

# The Fourth Wheel - 2012

Private Equity in the Corporate Landscape



### **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 and entrepreneurs. 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.

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# Acknowledgments

**We are extremely thankful to IVCA and industry experts for sharing their views.**

Abhishek Sharman – Principal, IEP Fund Advisors Private Limited  
Arun Gupta - President Business Development & Investments, Future Ventures India Ltd  
Ashley Menezes - Managing Director, Chryscapital  
Jayanta Banerjee - Managing Partner, ASK Pravi Capital Advisors Private Limited  
JM Trivedi - Partner; Head, South Asia, Actis  
Kumar Shiralagi - Managing Director, Kalaari Capital  
Nainesh Jaisingh - Managing Director & Global Co-Head, Standard Chartered PE  
Nitin Nayar - Managing Director, Warburg Pincus India Private Limited  
Pallavi Bakhru - Partner & Leader, Tax & Regulatory Services, Walker, Chandiook & Co  
Phanindra Sama – CEO, redBus.in  
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Raja Kumar - Founder & CEO, Ascent Capital Advisors  
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# Contents

	Page
I. Foreword	6
II. Editorial	9
III. Private Equity investments data and analysis	10
IV. Sector-wise Private Equity deal analysis	21
V. Global Private Equity survey findings	38
VI. Private Equity lifecycle	43
a. Commercial due diligence	44
b. Financial frauds – risks and challenges	47
c. Private Equity exits – challenges and opportunities	51
d. Expert insights	53
e. Tax and regulatory impact on Private Equity funds	54
f. Sector insights	60
g. Insight from an entrepreneur	65
VII. Investor views	66



# Foreword by IVCA



**Sumir Chadha**  
**Ex- Chairman, IVCA**  
**Co-founder and Managing Director**  
**WestBridge Capital**

It has always been our endeavour at IVCA to provide timely insight for the Indian Venture Capital (VC) and Private Equity (PE) Industry. Thus, it is with great pleasure that we, along with our Knowledge Partners, Grant Thornton, present the second edition of the PE report titled “Fourth Wheel.” At a time when the VC/PE industry is facing challenges and is in the process of change, this report will be very useful for understanding the role of VC/PE in India’s growth. The report has significant data on investments by VC/PE’s and tracks the growth of the industry across sectors and sizes based on the Grant Thornton Dealtracker, which has been a pioneer in deal tracking and VC/PE deals over the past seven years. Through this report we have also shared an analysis of the industry based on the experience of Grant Thornton professionals on due diligence, frauds, structuring and sector insights. In addition to this we also interviewed some reputed PE professionals for their insights on the subject matter.

The present time is clearly a challenging one as the industry is at a cross road with the slowing down of the Indian economy and policy paralysis in the government which is impacting progress of business, a dried up IPO exits difficult governance issues in investee companies and a global investors not as excited as before, on the India Inc. story. However, this also presents some great opportunity for the industry as India is still a high growth market and continues to present some exciting opportunities.

We believe the report provides insights on the current challenges and opportunities in the industry, along with providing a detailed analysis of investment trends as per stage, sector and players.

We look forward to your feedback and continued support.

# Foreword by Grant Thornton



**Harish HV**  
**Partner, India Leadership Team**  
**Grant Thornton - India**

We are pleased to bring out the second edition of the “Fourth Wheel” a publication on PE in India. I would first like to thank the industry experts from leading PE/VC Funds and entrepreneurs for their valuable insights as well as the Grant Thornton team in India for their support in collating this report.

This report aims to set out the key emerging trends in the Indian PE industry deal data based on Grant Thornton’s Dealtracker report, and views from experts across leading PE/VC funds and entrepreneurs.

To begin with, I am reproducing the logic behind using the title “Fourth Wheel” for those of you who are first time readers. The Indian corporate landscape has been dominated by 3 different types of companies for a long period of time; the public sector, the private sector and multinationals, over the past decade and a half. Now however we are seeing the emergence of the fourth variety which is companies owned/supported by PE, we call this segment the “Fourth Wheel.”

As we pointed out in the last issue, this segment has now reached significant scale With PE investors having invested in excess of US\$65bn over the past eight years. Presuming that they own an average of 25% of the companies they have invested in, and there is no appreciation or depreciation in the value, the value of the companies invested by PEs is US\$ 260bn. This is about 21% of market capitalisation of BSE & NSE respectively. Till date the number of companies that PEs have invested in is over 2,000. These are significant numbers and hence PE backed companies or the “Fourth Wheel” can justifiably be a separate category while within India Inc.

There are in excess of 200 PE funds operating in India in various forms. They can broadly be categorised as:

- international funds operating through an India office (investing from an India / Asia allocation or directly from a global pool of capital)
- funds sponsored or anchored by Indian financial institutions; or funds sponsored/ anchored by business houses (domestic/international) and;
- funds managed by general partners with prior investment or industry experience.

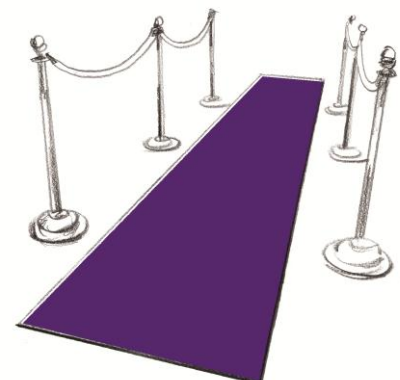
One of the issues with the industry earlier was that we had funds which were focused on providing only growth capital. Today, the industry looks balanced and we have funds at all stages of the lifecycle be it seed, venture, growth, buyout or distress.

