; however, they understand the need to hire good people to scale up the start-ups.

b. We have been able to overcome this challenge by partnering with entrepreneurs and engaging the entire team .

6. What are the typical challenges faced while exiting portfolio companies? Also, has the investment horizon for PEs extended given India's long term macroeconomic outlook?

a. Typical challenges are to get co-investors for follow-on funding, changing course to make profits instead of burning money. However, overall scenario seems to be improving for the sectors which were traditionally ignored, as PE investors are looking to hedge their own portfolio risks, which at present seem to be skewed in favour of only couple of sectors, and are facing big questions.

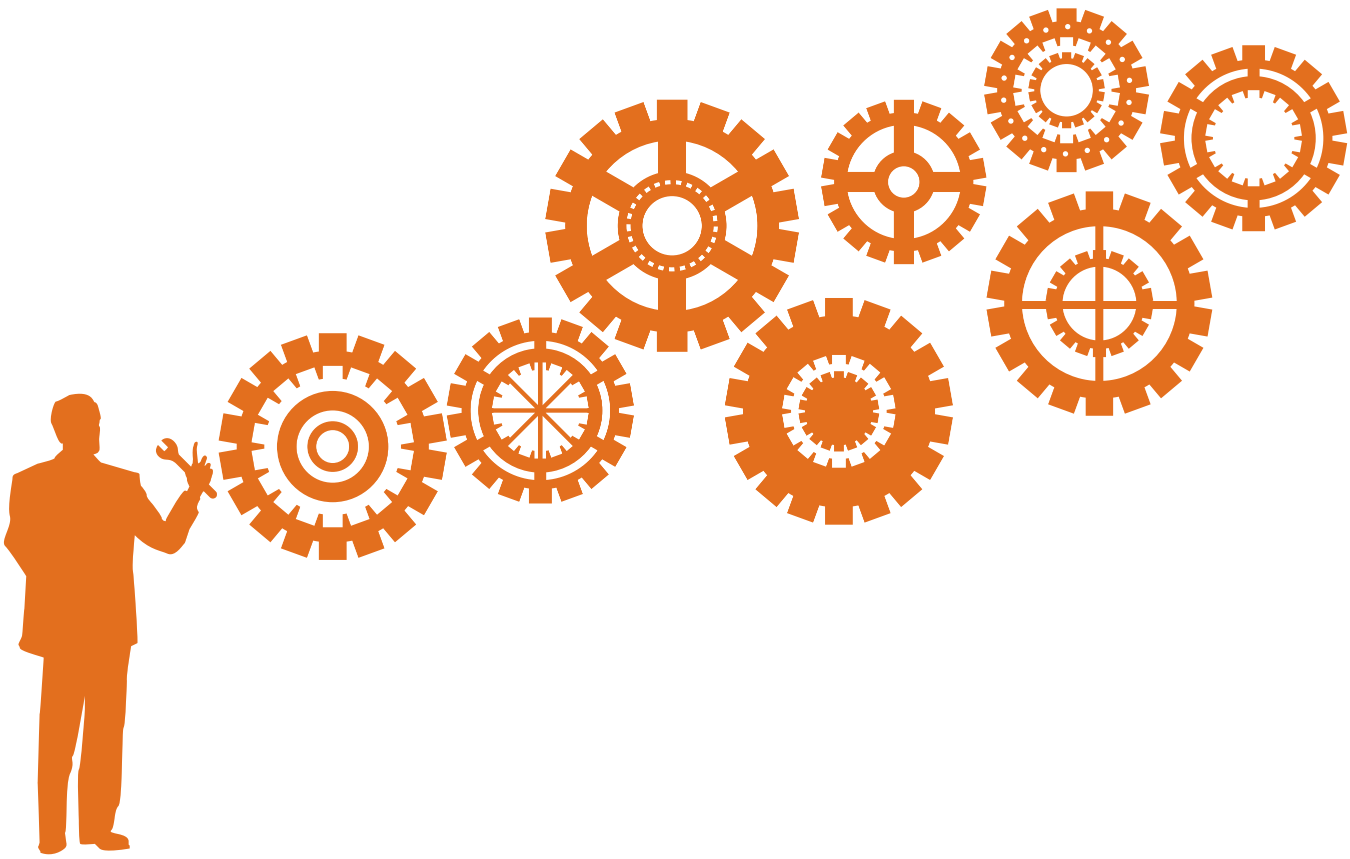
7. What are your top three asks from the Government/ Regulatory perspective to help boost participation of the PE/VC industry in India's economic growth, and why?

a. Clarity of regulations and no changes for 5 years

b. Similar to CSR initiative, if the large enterprises can be engaged to work with start-ups for their sourcing or any other kind of partnership. This can be also be seen as R&D investments by large corporations.

8. Any other matters to comment?

None



Investor speaks

Uday Garg
Founder, CEO
Mandala Capital

1. What are your views on the PE investment activity in 2016 as compared to 2015? Volume and value reduced in 2016 – does the trend depict a cautious approach adopted by PE/VCs?

This would simply be a guess, but I suspect it has more to do with the institutional investors in Europe, USA etc. reducing Indian fund commitments for various reasons and due to technical issues related to Fund commitment periods ending, rather than a cautious approach by PE/VCs.

2. What are the key challenges and opportunities (e.g. valuations, business scalability, profitability, regulatory changes, etc.) for the PE industry in the near term?

I don't have enough data on the overall Indian PE Industry but as far as Mandala, please see below in order of importance:

Challenges

- Finding multiple avenues to exit portfolios
- Scalability of business models of portfolio companies
- Regulatory changes effecting portfolio companies
- Valuation expectations Opportunities
- Investments to create sector leaders or establish sector leadership position
- Investments to substantially scale operations and transformational capital
- Infusing technology/systems to create globally competitive platforms

3. What are the key sectors that can provide attractive investment opportunities for PE funds in India in the next 12 months?

We focus 100 percent on Indian Agribusiness, which is a wide area covering everything from agri inputs to food/dairy processing, to logistics, to agri banks, to food consumer branded companies. We are finding several interesting opportunities in these sectors.

4. As a strategy and way forward would you prefer fresh funding in companies for organic growth or financing strategic acquisitions for companies in your portfolio?

We are open to both but the opportunities received have been inclined towards organic growth. Strategic acquisitions are usually something we have worked together with the promoters to evaluate, post-investment. Valuations paid for strategic acquisitions are usually the biggest consideration in such discussions.

5. What are the major challenges faced by you in managing relationships with promoters and how are you addressing the same?

Getting the promoter to stay focused/disciplined to execute the business plan, within the stipulated time frame, to provide an eventual exit to the investor, remains the biggest challenge.

This is managed by developing a set of pivots in the business early on, constant root-cause analysis and monitoring, value-addition through consultants/experts wherever necessary, clear shared vision for value creation and exit and most importantly, a sense of partnership with the promoter where there is sensitivity to the challenges of operating in the Indian environment.

6. What are the typical challenges faced while exiting portfolio companies? Also, has the investment horizon for PEs extended given India's long term macroeconomic outlook?

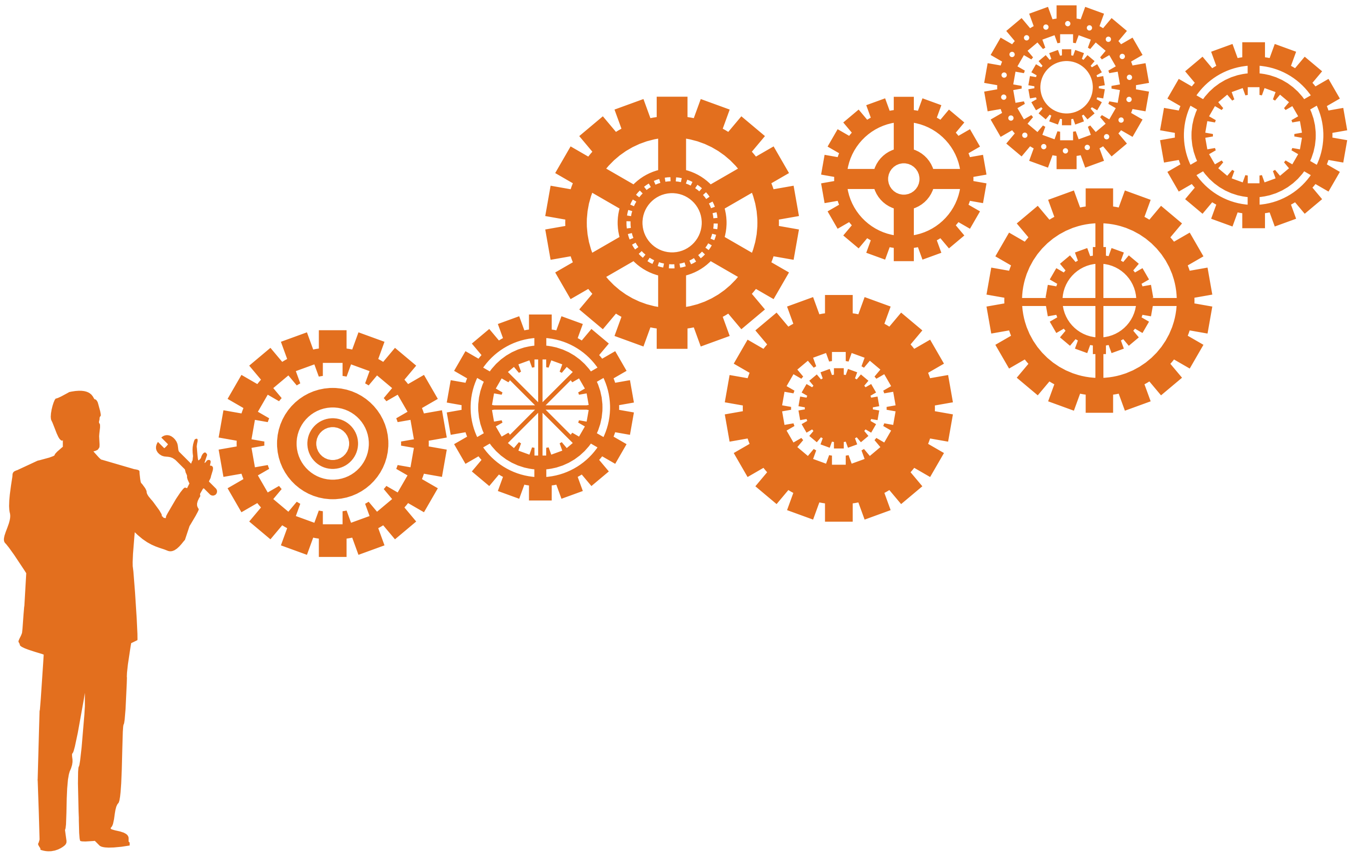
Historically, I believe the industry has had to deal with challenges on exit due to poor portfolio company performance, lack of exit options (IPO as the only option) and inability to force the company into an exit option. We have tried to address these challenges through continuous monitoring and business review, alignment of interest with promoters, structuring deals to ensure cash back and having >1 exit option identified pre-investment.

