The coming of age of the Indian startup ecosystem

By Darius Pandole | March 1, 2022

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2021 was a watershed year for private equity (PE) and venture capital (VC) investments in India, with investment activity reaching an all-time high of approximately $63 billion.

Since 2017, which was also a record year, PE-VC investments have been witnessing robust year-on-year growth. Exit activity also reached an all-time high of about $32 billion 2021, which in turn is likely to attract additional capital into India going ahead.

Investments in startups were a defining feature of 2021, as private investors committed over $30 billion to Indian startups, compared to the $11.5 billion they invested in 2020, as per the Indian Tech Unicorn report 2021.

The country also minted unicorns at an unprecedented pace, adding 46 in the last year alone and more than doubling its unicorn tally to over 90. India now has the distinction of being the third largest unicorn hub in the world (after the US and China).

Intervals between fundraising rounds shrank from years to months as businesses rapidly gained scale on the back of tremendous growth opportunities, created by a new generation of entrepreneurs, and supported by improving digital infrastructure, new investment themes, and abundance of risk capital.

Flipkart has emerged as the most valuable unicorn ($37 billion) whilst Mensa Brands was the fastest to turn unicorn.

The startup ecosystem in India has witnessed a sea change over the last decade as India's business landscape has become more conducive to entrepreneurship. This has fostered a vibrant startup ecosystem buzzing with new technologies and innovation, creating employment, and celebrating entrepreneurship.

As a result, PE-VC investments in India have also become more broad-based with the share of startup investments steadily increasing through the decade. It is heartening to note that a plethora of startups are being established, not only in the technology domain but also in consumer, financial services, logistics, etc.

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Fintech and ecommerce continue to remain investor favourites, accounting for over a third of the unicorns in India. The potential upside is huge: a majority of India's 700+ million internet users are just entering the world of social networking, online streaming, digital payments, and ecommerce.

Even in traditional sectors such as agriculture, increased digital engagement by farmers on new-age digital platforms is facilitating daily activities such as buying seeds or selling produce. As a consequence, there is a strong likelihood that India may see its first agritech unicorn in the near future.

A robust startup ecosystem

The opportunity looks even more attractive when seen in the context of the recent crackdown on internet companies in China, which has witnessed a concerted effort by the government to reign in its tech startups and wrest back control of user data.

The Indian government, on the other hand, is on a mission to build a robust startup ecosystem, which is indeed laudable. The government has undertaken several initiatives and introduced many schemes to promote and support entrepreneurs.

These include the Startup India Initiative which, among other things, provides tax benefits to startups, and the Startup Accelerators of MeitY for Product Innovation, Development and Growth (SAMRIDH) Scheme, which is designed to provide funding support to startups along with extending customer-connect, investor-connect, etc. Startups have become an important part of the Indian economy and a large source of much needed FDI.

2021 was also a landmark year for Indian startups going public. A total of 11 startups (including eight unicorns) raised $7+ billion on Indian bourses through public offerings. Digital startups, including beauty e-tailer Nykaa and food delivery app Zomato, saw overwhelming demand for their IPOs.

The successful listing of a few loss-making startups has also bolstered investor confidence in Indian capital markets as a viable avenue for exit. Flipkart, PharmEasy, Delhivery, Ola, etc. are amongst a slew of startups planning big-ticket public offerings in 2022.

In the midst of such unbridled euphoria, what are some of the pitfalls that the startup ecosystem needs to watch out for? Is the sector overheated? Will investors make money at these valuations?

Whilst these are issues to consider, it is important to note that the money raised will be used to hire people, build infrastructure, stimulate technology innovations, spur demand, build brands, etc. - all of which will result in a significant economic growth multiplier for the economy.

India's startup ecosystem has undergone a radical change due to a remarkable confluence of significantly increased risk capital funding as well as regulatory and business environment improvements.

As the ecosystem matures, there will be increased focus on sustainable growth, with reduced burn and better unit economics. The opportunity is huge and the stage is set for entrepreneurs to continue to innovate, do more with less, and build all-weather businesses that can deliver positive cash flows. If they manage to do that, there is no end in sight for the Indian startup juggernaut.

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