# Foreword by Grant Thornton

- a. the traditional view of IPO being the standard exit route is now no longer valid. It is clear that PEs are looking at other mechanisms for exit and there have been good examples of successful exits in the past year in spite of the lack of the IPO market
- b. the perception of India as an easy market to invest and make money based on its growth momentum is no longer valid. This has made global investors wary of making new investments into funds
- c. PEs have realised the need to focus on their investee companies at an operating level
- d. we have seen a few unpleasant surprises on the governance front amongst PE investee companies
- e. there have been regulatory challenges in taxation and other areas
- f. valuation challenges have eased relatively compared to last year
- g. entrepreneurship has seen a significant increase in the country and a large part of this boost is due to the PEs
- h. we are seeing the emergence of new sectors and with the India growth story still going strong there are available opportunities

We are extremely positive about the industry and the role it has played and will play in the growth of the Indian economy. This will happen through; the creation of new entrepreneurs, helping existing entrepreneurs grow, improving standards of governance and bringing in best practices. The PE/VC industry, like any other, is going through a cycle and in our opinion is presently consolidating and reorganising its business model. This will address the issues named above and will in our opinion continue to gain its strength, grow and make the Fourth and Youngest Wheel of India Inc. move faster than the other three.

I hope you find this report insightful and wish you all the success!



# Editorial



**Raja Lahiri**  
Partner, Transaction Advisory Services  
Grant Thornton - India

The impact of PE on the Indian entrepreneurship landscape has been significant in the last decade. The evolution of the industry from early stage venture capital investing to private equity growth capital, capital for distressed situations and capital for management buy-outs has clearly brought out the maturity of the PE industry.

During 2012, we witnessed PE investments of US\$ 7.35bn (400 deals) as against US\$ 8.8bn (373 deals) in 2011. The largest PE deal in 2012 is in the business process outsourcing sector which had Bain Capital investing in Genpact for US\$ 1bn.

Currently, the theme around the domestic consumption story appears to be attractive for investment in sectors like healthcare, FMCG, food, agriculture, dairy products and other consumer focused businesses. Another emerging sector which has attracted PE investments during 2012 is e-commerce. This is due to the significant potential for this sector to play out, given the opportunity to increase internet penetration in India.

Therefore, the investment opportunities in India continue to be large and we expect PE Funds to continue playing an active role in supporting entrepreneurs in India's growth story.

The PE Industry is now coming to a crucial juncture where Portfolio Company exits, returns to limited partnership and fund raising for the PE Funds itself are becoming key areas of focus. During 2012, the impact of global economic slowdown coupled with

India's slowing economic growth rates have possibly led to PE funds looking at the quality of portfolio assets more closely and focusing on "returns" more than ever before.

Given the global macro-economic weaknesses, fund raising has become challenging for many PE funds. However, we have also witnessed successful fund raising on the back of quality of teams, past portfolio performance and successful returns.

Portfolio company exits remain a key focus for PE funds. While exits are a challenge given the current stage of the IPO market, quality portfolio assets would remain an attractive asset for M&A and PE secondary buy-out situations.

During the early part of 2012, we witnessed several regulatory challenges around GAAR (General Anti Avoidance Rules) and retrospective taxation. However, the recent government focus on reforms and review of the tax regulations is expected to slowly but surely bring certainty back in the minds of PE Investors while, PE Funds continue to focus on delivering successful returns along with finding the right investment opportunities.

As Warren Buffet had said – "It's far better to buy a wonderful company at a fair price than a fair company at a wonderful price."

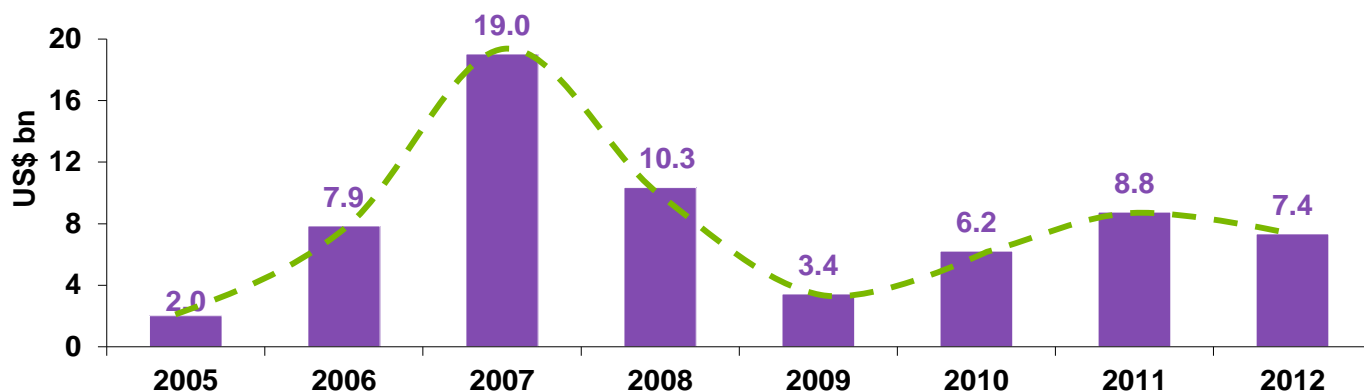
I believe that the PE Industry in India will continue to play a very active role as a key partner for entrepreneurs in India's growth story.