7. What are your top three asks from the Government/ Regulatory perspective to help boost participation of the PE/VC industry in India's economic growth, and why?

- Simplify and then be consistent on regulatory, tax and compliance processes
- Improve processes for bankruptcy and restructuring scenarios
- Allow more flexibility in investment structures

8. Any other matters to comment?

None



Investor speaks

Samir Inamdar
MD & CEO
PE Forum

1. What are your views on the PE investment activity in 2016 as compared to 2015? Volume and value reduced in 2016 – does the trend depict a cautious approach adopted by PE/VCs?

PE activity was muted as compared to 2015. The reasons should be searched inside out. The global events leading to increase in VUCA – Brexit, protectionism etc. – impacted the sentiments and proclivity of global funds as well as LPs to invest, especially in emerging markets. A delay in pick up in private investment in India has also affected PE investments. But in contrast to the volatility globally and especially in emerging economies, the wider Indian economy continues to be on a stable growth path with a positive outlook. The strength and stability of the Rs has been remarkable in the face of the stunning policy initiative of demonitisation. However, the sentiments in the PE/VC community in India have been impacted due to some of its own actions. The year 2015 in India was a year of momentum investing in e-commerce companies. A realisation that unreasonably high valuations were given for companies with unsustainable business models led to funds turning cautious in their approach towards further investments.

2. What are the key challenges and opportunities (e.g. valuations, business scalability, profitability, regulatory changes, etc.) for the PE industry in the near term?

The current government has done a commendable job in sorting out many sticky and festering regulatory issues. Going forward, it is the stated goal of this government to ensure stability and transparency in regulations. This augurs very well for the economy as well as business.

There is no dearth of good businesses that can scale up profitably if fund managers can look closely and deeply enough. As an investor, if you have built a reputation of being able to add value, you could drive down the expectations of unreasonable valuations.

Key challenge continues to be good, showcase exits, which is acting as a dampener on the enthusiasm of LPs about India. Although 2016 was a stellar year for exits, there is a lot more invested capital awaiting redemption.

3. What are the key sectors that can provide attractive investment opportunities for PE funds in India in the next 12 months?

The story remains as positive as the past two to three years. There is good growth in domestic consumption allowing rapid scale up of well managed businesses in manufacturing, education FMCG and related sectors. Increasing income levels, awareness and access is driving growth in healthcare sector at a fast clip. Some of the key initiatives of the current government - solar energy mission, electricity-for-all, clean India etc. – are giving a good impetus to competitive businesses in clean-tech and energy efficiency sectors. While the business models of traditional companies in India's IT/ITES sectors are under pressure due to technological advancements as well as geo-political developments, we see large emerging sub-sectors within the overall ICT – fin-tech, payments, mobile, electronic manufacturing, innovative internet models – which throw up good opportunities.

4. As a strategy and way forward would you prefer fresh funding in companies for organic growth or financing strategic acquisitions for companies in your portfolio?

We do not see this as an 'either/or' question. Depending on the situation in each company, a strategic view has to be taken on the growth path to be followed. This could include both organic as well as inorganic growth, but will also include tapping other avenues and strategies like alliances, joint ventures, geographical expansion, expansion into contiguous technology areas etc. One of the key considerations in fresh funding is the ability of the company to manage its operating cash flow.

5. What are the major challenges faced by you in managing relationships with promoters and how are you addressing the same?

We believe that a good foundation of this relationship has to be laid at the point prior to entry by filtering out wheat from chaff and ensuring a values and ethics match. An open and frank dialogue and time spent on assessing the DNA of entrepreneurs prior to investment, goes a long way in ensuring healthy relationship thereafter. Most entrepreneurs in our experience look for a strategic and operational value add from investors, which goes beyond the traditional 'opening of doors'. A healthy and mutually respectful relationship can be built if the entrepreneurs truly believe that the fund managers are adding value in these areas.

6. What are the typical challenges faced while exiting portfolio companies? Also, has the investment horizon for PEs extended given India's long term macroeconomic outlook?

There are multiple drivers towards availability of trade sale and strategic sale options. Increase in allocations by global funds as well as rapid growth in domestic investors expected in the coming years, will improve the market for strong assets. Further, with almost total liberalisation of FDI and increasing attractiveness of Indian market for global companies, strategic options for exit will also continue to improve. However, in our view, the biggest challenges to exit actually are internal to the companies. Companies which are able to execute on growth strategies, professionalise their management systems and make them transparent, build world class teams, build good technology and product offerings, will surely find eager buyers leading to easy exits for funds. Hence, we believe in focussing on operating performance of the companies.

7. What are your top three asks from the Government/Regulatory perspective to help boost participation of the PE/VC industry in India's economic growth, and why?

At an industry level, IVCA continues to take up various issues with the government and hence I would not like to add to that. In general, the only thing I will say is that a continuing push towards 'ease of doing business' reforms as well as 'ease of investing' reforms is what the government needs to drive.

8. Any other matters to comment?

None

Investor speaks

Kumar Shiralagi
MD
Kalaari Capital

1. What are your views on the PE investment activity in 2016 as compared to 2015? Volume and value reduced in 2016 – does the trend depict a cautious approach adopted by PE/VCs?

Inability to raise subsequent capital at increasing valuation by some of the unicorns has put the much needed caution into the hot market. Volumes slowed since it is not clear if exits can happen in a timely fashion especially if PE funding dries up prematurely. But profitable companies continue to attract funding assuming that basics support it.

2. What are the key challenges and opportunities (e.g. valuations, business scalability, profitability, regulatory changes, etc.) for the PE industry in the near term?

Sudden boom bust cycles, although expected to some extent, if very large, can leave a very negative impression on the ecosystem. We do not know yet how bad an impact the current cycle is going to be. Focusing heavily on profitability as a result of lack of capital at a very nascent stage will not allow companies to do the early innovation and hence will slow progress. This is particularly hard on technology and product companies that need a gestation period before they can show significant customer traction. When there is no mad rush or valuation run up, it will open up opportunities for investors to do their home work right to identify good companies to invest into. There always are many of those.

3. What are the key sectors that can provide attractive investment opportunities for PE funds in India in the next 12 months?

Anywhere there is significant inflection will create opportunities- payments, healthcare, mobile related are very interesting sectors.

4. As a strategy and way forward would you prefer fresh funding in companies for organic growth or financing strategic acquisitions for companies in your portfolio?

There is capital available if companies are making good progress, showing capital efficiency and have differentiated solutions. So, subsequent funding is still a good option for those. One would not want to sell companies prematurely but if value is right, it is always worth considering.

5. What are the major challenges faced by you in managing relationships with promoters and how are you addressing the same?

No different than what it was a couple of years ago! I had answered it then! Not a 2016/17 phenomenon!

6. What are the typical challenges faced while exiting portfolio companies? Also, has the investment horizon for PEs extended given India's long term macroeconomic outlook?

Not applicable

7. What are your top three asks from the Government/ Regulatory perspective to help boost participation of the PE/VC industry in India's economic growth, and why?

I think government should stay away from Seed/ Venture investing since it requires certain risk capital and mind set. Many failures come before successes and not sure if governments have an appetite for it. However governments and regulatory bodies can make a huge impact by facilitating and streamlining processes, eliminating corruption, setting up infrastructure, making it simpler for entrepreneurs to start companies and more importantly be able to shut down if things do not go well. In VC business, in terms of number of companies, more shut shop than become very successful. Today it is virtually impossible to easily close a company. So many entrepreneurs and VCs are left wasting huge amount of time and energy in trying to deal with those even when there is no value in managing them.

8. Any other matters to comment?

None

Investor speaks

Ajay Mittal
Director
Ascent Capital

1. **What are your views on the PE investment activity in 2016 as compared to 2015? Volume and value reduced in 2016 – does the trend depict a cautious approach adopted by PE/VCs?**

Yes there is an element of caution in the approach of VCPE industry after euphoria of 2015. The investment, particularly in e-comm/tech sector, has still to justify the valuation garnered in 2015.

2. **What are the key challenges and opportunities (e.g. valuations, business scalability, profitability, regulatory changes, etc.) for the PE industry in the near term?**

The challenges remain quality of entrepreneurs/ promoters, corporate governance, reliability of financial numbers etc. which are well within the control of portfolio companies. The external challenges include path to profitability, follow on round because of mismatch in valuation expectations etc. All of these factors ultimately affect the exits. The opportunities continue to be there for acquiring good businesses (which are otherwise struggling to survive because of lack of funds), good professionals for CXO positions etc.

3. **What are the key sectors that can provide attractive investment opportunities for PE funds in India in the next 12 months?**

Some of the attractive sectors include healthcare, pharma, financial services, technology and consumer.

4. **As a strategy and way forward would you prefer fresh funding in companies for organic growth or financing strategic acquisitions for companies in your portfolio?**

We are open to funding both the growth strategies: organic as well as inorganic.

