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FINANCIAL RESOURCES OF STARTUPS: AN EMPIRICAL ANALYSIS OF SELECTED INDIAN COMPANIES

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Abstract

Startups are young companies which are just beginning to develop. Initially, it is funded by a group of people having some innovative ideas. As per Nascom's report, India continues to be 3rd largest startup ecosystem in the world. even this is the case startup's exit rate also increase, which may be due to different factors such as lack of proper management, lack of finance, or inability to meet competition etc… Among these factors finance plays a tremendous role in the survival of an enterprise. Now there are many innovative measures are available for startup financing such as bootstrapping, crowd funding, mezzanines finance etc and its proper deployment is considered as the base for further development. There must be proper care regarding investing in various stages of its operation. So this paper attempt to provide an awareness regarding what are the various modes of financing available for startups and also to evaluate is there any relation exist between startup funding and stage of operation. Both descriptive statistics, as well as multivariate analysis are applied for the analysis of data. Non parametric Kruskal Wallis test is adopted to know is there any relation exists between stage of startup funding and the amount invested in different startups. When startups are at earlier stages, then smaller amount of external capital is required because of they always relies on their own fund at that time, external source of finance are applied when they are at later stages.

Keywords: *Bootstrapping, Mezzanine finance, crowd funding*

Introduction

Newly established firm has important role for knowledge based economies. Because it has to contribute source for new jobs, radical innovation as well as productivity growth firms **(Block et al. 2016).** Unfortunately, these firms often suffer from financing constraints, which limit their growth and threaten their survival **(Brown and Earle 2015; Carpenter and Petersen2002**; **Cosh et al. 2009.** Startups are innovative and newly established firm which are highly risks oriented and probability of success is very low. In order to survive in the business, they need to ensure core competency which cannot be guaranteed by others. Since they are small in size, there is need to ensure many barriers such as finance, technology, managerial etc…among these finance is the major reason for exiting from business organization.

So startups can be survived through introduction of many business incubation centers and supporting agencies. These agencies are offering number of services such as managerial and technical advice, financial assistance and risk diversification etc…The concept of startup finance has changed last year. It include new method such as crowd funding, peer to peer methods, PPP etc…and one of the main problem is that in order to acquire loans and advances from financial institutions, there is need to provide mortgage as securities, but in case of startup companies, they don't have prior experience and good asset records. So these enable to search for alternative and innovative methods. Apart from that entrepreneurs should be very careful while investing in each stage of its operation.

Finance is considered as the life blood of business and if it is not properly utilized it will not run the ever running wheel of the business enterprises. Finance is provided by both public and private financial institutions. In 26th January 2015 Prime Minister Narendra Modi announced Startup India Standup India plan, which encourage many startup companies to compete with giant business enterprises. Similarly as part of MSME Act, Government has given certain reservation for Micro Small and Medium enterprises. All these are considered as the foundation stone for the business enterprise to introduce innovative ideas. Even this is the case; much business enterprise cannot survive for long period of time. Startups exit rate is higher because of various reasons including financial crisis. So they have to bring innovative tools like TQM, Lean startup methodology and other innovative measures

Globalized era enhance the growth of large number of startups in India. During the period of 2018-2019, there are 1200+ startups are added. Now there are 7700+ startups are working in India. Among these Bengaluru, Delhi and Mumbai are the top startups hub. Business incubation centers has important role for the development of these startup companies and there are different agencies such as Kerala Startup Mission, Technology business incubation centers etc are performing an important role for the survival of business enterprises. India has highest number of unicorn startup after US and China. On the basis of its growing statistics highest numbers of startups are attracted towards these sectors.

Startup companies are facing many barriers for acquiring finance from investors. Investors always conduct feasibility analysis and technical analysis while investing in newly established firms. Scalable and viable business ideas are more accepted. Nowadays most startups are service oriented and they lack collateral for accessing bank loans. So they may find difficult to access these kinds of funds.

Review of literature

Carmen Cotei.et.al (2017) makes critical analysis of how startup finance overtime. Data was analyzed through Latent Growth Modeling. They found that when business is at the startup stage, they always prefer private source of fund or their friends and family. When their business become grows, entrepreneurs are injecting proportion of debt to its capital structure. Study concluded that entrepreneur's characteristics also influence the use of debt and equity. When startups with high R&D use lower proportion of debt.