# PE investments data and analysis

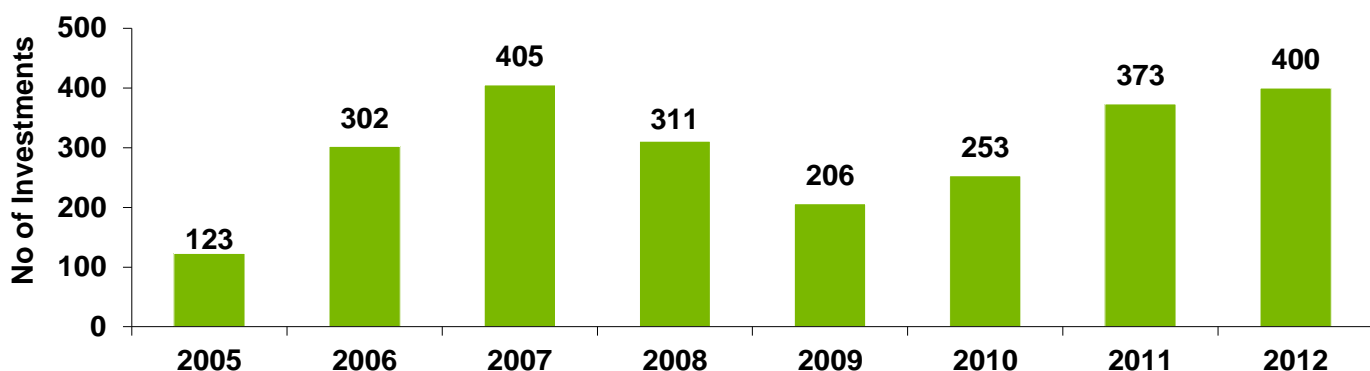


# PE: Investments in India

Total PE investments (value) (2005 – 2012)



Total PE investments (volume) (2005 – 2012)



During the boom years between 2004-2009, India had reached the status of an ‘Asset Class’ in itself. The developments over the last three years on the political, economic and governance fronts – mean that it has lost that status and reverted to being a market for selective investment. This is already separating the men from the boys, not only amongst investors – but even the entrepreneurs themselves. Some of the best attributes of Indian businessmen – (a) resilience in an uncertain/ unhelpful environment (b) management of capital frugally for high returns and (c) innovation – are required now more than ever.

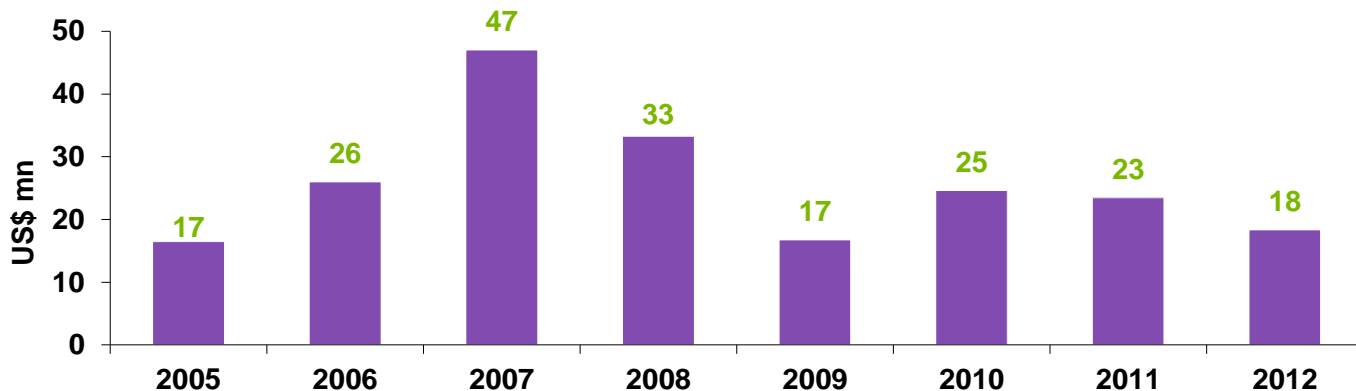
The PE community will likewise be required to dig deep, where only seasoned / mature teams and flexible business models will be able to partner successfully with Indian business going forward.

**Nainesh Jaisingh**  
**Managing Director & Global Co-Head**  
**Standard Chartered PE**

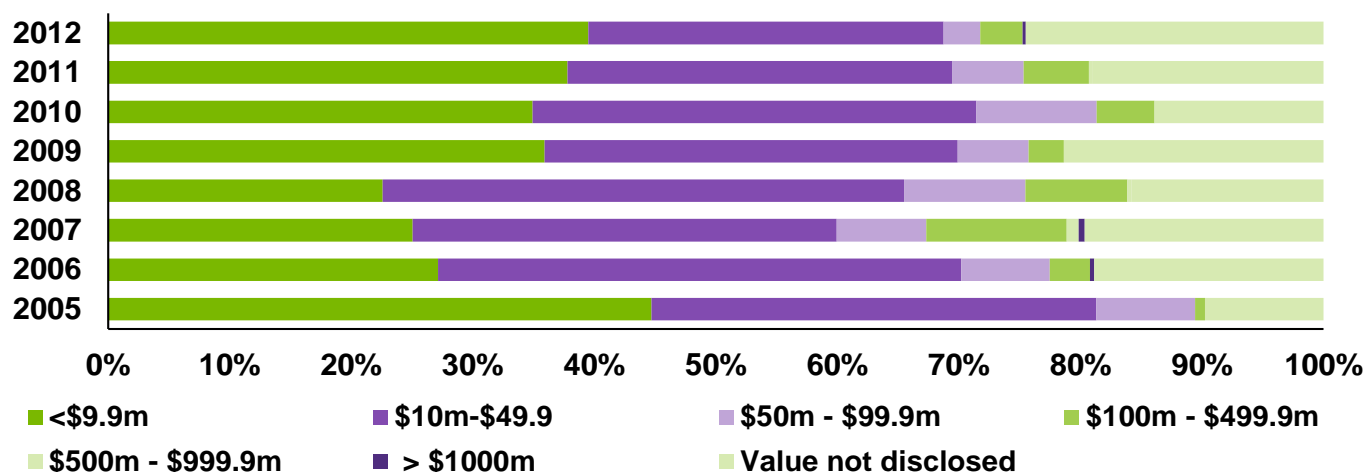
Source : Grant Thornton Dealtracker and Grant Thornton analysis