5. **What are the major challenges faced by you in managing relationships with promoters and how are you addressing the same?**

Most of the promoters don't take their contractual obligations (such as exit to VCPE investors, IRR, ESOP to employees, appointing professional CXOs, appointing Big4 auditors etc) seriously. Further, timelines for exit can be vastly different for promoters and VCPE investors. This invariably leads to conflict. This is the biggest challenge. Therefore, it is better to do proper due diligence on promoters at the time of investment, checking their moral/ethical background, also make sure there is alignment in time of exit. Besides, there should be enough of incentives built in in the valuation structure to incentivise promoters at the time of exit. It is also necessary that there is a balanced approach in dealing with promoters from the very beginning…unlike the usual roller-coaster type of 'honeymoon phase' to 'phase of despair' relationship.

6. **What are the typical challenges faced while exiting portfolio companies? Also, has the investment horizon for PEs extended given India's long term macroeconomic outlook?**

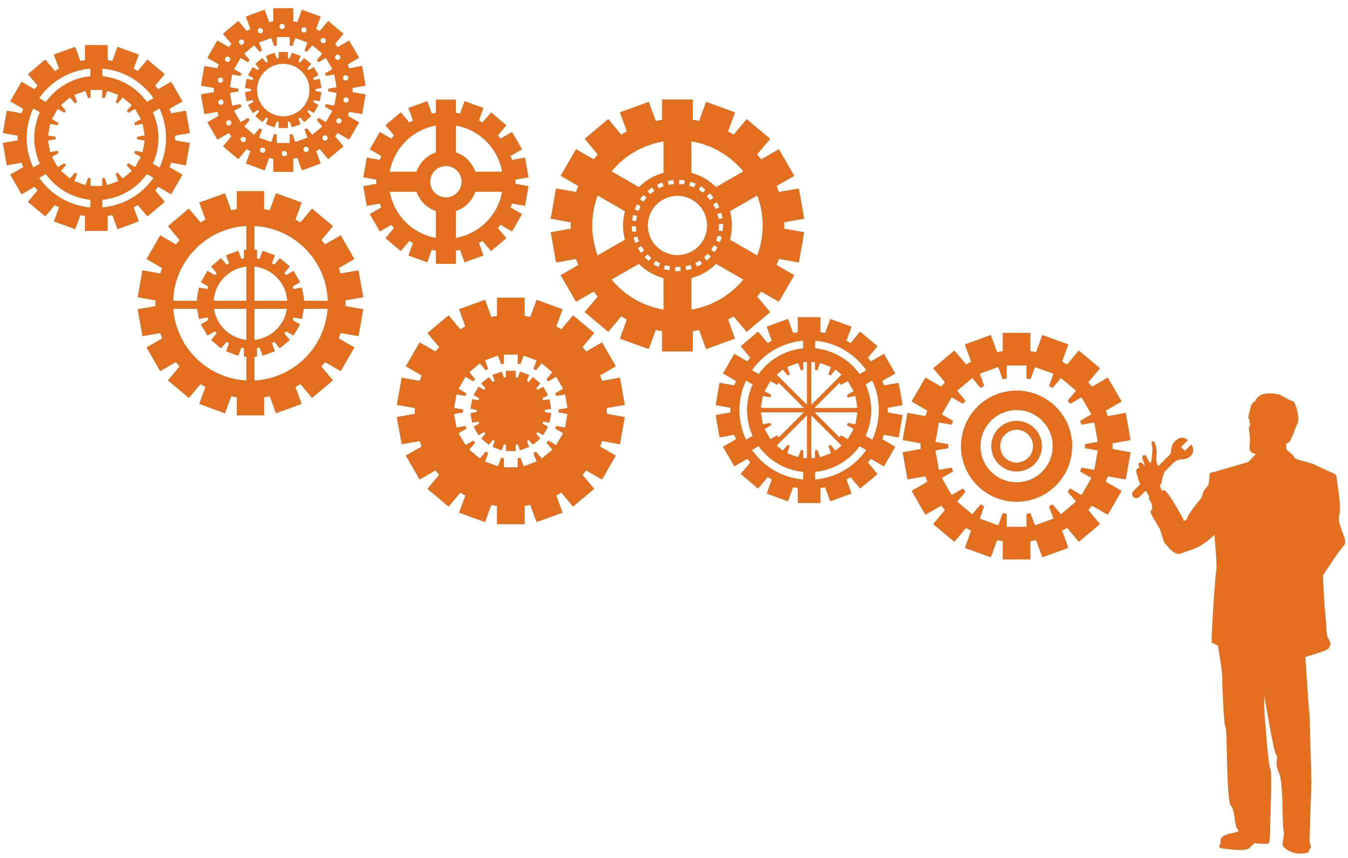
The challenges include under performance of the portfolio company leading to low valuations, non-cooperation of promoters for strategic sale, conservative projections for future outlook, refusal to hour contractual exit obligations by promoters etc. The exit time horizon have extended mainly because the exits are not coming through easily. In some cases though, the time lines have been voluntarily extended to take advantage of a visible growth in near future.

7. **What are your top three asks from the Government/ Regulatory perspective to help boost participation of the PE/VC industry in India's economic growth, and why?**

VCPE is an asset class for matured investors. Government/regulators should have no/minimal role in its regulation. If at all, the government should encourage FDI and domestic participation in this asset class by streamlining SEBI, Income Tax and FEMA regulations for smooth inflow, tax pass-through, easy redemption/repatriation etc. The government should also rationalise POEM regulations for retention of fund managers talent pool in India. Insurance and Banking regulations should be amended for easy participation by these institution (insurance companies and banks) in this asset class

8. Any other matters to comment?

None



Investor speaks

K K Rathi
Managing Director
IndiaNivesh Fund Managers Private Limited

1. **What are your views on the PE investment activity in 2016 as compared to 2015? Volume and value reduced in 2016 – does the trend depict a cautious approach adopted by PE/VCs?**

The PE/VC industry is increasingly realising that in the recent past, businesses were being very richly valued based on overestimated growth assumptions. Additionally, several funded starts up have not been able to deliver on projections. At macro level, the economy did not grow as well as expected impacting the growth in general. Generally exuberant VCs have certainly become cautious in face of such ground realities.

2. **What are the key challenges and opportunities (e.g. valuations, business scalability, profitability, regulatory changes, etc.) for the PE industry in the near term?**

Key challenge is to deliver on the high growth expectations in view of a moderating economy in the near term. The existing business models are going through a churn to manage this situation. The valuations are still ahead of the growth curve forcing rethink on new investments.

With favourable regulatory changes and medium term business outlook continuing to be bullish, there are opportunities for keen investors. Entrepreneurial activity continues to be high in the country with new and innovative business models coming through though they need greater scrutiny and diligence.

3. **What are the key sectors that can provide attractive investment opportunities for PE funds in India in the next 12 months?**

Promising sectors continue to be consumer facing businesses focusing on digital technology and new age customers. Infrastructure and logistics will be other key sectors.

4. **As a strategy and way forward would you prefer fresh funding in companies for organic growth or financing strategic acquisitions for companies in your portfolio?**

While organic growth will remain the preferred route for growth, it is clear that a whole lot of consolidation opportunities are emerging which can be used selectively to foster efficiency and scalability.

5. **What are the major challenges faced by you in managing relationships with promoters and how are you addressing the same?**

Promoters are generally very optimistic about their prospects. The main task is to keep them grounded. This is possible only by spending quality time with them more frequently, keeping discussions objective and focusing on the near term objectives, all to help in achieving the long term goals.

6. **What are the typical challenges faced while exiting portfolio companies? Also, has the investment horizon for PEs extended given India's long term macroeconomic outlook?**

Main challenge is to achieve sustainable growth path for the business, which makes it attractive for the incoming investors, else valuation expectations have to be compromised. The long term outlook for India is quite positive, therefore the PEs need to focus more on creating value than extending the time horizon.

7. **What are your top three asks from the Government/ Regulatory perspective to help boost participation of the PE/VC industry in India's economic growth, and why?**

PE/VC should be given special treatment in line with international practice in investing and exit both in terms of taxation and flow of capital. Therefore, stability in taxation regime is a must with no restrictions on flow of capital

8. **Any other matters to comment**

None

Investor speaks

TCM Sundaram
Founder & Managing DirectorIndiaNivesh
IDG Ventures India Advisors

1. What are your views on the PE investment activity in 2016 as compared to 2015? Volume and value reduced in 2016 – does the trend depict a cautious approach adopted by PE/VCs?

At a high level, most of the regular investors in the industry continued investing thru' 2016 though with caution and high bar for the companies that they invested in. The total investments are lower in 2016 (than 2015) due to lack of large investments US$ 500 mn+ from hedge funds, strategic and occasional investors. This is a natural reaction to the euphoria of 2014 and 2015 when large funding rounds were done at high valuations before the underlying company performance could justify such valuations. Now the investors are waiting for the dust to settle down and the underlying company performance to either justify the valuations given or to correct the same based on the actual performances.

2. What are the key challenges and opportunities (e.g. valuations, business scalability, profitability, regulatory changes, etc.) for the PE industry in the near term?

Key challenges are in terms of scalability of business on a sustainable, profitable manner. Especially in the consumer/ecommerce segments, the key challenge is to find the next stage of growth on sustainable basis going beyond the first 60-70 mn consumers for whose wallet share disproportionate amounts are being spent by the top 2-3 companies. With respect to 2017 the opportunity for the PE/VC investors is in find value investment opportunity from Series B to Series E rounds to back market leaders. Investors should be wary of following the flavor of the quarter approach to avoid over investing in sectors which will bring grief in return of capital as well as return on capital.

3. What are the key sectors that can provide attractive investment opportunities for PE funds in India in the next 12 months?

Software/SaaS is a sector that is seeing strong potential as well as significant interest from PE/VC investors who have not invested much in that sector. The Healthtech sector opportunities based on technology disruption are an attractive investment opportunity

4. As a strategy and way forward would you prefer fresh funding in companies for organic growth or financing strategic acquisitions for companies in your portfolio?