Swati Patil(2019) conducted an empirical analysis of startup finance for entrepreneurs in India. Study was aimed to find various financial sources available for startup financing. Apart from that study also aims for the customer satisfaction towards startup financing and choice of people on private and public finance. Content validity was established by using factor analysis. Data was analyzed though t test, Anova, chi square, Karl Pearson correlation and Spearman Rank correlation. Study found that gaining high qualification and experience is important for startup financing. Similarly startups having high financial capital and asset can access startup fund easily. On incubators point of view, they can provide positive growth and success and they offer fund on the basis of technical, financial and managerial capabilities

Research Methodology

Data collected for the study is secondary in nature. Data from various journals and Nascom report for the period of 2019 is taken for finding relation between startup funding and its various stage of operation. SPSS 21.0 is used for analyzing data. Normality is measured by using Shapiro Wilk test and failed to accept null hypothesis. So Kruskal Wallis test is used to show the relation between variables. Descriptive statistics like mean and SD also applied to show frequency of growth of startup companies.

Objectives of the study

1. To provide awareness regarding innovative financing avenues for startups
2. To identify the relation between startup funding and stage of operation

Hypothesis

H0: median of startup fund are same across startup stages

H1: median of startup fund are different across startup stage

NEW CONCEPTS IN STARTUP FINANCING:

Boot strapping: Bootstrapping is the method in which entrepreneurs are not actually using external source of finance. It is the method in which they are converting human capital into productive ideas. Generally this kind of financing is used when they are at startup stage. Benefit of these methods is that dilution of ownership will not take place.

Seed financing; Seed financing is applied at the initial stage of business. This fund can be used for growth and expansion of business enterprises. When investing in seed capital, investor can enjoy all the privilege of equity share holders. Such amount can be used for research and development and marketing activities. In case of investors is concerned, it is most complicated investment avenue because they having only limited information about the company

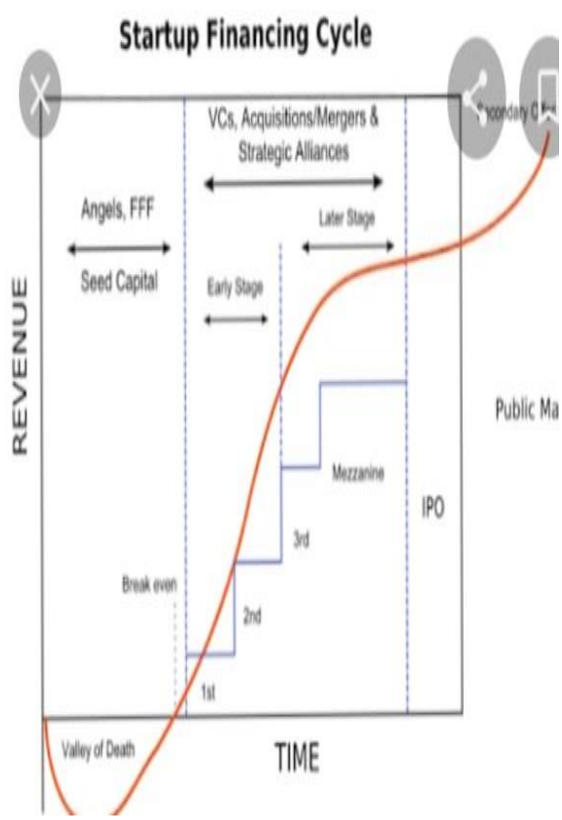
***Angel investors*:** Angel investor's helps the companies not only providing finance, but also share networking and expertise. It is referred to as smart funding. Because of knowledge are shared between the people. These kinds of funds are needed in both in initial stage and any company stuck during its level of operation. They are also referred to as business angel or seed investor and they provide capital as a return to convertible debt or ownership equity.

Venture capital: venture capital is coming from individual, organization or group focused on the development of startup companies. These are considered as the high risk and high return investment and they take part all kind of services including managerial, technical and financial expertise. They assist in taking decision regarding purchase of raw material, vendors etc. generally it provide finance in both early stage and growth stage of business operations.

Startup finance during its various stage of operation:

The performance of the startup companies are influenced by the various factors. Entrepreneurs have to take decision regarding how much amount to be invested in each stage. When business has grown up, then different funding pattern has to be adopted.

- **Early stage**: this stage is referred to as pioneer stage in which fund are required to meet establishment of business and setting up of production unit. Many entrepreneurs are always using their own fund and friends and family for the financing. Such entrepreneurs can always enjoy full control over the companies.
- **Second stage:** in this stage, funds are used for further expansion and development of the business. So they inject equity capital into the capital structure. Fund developed can be used as a method for making marketing and distribution of products and services. Here there is a chance of dilution of ownership takes place.
- **Third stage:** here always external source of funds are preferred by entrepreneurs. These external agencies are not only providing finance. But also helps to provide advice regarding how to survive in the business**.** It include mezzanine finance, bridge finance, angel investors, crowd funding etc
    - **Mezzanines finance:** this amount can be used for further expansion. It is the combination of debt and equity. They always offer a safest mode of investment. But the cost of capital is higher and at the time of dissolution, they can pay after paying all financial requirements. In compensation for higher risk involved it will guarantee higher return
    - **Bridge financing**: it is a kind of short term loan particularly for a period of more than 2 weeks to 3 years. It is also referred to as interim financing for business until all next stage of fund are received. Similar to Mezzanines finance, bridge finance is also riskier capital and higher amount of interest is needed
    - **Crowd funding:**_crowd funding is the method of raising small amount of fund from large number of people, generally amount is collected through internet. There are two types of crowd funding: reward based crowd funding and equity based crowd funding. Crowd funding requires three types of platforms; project initiator, individual or group who support idea and mediator.