# PE: Investments in India

PE average deal size (2005 – 2012)



PE investment ranges (2005 – 2012)



PE activity in 2012 looks robust despite moderation in the economic growth rate in India. 2012 has witnessed 400 deals compared to 373 deals in 2011. However, the average deal size has reduced in 2012 compared to 2011. Mid-market growth capital deals continued to be the focus of the PE funds.

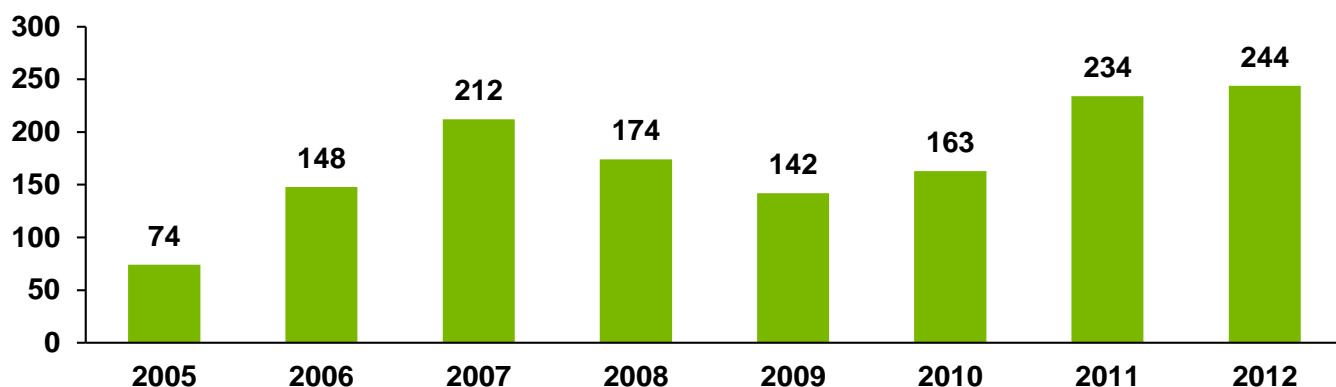
"It is no secret that the PE market in India is very competitive, this is equally true for markets such as the US and Europe. Macro-economic slowdowns, market volatility and regulatory uncertainty are also not unique to India. However, the structural tailwinds, especially relating to domestic consumption and demographics, are powerful long-term trends and should continue to create opportunities. Further, new sectors will inevitably emerge, either through regulatory discontinuity (e.g., modern retail), or technological discontinuity (e.g., internet)."

Nitin Nayar  
 Managing Director  
 Warburg Pincus India Private Limited

Source : Grant Thornton Dealtracker and Grant Thornton analysis

# PE: Investments in India

Number of PE investors



PE industry earlier had funds which were focused on providing only growth capital. Now however, the industry looks balanced with funds available at all stages of the lifecycle be it seed, venture, growth, buyout and distress.

"The biggest challenge is the need for consolidation amongst PE players. There are many capital providers today and sometimes, oversupply causes irrationality in paying too high an entry price that impairs the return on an investment for a long time. Over time, one would expect the industry to consolidate itself."

**Ashley Menezes**  
Managing Director  
Chryscapital

"The lacklustre equity markets have not helped either, with exits being deferred indefinitely until the markets improve. Therefore, fund raising will be a challenge in the medium term when the industry is ripe for consolidation. However, the silver lining is that there are still plenty of good opportunities to invest with quality entrepreneurs."