In the early stage investment eco-system, it is important for companies to grow organically. However, we have come across great opportunity for the market leaders to acquire some of the smaller companies to consolidate their market leadership as well as improve profitability due to scale benefits as well as reduction of uneconomic competition.

5. What are the major challenges faced by you in managing relationships with promoters and how are you addressing the same?

Not applicable

6. What are the typical challenges faced while exiting portfolio companies? Also, has the investment horizon for PEs extended given India's long term macroeconomic outlook?

Finding quick exit continues to be a major challenge in the process of exits. The investment horizon in India has always remained between 5-8 years from entry depending on the round/stage of the investment at the time of initial investment. The scale and profitability to achieve a successful public issue/offer has gone up in line with the market dynamics which tends to extend the holding period for the investors. The sense that investment horizon has extended for PE/VCs is more due to the hope that the period would come down which has not happened.

7. What are your top three asks from the Government/ Regulatory perspective to help boost participation of the PE/VC industry in India's economic growth, and why?

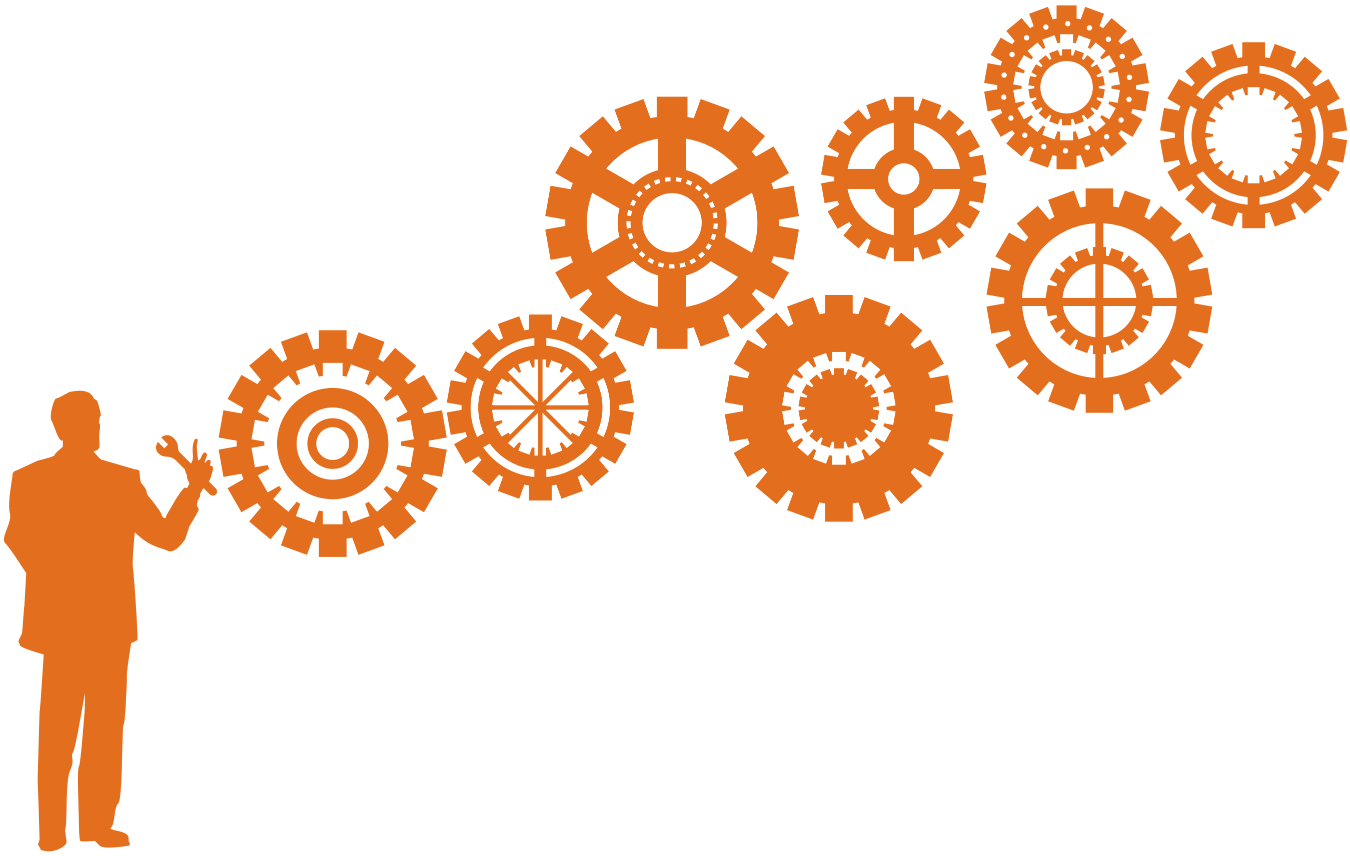
a. To bring PE/VC investments under FDI/AIF regulations at least on par with the FPI investments in listed companies. There are many reasons for this including the fact that most times FDI/AIF investments go in to the companies to create new jobs while most times FPI investments tend to be in secondary markets which don't necessarily to create new jobs;

b. Domestic AIF investors currently pay Capital Gains tax at rates higher than applicable to offshore investors as well as public market investors. This anamoly should be fixed to encourage more early/ growth capital to be raised from domestic investor sources.

c. Regulatory clarity and consistency for the life of the funds. For e.g. while some clarity has emerged in terms of taxation of investments made by off-shore investors after Apr 1, 2017, the differing opinions on GAAR and POEM continue to have some cloud of uncertainty on the tax situation.

8. Any other matters to comment

None



Grant Thornton view

Tax & regulatory developments and expectations from a PE perspective

Ravi Mehta
Partner
Grant Thornton India LLP

Private Equity ("PE")/Venture Capital ("VC") remain one of the cornerstones for India's growth story, providing valuable capital (including risk capital) to Country's businesses. The PE/VC funding has been valuable for several Indian businesses for undertaking their expansion initiatives, and also remains critical for the Indian Startup sector. Despite the lukewarm macro-economic situation, PE/VC continues to believe in India's growth story and the country did witness several big ticket investments (>US$ 50 Mn) deals in 2016.

Government Initiatives so far

The Government too on their part, have remained focused in encouraging foreign investments into the country, and facilitating ease of doing business in India. The key 2016 initiatives include:

- Several key policy amendments such as relaxing some key FDI norms for e-commerce companies, ARCs, trading in agri-products, pharmaceuticals, etc.
- Renegotiation of tax treaties with Mauritius, Cyprus and Singapore while grand-fathering the investments made upto 31 March 2017 (i.e., the capital gains arising from sale of those investments even after 31 March 2017 remain non-taxable in India).
- Bringing clarity in several tax areas such as income characterisation from sale of listed and unlisted securities, holding period for debentures, rules on Place of Effective Management ("POEM") and General Anti-Avoidance ("GAAR"), etc.
- Notification of Indirect transfer rules (although there remained areas which concerned Foreign Investors, and Government have made serious endeavours to address these concerns)

Harping on the same Government-thrust, the PE/VC fraternity expected some key reforms in Budget 2017, which can facilitate maintaining the investment momentum in the country.

Budget 2017 – key proposals

The Finance Bill 2017 contained some key proposals which could impact the M&A, corporate reorganisation and fund raising going forward. These broadly cover:

- Conversion of Preference Shares (Compulsory or Optionally) to Equity Shares is now proposed to be made specifically an exempt transaction. Even the tax basis and holding period of Preference Shares are proposed to be rolled over to the equity shares. Convertible Preference Share is an important instrument largely used in PE/VCs transactions, esp. for their investments in startups, and hence, this amendment is a welcome move to put to rest any potential controversy emanating out of the conversion of such shares.
- Exception to specified FPIs registered as Category I and II on applicability of indirect share transfer provisions, so as to avoid multiple taxation. It may be noted that the Finance Minister had mentioned in his Budget Speech that indirect transfer provisions also would not apply on redemption of shares/interests outside India arising consequent to redemption/ sale of investments which has already suffered tax in India. However, no amendment is proposed in the Finance Bill to this effect. Possibly, an amendment or notification on the part of the Government would be expected.
- Abiding by the BEPS proposals, thin capitalisation provisions are being proposed to be introduced for the first time in the Indian Tax law. Under such proposals, the deduction of interest in the hands of an Indian borrower on loans from a non-resident related party would now be restricted to 30 percent of former's EBITDA. The provisions also contain a safe harbour test (apply only to interest payments exceeding Rs 1 crore) and a roll-over eligibility (viz, unabsorbed interest can be rolled over next 8 years for offset against future profits, subject to adherence of thin cap limits). The related party loan is also proposed to cover a third party loan, where a related party has acted as a guarantor or a depositor to the Lender. This is an important development which, once enacted, could fundamentally change the manner in which MNEs determined the Funding

Structures for their Indian operations. It may also require those Foreign Parents who have largely used debt instruments to leverage their Indian operations, to revisit their existing funding structures to factor-in this development.