Source: Google images

Descriptive statistics

Descriptive Statistics

	N	Minimum	Maximum	Mean	Std. Deviation	Variance
2016	4	1.70	3.80	2.2500	1.03441	1.070
2017	4	.60	1.30	1.0000	.35590	.127
2018	4	.60	3.60	2.0750	1.36961	1.876
2019	4	1.30	3.60	2.3000	1.09240	1.193
Valid N (listwise)	4					

Table shows descriptive statistics of total amount of startup funding received in India for the period of 2016-2019. Each year is divided into 4 quarters and maximum amount of fund received in 2016 is 3.8 Billion dollars and minimum amount received is 1.70 billion dollars. In that year, Indian startup companies received average of 2.25 billion dollars with SD of 1.070 billion dollars among 4 quarters. Similarly in 2017, minimum funding is 0.60 Billion dollars and maximum amount received is 1.30 billion dollars. From that analysis it can see that there is flat decline of startup funding from 2016 to 2017. Investors made only average1 billion dollars with SD of 0.35590.

After that 4 quarters there can see a small variation in startup funding and mean amount of fund invested is 2.0750 billion dollars with SD of 1.36 Bn Dollars. In 2019 also startup funding can be increased. Mean amount can be increased to 2.30 bn dollars with SD of 1.09 bn dollars. So the above table depicts that startup funding can be increased from 2016 to 2019 period and there is higher standard deviation among different quarters. That means startup amount needed for each quarters are different.

Multivariate Analysis:

Ranks

	startup stage	N	Mean Rank
Sfund	seed stage	183	101.66
	series A	77	222.90
	Series B	44	246.56
	series c	23	306.76
	series D	3	320.33
	SERIES E	5	330.00
	SERIES F	1	333.00
	Total	336	

Test Statistics[a,b]

	Sfund
Chi-Square	210.944
Df	6
Asymp. Sig.	.000

a. Kruskal Wallis Test

b. Grouping Variable: startup stage

Hypothesis Test Summary

	Null Hypothesis	Test	Sig.	Decision
1	The medians of Sfund are the same across categories of startup stage.	Independent-Samples Median Test	.000	Reject the null hypothesis.
2	The distribution of Sfund is the same across categories of startup stage.	Independent-Samples Kruskal-Wallis Test	.000	Reject the null hypothesis.

Asymptotic significances are displayed. The significance level is .05.

Data is taken from Nascom Report 2019; it can see that there is growth in performance of startup companies. As per this report, 336 startup companies are taken and studies relation between stage of startup funding and amount of funding. Non parametric Kruskal Wallis test is applied to establish relation between variable. SPSS 21.0 are used to analyze data. Here startup funding stage is divided into 7 categories.ie, seed stage, Series A, Series B, Series C, Series D , Series E and Series F. among these 7 stages seed stage, A and B are considered as the early funding stage and others are late funding stages.

Table shows that majority of startup companies are depending on seed and early stage of funding. When firms are at earlier stage, then it requires few amount of fund. In the earlier period every startup companies are relies on their own fund and only small amount is extracted from external sources. As per the analysis, it can conclude that we can reject null hypothesis. Because of sig value is less than 0.05 and it is clear that median of startup fund are different among different startup stage. A Kruskal Wallis test showed that there was statistically significant difference in amount of fund received during the various stages ,chi square =210.944 and p=0.0000 with a mean rank for 101.66 for seed, 222.90 for A, 246.56 for B, 306.76 for C, 320.33 for D, 330 For E and 333 for F. So every entrepreneur has to take proper decisions regarding how much amount are to be needed for its development stage and final stage.

Conclusion:

Startups are young and newly established firm. These companies are facing too much challenge with a view to survive in the business. Among these amount of finance invested during each stage are decided effectively by proper planning. When startups are earlier stages, only few amounts are extracted from external source of finance. Otherwise they depends on their own funds and fund from friends and relatives. Even small amount needed, majority of startups are depending on seed and early stage finance for development of their business enterprises. So finance has important role for survival of business. Now there are innovative measures are available for startup financing such as crow funding, mezzanine finance, venture capital and angel investors. Each of them has its own way of investing in different stage of funding.

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