**Raja Kumar**  
Founder & CEO  
Ascent Capital Advisors

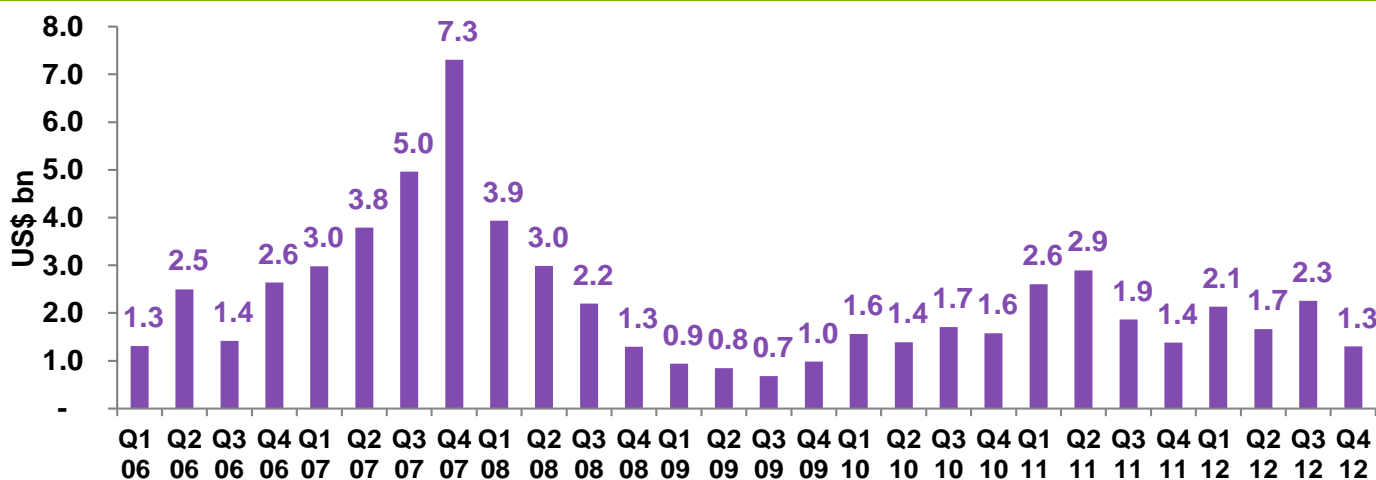
"India has risen as a key emerging market destination for global Venture Capital (VC) investing over the last few years, with one of the fastest growing economies globally. A positive development in recent years has been the rise of organised institutional seed-stage funds, accelerators and incubators in India. These are filling a long-standing gap by providing both capital and mentoring at the seed stage, which is critical to provide early impetus to Indian entrepreneurs."

**Sudhir Sethi**  
Founder and Managing General Partner  
IDG Ventures India

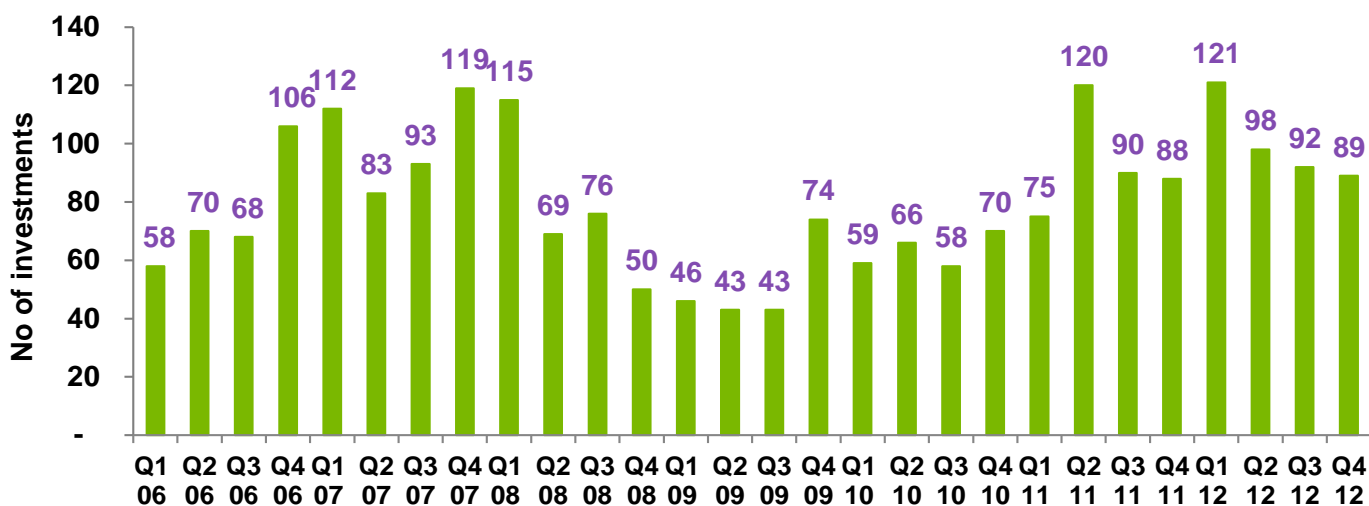
Source : Grant Thornton Dealtracker and Grant Thornton analysis

# PE: Quarterly trend

PE investments quarterly breakup (value) (2006 – 2012)



Total PE investments (volume) (2006 – 2012)



The US\$ 40bn invested between 2005 and 2008 is ripe for exit and a lot of these deals are already in the market thus, boosting demand for capital. "

**JM Trivedi**  
Partner; Head, South Asia  
Actis

"Inspite of a problematic world economic scenario, in early 2011, the level of exits by PE's operating in India was high. This was enabled by a continued belief and faith that inspite of the global crisis the Indian story remained largely intact. Marquee exits included landmark transactions such as investments in Paras Pharma, Patni Computers, Lilliput, SKS Micro finance, Intelenet and many others. These exits were a combination of IPO's, strategic sales and in some cases sale to other PE firms."