- The Gifting provisions under S. 56 are proposed to be expanded to cover any property (including shares) transaction by any person either without or for inadequate consideration. So long it had been restricted to only cover Individuals and HUFs, and Corporates for select transactions in shares. Likewise, specific computation mechanism is proposed to be introduced for valuation of unquoted shares for determination of its capital gains. Both these developments could have the potential of increasing the tax incidence in case of internal reorganisations.
- In the last budget, the Additional Dividend Tax of 10 percent was introduced for three categories of resident investors - individuals, HUFs and Firms (both limited and unlimited liability partnership firms)- if their dividend receipts exceeded Rs. 10 Lakh. Now, the Finance Bill proposes to expand the coverage by resorting to an exception method. So any resident shareholder, except for a domestic company, specific institutions and charitable institutions/trusts, is now included. This means seven non-exempt private Trusts (family trusts or otherwise) or Co-operatives may possibly have to shell out the extra 10 percent Additional Dividend Tax.
- There is a proposal to restrict the offset of foreign tax credits against MAT and AMT, to the extent of Indian tax liability that would have been determined had the underlying income been subject to normal tax provisions. Basis the proposed amendment, the MAT Credit available to the Indian company for carry forward would need to be reduced to the extent - the FTC claimed against MAT exceeds the FTC that would be have been availed had it been subject to normal provisions. What remains unclear is what would happen if a company is subject to MAT because of losses under normal provisions.
- Also, bringing MSMEs of Turnover of upto Rs. 50 crore within the 25 percent Corporate tax regime, amendments in tax concessions for startups, including the roll-over of their losses in the initial 7 years, and enhanced MAT credit period from 10 to 15 years could effectively contribute improving the valuations of Indian businesses looking for capital funding
- Extending the concessional withholding tax benefit of 5 percent on ECB and Masala Bonds interest upto 30 June 2020 provides fund-raising avenue for the Indian businesses
- Extension of the base year for Cost Inflation Index to 01/04/2001 (Previously 01/04/1981) improves the tax efficiency of a transaction, and is a welcome move
- Proposal to abolish the FIPB is a positive development which will go a long way in facilitating the Government's agenda of 'ease of doing investments/transactions'.
- Partial roll-back of Long Term Capital Gains (LTCG) exemption on listed equity share transactions, where the Seller has not paid Securities Transaction Tax (STT) on acquisition made post 01 October 2004. The Memorandum states the proposed amendment to be an anti-avoidance measure from the Government. However, this could have an adversarial impact if it engulfs genuine restructuring transactions. The amendment states the Government's commitment to notify an exception list for genuine transactions. We believe that this list would need to be extensive enough to ensure that transactions with bona fide commercial/business rationale do not fall within the purview of this amendment.

Key Expectations which still remain unattended

Some of the key areas where a clarity from the Government was expected in Budget 2017, but which remain unattended:

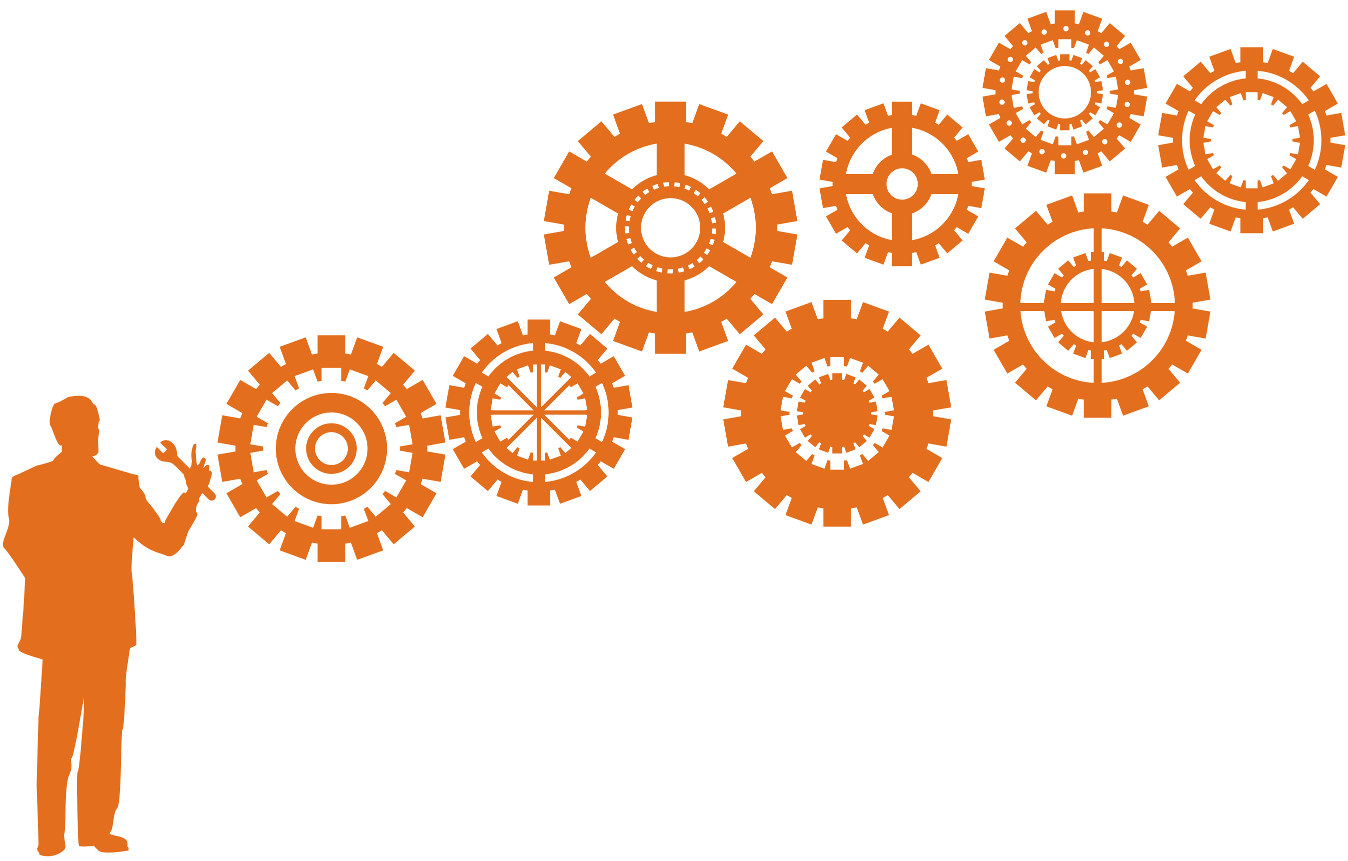
- Making an exception on taxation of startups for the premiums received from Angel investors. Recently, several start-ups received notices for the taxation of high premium received in their fund rounds, when there was a subsequent mark-down in their valuations. An amendment or notification in S.56(2)(viib), making an exception for startup Companies, is the need of the hour, if the Start-Up initiative and entrepreneurship are to be encouraged.
- Given that the POEM rules have just been introduced, the PE fraternity expected a breathing period to analyse and digest the impact thereof. However, the deferral of applicability of POEM rules remains a miss, and technically becomes applicable effective April 1, 2017.
- Most of the PE/VC investments do not involve any significant involvement in management and control of the Indian target. Hence, increasing the indirect transfer exception threshold from 5 percent (existing) to 26 percent in case of such investments (not involving management and control) made by PE/VC is a much-awaited expectation, which did not see the light of the day even in the current Finance Bill.
- As a step forward in its 'Start Up India-Stand Up India' agenda, there was an expectation for

Government to lengthen the Tax Holiday period from current 'three out of initial five years' to a longer period (eg. 7 years) for facilitating them some recovery from the initial substantial cash-burn. cash-burn. However, the same still remains a dream.

- There was also an expectation that to encourage mobility of funds, the holding period for Start Up investments be reduced from two years to one year to classify as a long-term. However, this too has been left out in the current Finance Bill
- • One of the key cost elements that has discouraged the relocation of off-shore funds (India-focused) to India is the applicability of Service tax @ 15 percent on the management fees charged by the domestic fund managers to these Funds. These have remained a key deterrent discouraging the relocation, since the management fees charged to a fund located outside India is exempt from Service tax. The current Budget fails to address this bias, and would continue discouraging the relocation initiative of bringing these Funds into India.

Summary

On a holistic basis, it has been a decent effort on the part of the Government to provide tax boosters such as extension of 5 percent concessional WHT rates on ECBs/Masala Bonds, CII base year extension to 1/4/2001, tax neutrality on masala bond transactions between non-residents, as well as clarity on the tax neutrality to preference shares conversion, that could encourage investments. At the same time, it has thrived to meet up with the global standards by introducing thin-cap under the India tax law, and plugging some of the loose-ends in the existing law such as gifting provisions, additional dividend tax provisions, which they believe, was leading to revenue leakage. Bringing MSMEs within the 25 percent Corporate tax regime, improving tax concessions for startups and enhanced MAT credit period could effectively contribute improving the valuations of Indian businesses looking for capital funding. In nutshell, a well-balanced effort on 3 core aspects – Transparency, Growth and Prudence.



Startup insights from a growth accelerator perspective

Vidhya Shankar
Executive Director
Grant Thornton India LLP

For the burgeoning Indian start-up eco system, 2016 has been one of many ups and downs – the significant mark down on valuation/write-offs of Unicorns, consolidation of the on-demand market place start-ups, the rise in B2B funding, the overall slowing down of investments in startups to some exciting shifts in the Fintech space on the back of interoperable India stack.

Despite the fall in total investments from nearly US$ 5bn to about US$ 3bn in 2016, the total volume of investments has actually increased by 8 percent from the past year. This is a very encouraging sign for the innovation economy given that 74 percent of the investments have been in the series A/pre-series levels – attributed to the evolving capabilities of the founders, maturity levels of business models with sustainable valuations and more importantly a huge increase in Angel/Seed stage investments resulting in higher potential start-ups funded.