**Munesh Khanna**  
Senior Partner, Lead Advisory Services  
Grant Thornton - India

Source : Grant Thornton Dealtracker and Grant Thornton analysis

# PE: Large deals

## Large deals (2005 –2012)

Year	Investor	Investee	Sector	%	US\$ mn
2007	Temasek Holdings	Bharti Airtel	Telecom	5%	1,907
2006	Kohlberg Kravis Roberts & Co	Flextronics Software	IT & ITeS	85%	1,035
2012	Bain Capital	Genpact Ltd	IT & ITeS	30%	1,000
2007	Temasek Holdings, Investment Corp of Dubai, GS, IEP, Macquarie, AIF Capital, Citigroup	Bharti Infratel	Telecom	10%	1,000
2011	Bain Capital, GIC	Hero Investment	Automotive	30%	848
2007	ICICI Venture Funds	Jaypee Infratech	Real Estate	N.A.	800
2007	George Soros, Eton Park Capital, Deutsche Asset Mgmt, Capital International, Citigroup, T Rowe Price, Credit Agricole, UBS & Kotak Mahindra	GMR Infrastructure	Infrastructure Management	N.A.	767
2007	Carlyle Group	HDFC	Banking & Financial Services	6%	650
2008	Providence Equity Partners	Aditya Birla Telecom	Telecom	20%	640
2007	Avenue Capital Group	SKIL Infrastructure	Infrastructure Management	26%	500

Largest deal in 2012: Bain Capital– Genpact Ltd deal was a secondary deal paving way for the exit of the existing investors.

Source : Grant Thornton Dealtracker and Grant Thornton analysis

# Indian Venture Capital outlook and trends



**Sudhir Sethi**

**Founder and Managing General Partner  
IDG Ventures India**

## Introduction

India has risen as a key emerging market destination for global VC investing over the last few years, with one of the fastest growing economies globally, driven by a large middle class leading to vibrant domestic consumption, robust domestic talent pool and strong manufacturing base.

India witnessed close to US\$ 5bn VC investments across 973 deals between 2007 and 9M 2012<sup>1</sup>. Technology—defined as Enterprise Software, Digital Consumer (internet, mobile and new media), and Engineering – has been the critical growth engine of Indian venture investing, accounting for about 70% of all VC investments between 2004-2009<sup>2</sup>.

In addition, technology has also dominated the venture-backed exit landscape in India, both in terms of number of exits and return multiples for investors. Between 2004 and August 2011, there were 152 venture-backed exits in India, with 111 (73% of the total) tied to technology companies<sup>3</sup>. In terms of returns, the average multiple on invested capital for technology exits was about 5.2x, compared with 3.4x for non-technology exits<sup>4</sup>. Close to 30% of technology exits resulted in return multiples in excess of 4.0x to investors.

In terms of geographical spread, Bangalore is firmly established as India's 'Silicon Valley', with the city witnessing maximum entrepreneurial activity across a variety of sectors. Delhi has emerged on the technology scene over last 2-3 years, especially in Internet/ telecom.

These Indian cities are now competing with global tech hubs by moving up the innovation ladder, from being pure outsourcing destinations to emerging as originators of cutting edge technology innovation, R&D and IP.

Another positive development in recent years has been the rise of organised institutional seed-stage funds, accelerators and incubators in India. These are filling a long-standing gap by providing both capital and mentoring at the seed stage, which is critical to provide early impetus to Indian entrepreneurs.

## Key areas of opportunity

Within technology, there are three major areas of opportunity in Indian Venture Capital:

### 1. Digital consumer

Multiple factors – such as rise of a young, well-earning and globally exposed middle class, mobile internet and broadband wireless access and affordable smartphones, are giving rise to a digital consumption wave in India. The Indian digital consumer segment comprises of close to US\$150mn Internet Users (projected to reach US\$ 450mn by 2015)<sup>5</sup>, close to US\$ 50mn mobile internet users<sup>6</sup> and about US\$900mn wireless subscribers<sup>7</sup>. This large base is driving rapid consumption of products, services and content via digital mediums.

<sup>1</sup>Venture Intelligence

<sup>2</sup>Venture Intelligence

<sup>3</sup>Venture Intelligence (calculated for deals where exit data is publicly available)

<sup>4</sup>Venture Intelligence (calculated for deals where exit data is publicly available)

<sup>5</sup>IAMAI, McKinsey

<sup>6</sup>IAMAI

<sup>7</sup>TRAI

<sup>8</sup>India Goes Digital – Avendus Report

# Indian Venture Capital outlook and trends

An attractive area of growth in digital consumer is e-commerce, which is being fuelled by a combination of rising consumption power in Tier II and III cities, and lack of availability of high quality branded products in offline channels. Indian e-commerce (travel + e-tailing) is expected to grow from close to US\$ 9bn in 2012 to about US\$ 24bn by 2015<sup>8</sup>. This growth will be driven by industry leaders such as Flipkart and Myntra.

## 2. Enterprise Software

The US\$ 100bn Indian Enterprise Software segment has gradually evolved from providing outsourced IT services to developing cutting-edge software products for global enterprises, with companies such as Tally, Manthan and Zoho leading this evolution. Major areas of growth in this segment include business intelligence and analytics products and security products and services. Going forward, the next wave of growth in Indian Enterprise Software ventures is expected to come from Cloud, Big Data and Enterprise Mobility etc.

## 3. Engineering

The Indian Engineering space is being driven by increasing willingness of global manufacturers to use India for high-value and commercially sensitive activities such as R&D and the production of goods involving significant IP and Patents. With about 30% of the Top 1,000 global R&D spenders having a centre in India<sup>9</sup>, the country is abundant with

entrepreneurial talent that is emerging out of these global giants and creating ground-up innovative engineering start-ups.

A key area of growth within this space is medical devices, with the Indian Medical Electronics market size expected to reach about US\$ 6.4bn by 2020<sup>10</sup>. Companies such as Perfint and Forus are leading this charge by building globally relevant and IP driven medical device product platforms out of India.

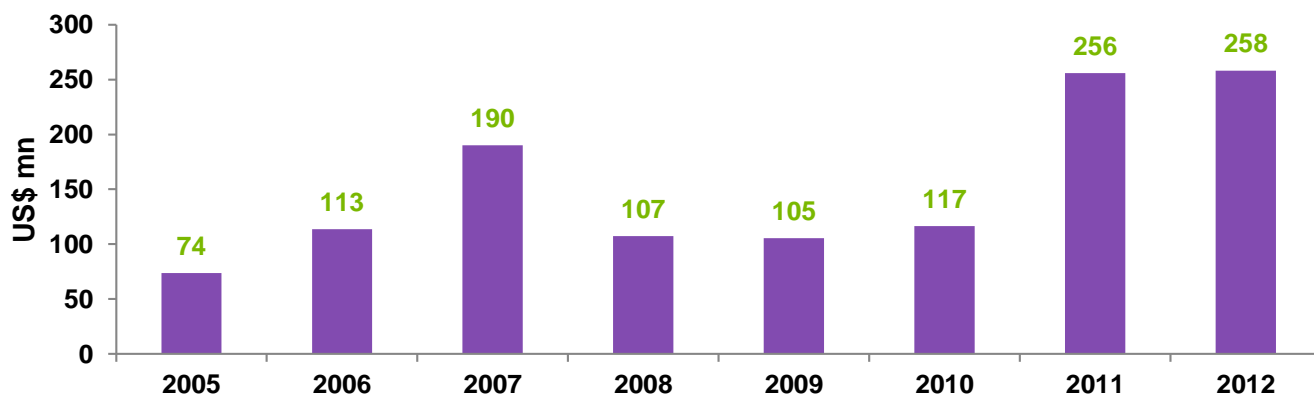
<sup>8</sup>India Goes Digital – Avendus Report

<sup>9</sup>Global R&D Benchmarking Study by Zinnov

<sup>10</sup> Deloitte Report on Indian Medical Electronics

# Early stage investment trends

Early stage investments (value) (2005 – 2012)



Early stage investment represents investments made by venture capital funds (value less than US\$ 5mn)

"Key sectors of interest are; technology & tech-enabled companies, which includes software products, services, embedded software, internet and mobile.

We have seen a big boost in entrepreneurial activity over the past few years – both in quantity of entrepreneurs, and more importantly in their quality. The key challenge would be in the mind-set to create very large corporations, given that there has not been much history of this taking place. "

**Samir Kumar**  
Managing Director  
Inventus Capital

"Considering we are an early stage fund investing about US\$ 5mn in the first round, we keep away from asset intensive business and look for capital efficiency in the companies we invest in. Generally we seek companies that have technology as an enabler in their business model. This could be across various sectors such as IT, software products, telecom, e-commerce, Internet, healthcare, education and clean technologies. We continue to see attractive opportunities in all these sectors although at any given time, market vagaries could significantly affect sector sentiment."

**Kumar Shiralagi**  
Managing Director  
Kalaari Capital

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**Reason says:  
this acquisition  
is too costly.**



**Instinct says:  
not as costly  
as missing out.**

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<b>Dhanraj Bhagat</b>		<b>Mahad Narayanamoni</b>		<b>Sridhar V</b>
<b>Dynamic</b>		<b>Empowered</b>		<b>Competent</b>
	<b>Prashant Mehra</b>		<b>Raja Lahiri</b>	
	<b>Engaged</b>		<b>Cohesive</b>	
<b>Darshana Kadakia</b>		<b>David Panna</b>		<b>Arunkumar Krishnamurthy</b>

# Sector-wise PE deals



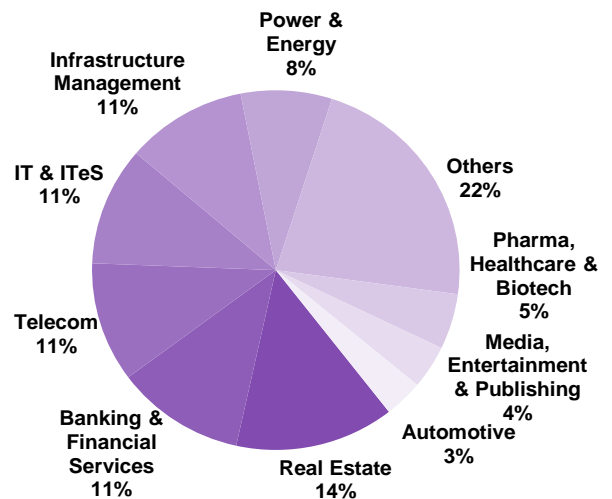
# PE: Investments by sectors

Sector break-up (2005 –2012)		
Sector	US\$ mn	Volume
Real Estate	9,055	152
Banking & Financial Services	7,353	263
Telecom	6,953	61
IT & ITeS	6,887	517
Infrastructure Management	6,887	115
Power & Energy	5,178	119
Pharma, Healthcare & Biotech	3,220	195
Publishing	2,513	119
Automotive	2,214	58
Manufacturing	1,774	81
Textile & Apparels	1,562	71
Hospitality	1,290	63
Others	1,121	92
FMCG, Food & Beverages	1,094	57
Logistics	893	47
Engineering	870	40
Shipping & Ports	869	17
Electrical & Electronics	666	25
Cement	567	13
Agriculture & Agro Products	515	37
Retail	505	43
Education	493	70
Oil & Gas	470	18
Steel	359	11
Plastic & Chemicals	340	25
Aviation	319	23
Travel & Tourism	208	13
Mining	184	5
Metals & Ores	83	8
Packaging	59	4
Printing & Stationary	50	7
Breweries & Distilleries	27	2
Gems & Jewellery	25	2
<b>Grand Total</b>	<b>64,602</b>	<b>2,373</b>