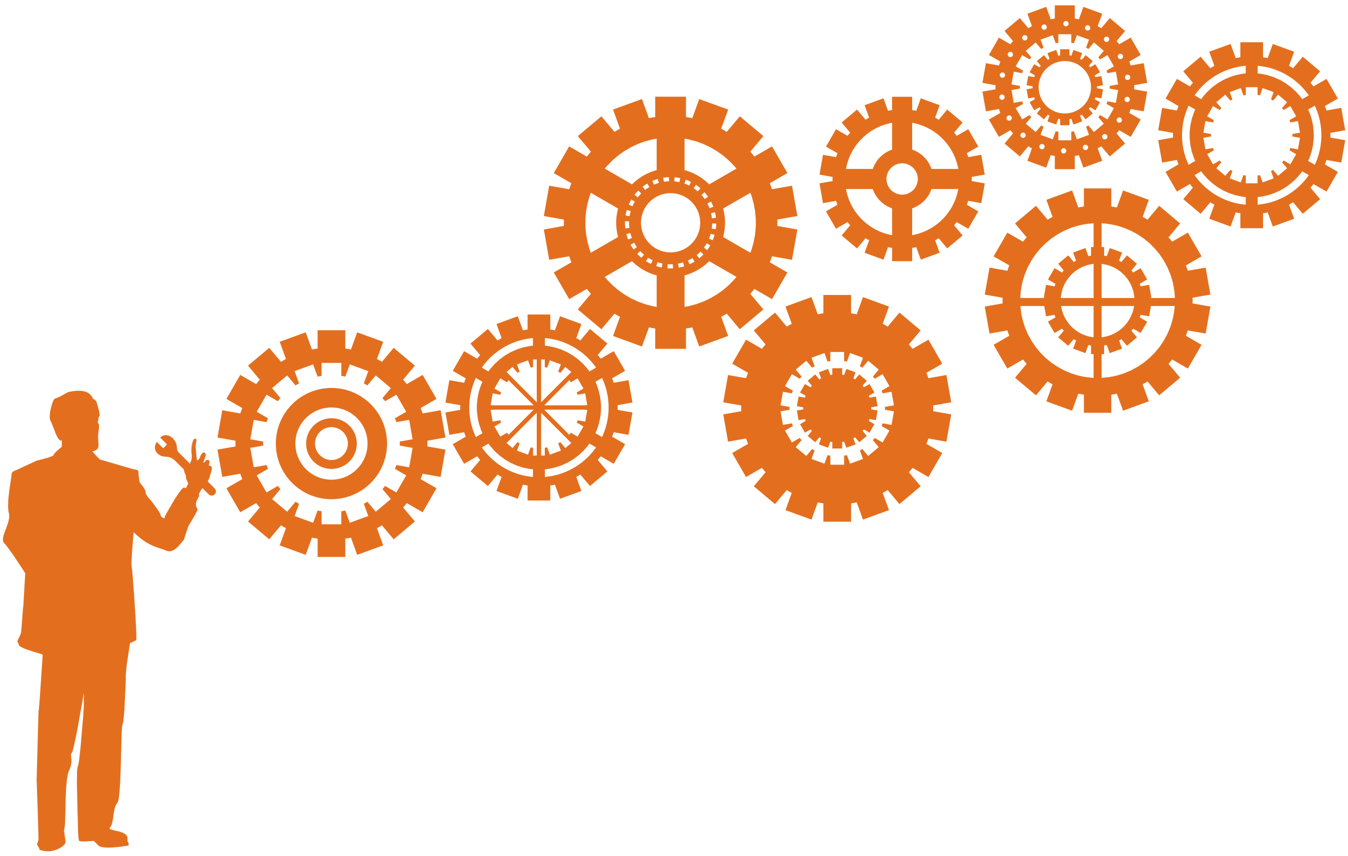
And, it is no surprise to see the continuing growth in B2C sector investments, with nearly 500 mn new smartphone users expected to enter the Indian economy by 2020, according to Ministry of I&B. With the total number of technology startups touching about 4750 as per Nasscom estimate, the B2B sector is seeing a rise in investments particularly in the Enterprise applications and infrastructure space garnering 55 percent of the about 1.2 bn worth B2B investments. This augurs well as Corporate Accelerators and Open Innovation platforms are increasingly being adopted in various forms – some choose the Corporate Venture Capital route like Intel Capital, Cisco Ventures, Amex ventures etc., while others opt for the growth accelerator format like Microsoft Ventures, Target Accelerator etc. At the end of the day, the Indian entrepreneur gains a lot through product validation, market access and strategic investments to boost the prospects. It is indeed very encouraging to see the launch of Brigade group's Real Estate Accelerator Program (REAP) and Lodha Group its own initiative to tap innovation. Coincidentally, the real estate sector in 2016 saw a 55 percent increase in investments – the acquisition of Common Floor by Quickr and the mark down of Housing.com being some other highlights. Combining the impact of technology in this area with last mile connectivity/on-demand services, the widespread adoption of sharing economy fuelled by increasing urbanisation - Urban Infrastructure as a category would emerge to be a highly lucrative investment option catering to the growing middle class and young workforce of India leading to a large addressable market.

With the emergence of ubiquitous connectivity & mobility, 2016 saw a whopping 11 times rise in Data Analytics & AI investments amounting to US$ 577 mn from a just US$ 47 mn previous year chiefly due to M&A. It's truly a time of reckoning given the increasing digitisation and the impending Singularity attributed to large scale IoT adoption with connected devices expected to be 6 times more than human beings alive as of 2020.

Expect 2017 to be a year of continued consolidation – the expected mortality rate overall is about 18-20 percent per Nasscom estimate and that the average size of VC deals has come down by nearly 50 percent suggests challenging times for startups either due to down rounds or significant adaptation to their growth plans involving cost-cutting, lay-offs; some cases creating already shorter runway shorter indicating an all-round rise in M&As in both enterprise and consumer spaces. Also, the launch of new funds by Micromax, RPG group, Hero Corp. services will spurt action from the Indian LP in addition to the significant dry powder cached with Sequoia Capital, Blume Ventures, Accel Partners and IDG ventures. It remains to be seen the effectiveness of the Start-up India plan if a lot more qualify for tax benefits or gain from the fund of funds; the influence of large corporates (particularly BFSI sector) in shaping the innovation economy can't be discounted; there are almost 1400 registered fintech start-ups in India – the effect of demonetisation and beyond remains to be seen, nevertheless, there exists medium to long term significant opportunities for financial services in Mutual funds, Insurance and Credit related product distribution.

With increasing digitisation, the prevalence of IoT and AI will continue sky rocketing in the coming days – smart startups that are product driven and IP focused will certainly edge past the 'me-too' founders to ride the wave of disruption witnessed in every industry, business sector across global markets. As it would become apparent, fledgling businesses (Davids of the start-up world) and established business (Goliaths of the corporate world) will have to collaborate, as more often complementary partnerships determines the future trajectory of meaningful innovation be it in democratisation of genomics led health & wellness; advances in machine learning leading to high level of automation; prevalence of sharing economy and the changing nature of jobs led economic livelihood. Of course, the government and public sector is pivotal to the future of innovation led economy as the pace of rapid change demands seismic shifts in policy making doing away with the incremental prescription..

Identifying the driving forces of change while continuing to emphasise on holistic development, protection of environment, boosting productivity of the agrarian economy would help a long way in not just poverty alleviation but overall higher standards of living. Clearly, the startups that cater to the bottom of pyramid through Edutech, Fintech, Healthtech and Agritech will scale up to be true unicorns bringing home the benefits of revolutionary science and technological development.



Safeguard the deal

Samir Paranjpe
Partner
Grant Thornton India LLP

"Look before you leap" is a standard adage which holds true when it comes to making investments in portfolio entities. To further add to the saying, still don't take the elevator once you've "looked" and "leapt"!

The nature of investing is such that there would be some successes and some failures. However, investors are willing to stomach losses due to an investment call going wrong or due to genuine business issues. What tends to keep them awake at night – especially in emerging markets – is the spectre of losses on account of fraud, misconduct or misappropriation in their portfolio companies.

However, to avoid this, there are certain red flags – whether during the pre-investment diligence or post investment that should ring the alarm bells:

- Withholding facts: The portfolio entity exhibits hesitancy in sharing complete details;
- Government presence: Majority of the portfolio entity's dealings are with the Government;
- Consistency in business performance: While consistency in business performance is a good sign, a near about consistency across all years may also mean that the financials need a deeper review; and
- History of internal issues: Lastly, a history of internal issues and conflicts with third parties is a definitive indicator that all is not well.
- If multiple members across different branches of the family tree are all involved with the portfolio company, it might indicate that a certain amount of inter-personal stress – either immediately or in the future - is inevitable

While the essential question remains that whether the investors can trust the portfolio entities or not, a detailed scrutiny rather than a checklist tick approach would give essential insights to take an informed decision.

Pre-investment stage:

Though most investors carry out a structured due diligence exercise, it is important to be aware of certain facts:

- Whilst public domain searches comprising of reviews on specialised and advanced database reveal essential details about the entities such as other business interests, employees' perception about the management of the entity, involvement in litigation cases, indications of poor business performance etc., it needs to be noted that in case of startups or newish Indian businesses, there is very little information that is available in the public domain.
- In such cases and in investments in the SME sector, discreet market intelligence enquiries with various stakeholders such as customers, vendors, employees and competitors would give us far more inputs than what is envisaged.
- There is no better tool than a detailed forensic review consisting of steps such as advanced data analytics, review of financial ratios, deep dive testing of transactions with vendors, customers and related parties that can help to effectively discern the current and past performance of the entity.
- Other mechanisms such as reviewing the whistle blower complaints and other internal audit reports throw light on the potential problems that are bubbling beneath the surface.

All these mechanisms put together help to give a complete view of the potential investee company to the investor

Post investment stage:

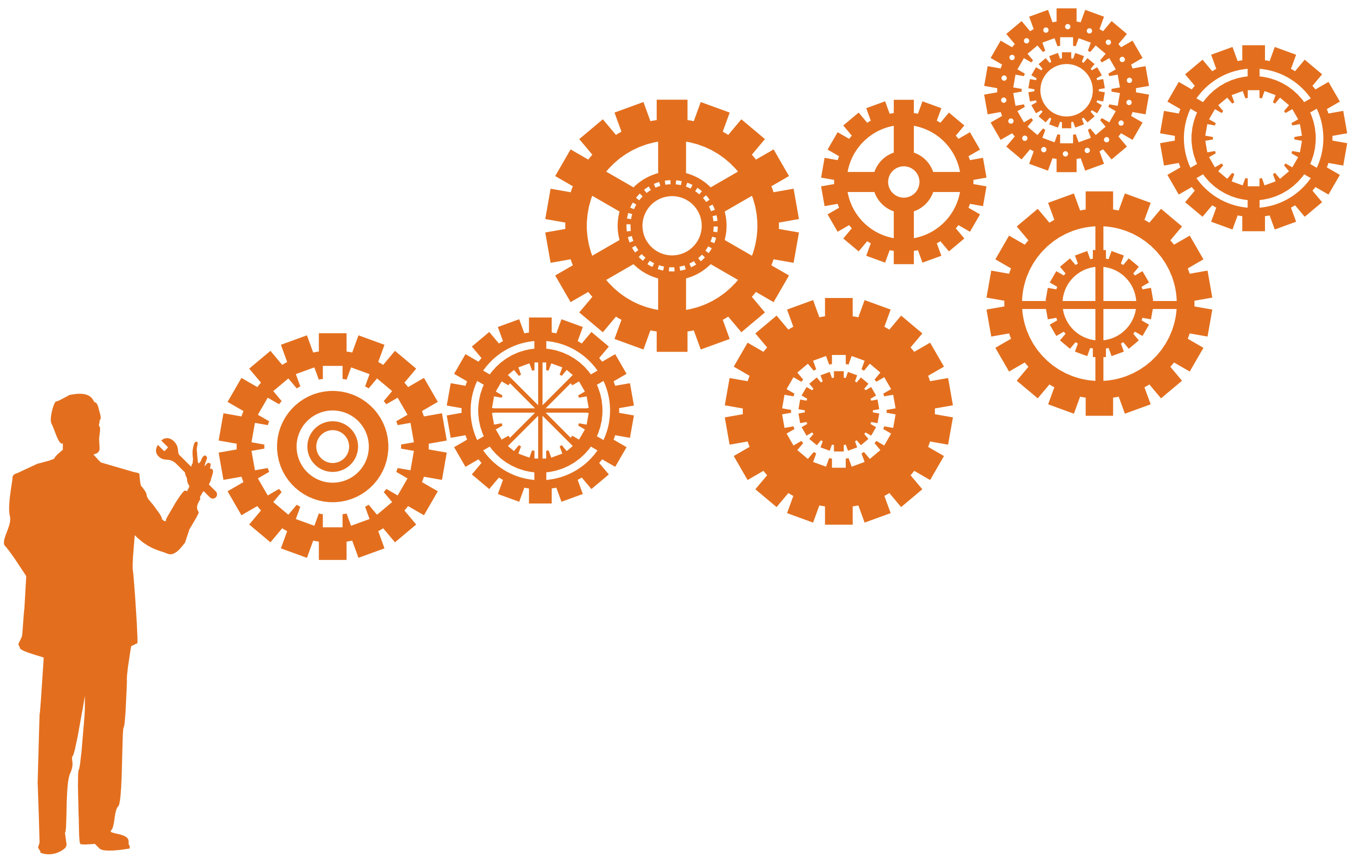
The deal doesn't end with the transfer of funds. Investors need to stay involved; keep the dialogue going and can protect the deal from going sour by adopting periodic vigilance measures consisting of the following:

- Structure the MIS and other documentation requirements better. Once it has been better structured, please read the MIS and other reports diligently.
- Periodic reviews of the cash flows, business performance including revenues and expenditures to ensure that business is moving in the right direction.
- A comprehensive fraud risk assessment exercise on the portfolio entity would serve a dual purpose by enabling the portfolio entity identify gaps in their control framework and assist in ensuring more robust processes. Secondly, such a review could also function as an early warning signal system to the investor and will help highlight any potential indicators of misconduct.
- Nudging the management of the portfolio companies to put in place an effective policy framework as well as measures like whistle blowing mechanism to provide a forum to employees and other entities associated with the company to highlight issues/ concerns.
- Building an effective oversight and control mechanism
- Meeting senior management team of the investee companies on a regular basis

Any issue identified either through whistle blowing channels or otherwise should be thoroughly investigated so that the impact can be contained in a timely manner.

Timely and focused measures would prevent the investor and portfolio entity from being embroiled in disputes later which result in lengthy and expensive litigation suits.

Taking risks is an intrinsic part of investing however, let the risk be on the quality of the asset or the price or the business and not on the level of diligence that is exercised by the investor.



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Grant Thornton Team

Our Corporate Finance practice comprises 100 senior multi-faceted specialists experienced in providing end-to-end solutions


Vishesh Chandiok


Harish HV


Raja Lahiri


Siddhartha Nigam


Sridhar V


Dhanraj Bhagat


Prashant Mehra


Sumeet Abrol


Darshana Kadakia


Rahul Kapur


Ashish Chhawchharia


Vrinda Mathur


Vikarth Kumar


Chetan Khandhadia


Manish Saxena


Santhosh C


Gautam D


Abhay Anand


Pankaj Chopda


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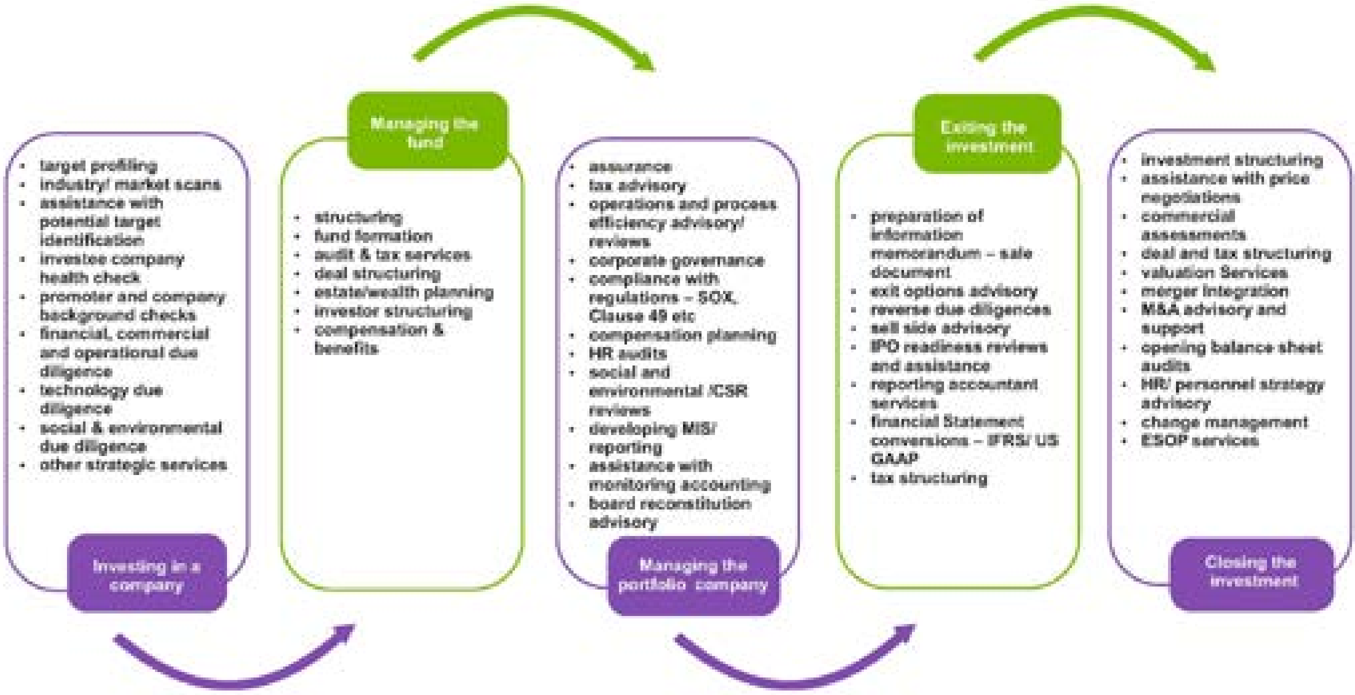
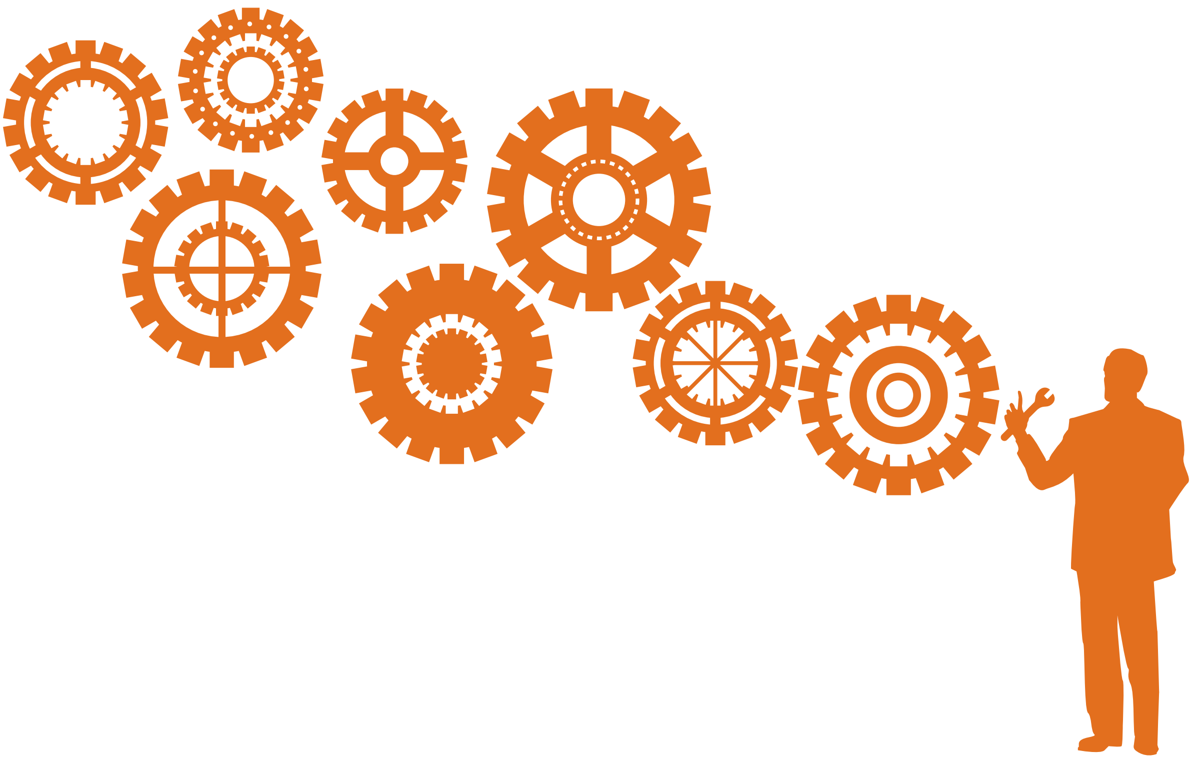
Anirudh Gupta


Meghna Bansal

GT PE advisory services





About this publication

Methodology

The deal data for this report has been sourced from Grant Thornton's Dealtracker report. This report includes views from experts across leading Private Equity (PE)/Venture Capital (VC) funds. We highlight that the views of the investor are their personal views and may not always necessarily reflect the views of the organisation. The reference to PE in the report includes VC unless mentioned otherwise. Deals have been classified by sectors based on certain assumptions, wherever necessary. If different assumptions were to be adopted, the classification would therefore be different.

Please write to contact@in.gt.com for details on the list of private equity deals in India

Disclaimer

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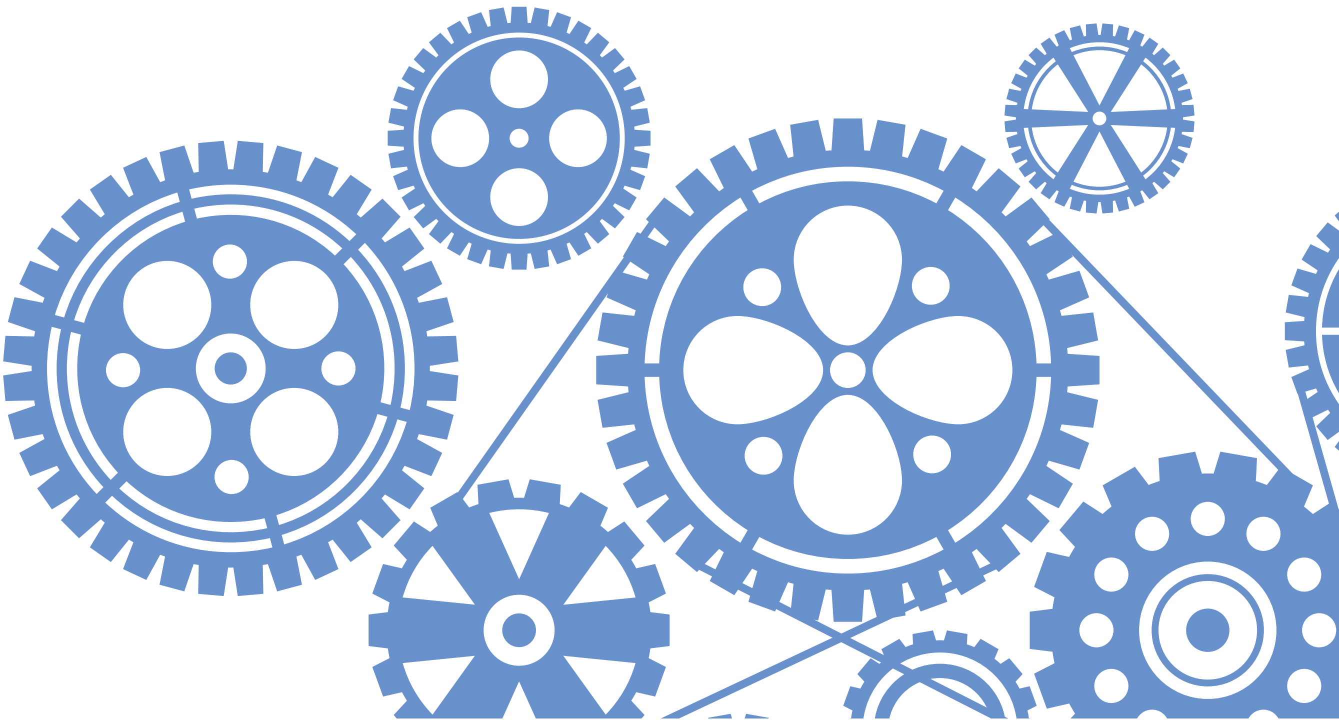

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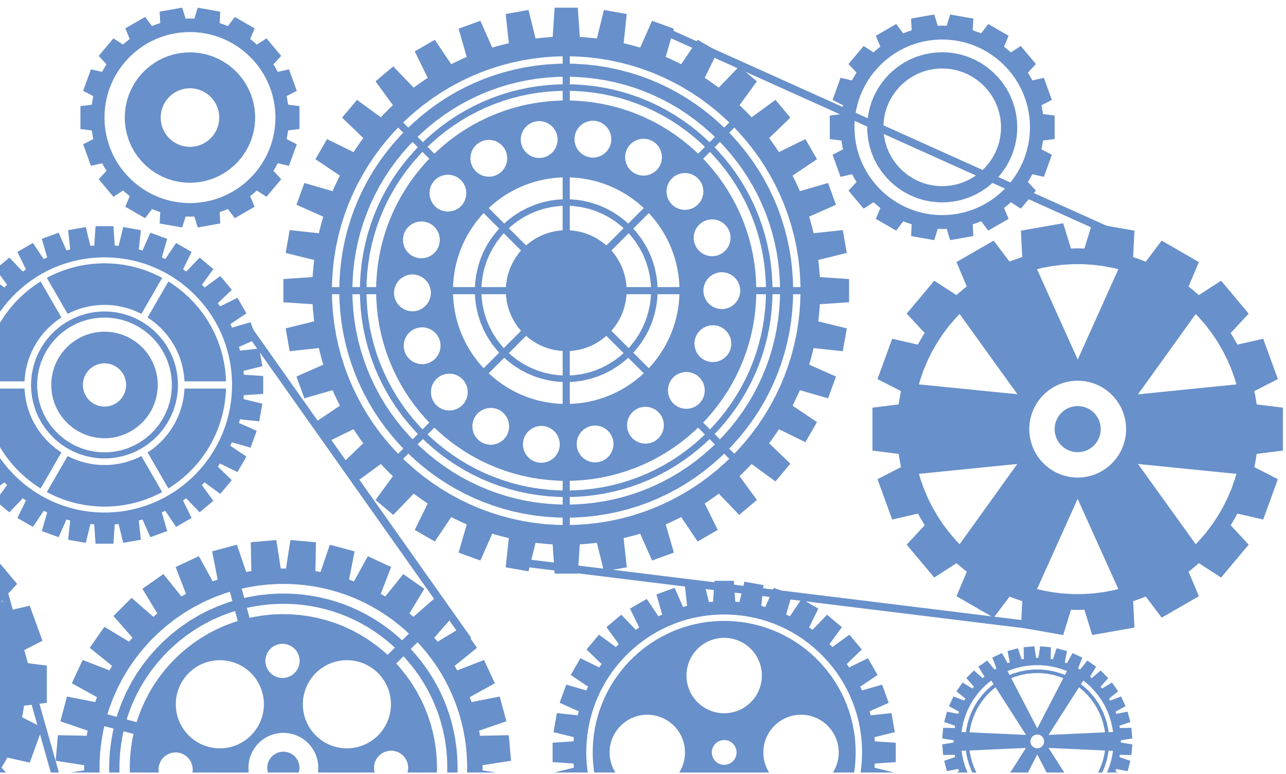
Credits		
Authors Gautam Dayaldasani Chinmay Naik Rony Thomas Prashant Mehra Divyabala N Monica Kothari	**Editorial review** Devesh Chandra Srivastava	**Design** Gourav Kalra



Contact us

To know more, please visit **www.grantthornton.in** or contact any of our offices as mentioned below:

NEW DELHI
National Office
Outer Circle
L 41 Connaught Circus
New Delhi 110001
T +91 11 4278 7070

AHMEDABAD
BSQUARE Managed Offices
7th Floor, Shree Krishna Centre
Nr. Mithakali Six Roads
Navrangpura
Ahmedabad 380009
T +91 76000 01620

BENGALURU
Bagmane Tridib, Bagmane Tech Park,
C V Raman Nagar,
Bengaluru - 560 093
T +91 80 4243 0700

CHANDIGARH
B-406A, 4th Floor
L&T Elante Office Building
Industrial Area Phase I
Chandigarh 160002
T +91 172 4338 000

CHENNAI
A7th Floor, Prestige Polygon 471, Anna Salai,
Teynampet
Chennai 600 018
T +91 44 4294 0000

GURGAON
21st Floor, DLF Square
Jacaranda Marg
DLF Phase II
Gurgaon 122002
T +91 124 462 8000

HYDERABAD
7th Floor, Block III
White House
Kundan Bagh, Begumpet
Hyderabad 500016
T +91 40 6630 8200

KOCHI
7th Floor, Modayil Centre point
Warriam road junction
M. G. Road
Kochi 682016
T +91 484 406 4541

KOLKATA
10C Hungerford Street
5th Floor
Kolkata 700017
T +91 33 4050 8000

MUMBAI
16th Floor, Tower II
Indiabulls Finance Centre
SB Marg, Elphinstone (W)
Mumbai 400013
T +91 22 6626 2600

MUMBAI
9th Floor, Classic Pentagon
Nr Bisleri factory, Western Express Highway
Andheri (E)
Mumbai 400099
T +91 22 6176 7800

NOIDA
Plot No. 19A, 7th Floor
Sector – 16A
Noida 201301
T +91 120 7109 001

PUNE
3rd Floor, Unit No 309 to 312, West Wing, Nyati Unitree Nagar Road,
Yerwada ,Pune 411006
T +91 20 6744 8800

For more information or for any queries, write to us at **contact@in.gt.com**

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