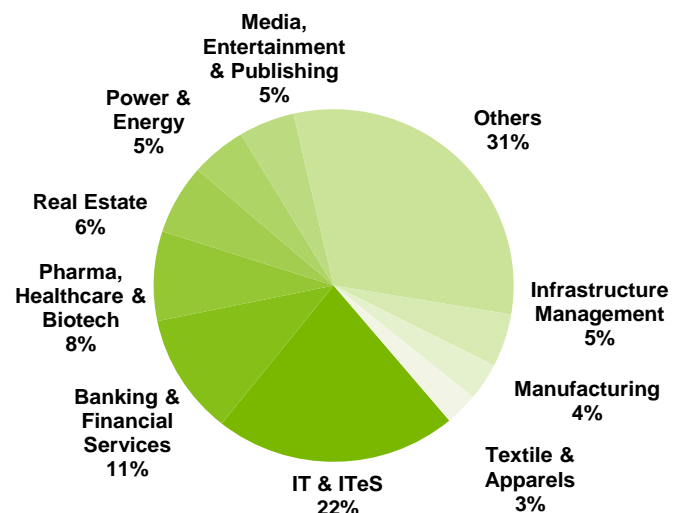
Infrastructure management represents investments in airport, roads, highways etc.

Source : Grant Thornton Dealtracker and Grant Thornton analysis

Sector break-up (value) (2005 – 2012)



Sector break-up (volume) (2005 – 2012)



"In general, PE funds have started to focus on sectors which are relatively insulated from the volatile macro-environment such as healthcare, education and technology."

**Raja Kumar**  
**Founder & CEO**  
**Ascent Capital Advisors**

# PE: Sector trends

Sectorboard			TOP PE Sector 2012
Rank	Last Year	Move	(Deal Value - Deal Volume)
1	1	↔	IT & ITeS (US\$ 1,867mn - 140 Deals)
2	10	↑	Pharma, Healthcare & Biotech (US\$ 856mn - 38 Deals)
3	3	↔	Real Estate (US\$ 715mn - 25 Deals)
4	5	↑	Banking & Financial Services (US\$ 687mn - 45 Deals)
5	4	↓	Power & Energy (US\$ 375mn - 16 Deals)
6	★	↑	FMCG, Food & Beverages (US\$ 338mn - 13 Deals)
7	9	↑	Hospitality (US\$ 322mn - 13 Deals)
8	6	↓	Infrastructure Management (US\$ 311mn - 8 Deals)
9	★	↑	Logistics (US\$ 292mn - 10 Deals)
10	8	↓	Media, Entertainment & Publishing (US\$ 272mn - 17 Deals)

Sectorboard			TOP PE Sector 2010
Rank	Last Year	Move	(Deal Value - Deal Volume)
1	2	↑	Power & Energy (US\$ 1,537.1 Mn - 24 Deals)
2	1	↓	Real Estate (US\$ 626.7 Mn - 20 Deals)
3	3	↔	Banking & Financial Services (US\$ 594.1 Mn - 33 Deals)
4	10	↑	Telecom (US\$ 515.4 Mn - 6 Deals)
5	6	↑	IT & ITeS (US\$ 398.1 Mn - 41 Deals)
6	9	↑	Pharma, Healthcare & Biotech (US\$ 320.4 Mn - 23 Deals)
7	4	↑	Infrastructure Management (US\$ 317.9 Mn - 13 Deals)
8	★	↑	FMCG, Food & Beverages (US\$ 221.3 Mn - 6 Deals)
9	★	↑	Education (US\$ 174.6 Mn - 20 Deals)
10	★	↑	Manufacturing (US\$ 163.9 Mn - 6 Deals)

Sectorboard			TOP PE Sector 2011
Rank	Last Year	Move	(Deal Value - Deal Volume)
1	5	↑	IT & ITeS (US\$ 1,408.0 Mn - 100 Deals)
2	★	↑	Automotive (US\$ 1,077.3 Mn - 9 Deals)
3	2	↓	Real Estate (US\$ 1075.3 Mn - 23 Deals)
4	1	↓	Power & Energy (US\$ 1,030.9 Mn - 25 Deals)
5	3	↓	Banking & Financial Services (US\$ 815.6 Mn - 32 Deals)
6	7	↑	Infrastructure Management (US\$ 766.4 Mn - 8 Deals)
7	10	↑	Manufacturing (US\$ 550.1Mn - 19 Deals)
8	★	↑	Media, Entertainment & Publishing (US\$ 319.5 Mn - 16 Deals)
9	★	↑	Hospitality (US\$ 295.3 Mn - 14 Deals)
10	6	↓	Pharma, Healthcare & Biotech (US\$ 261.3 Mn - 18 Deals)

Source : Grant Thornton Dealtracker and Grant Thornton analysis

Domestic consumption sectors like pharma, healthcare, food & beverages, FMCG, education look attractive for PE investors as witnessed in sector-wise activity over the years.

E-commerce, which is dependent on these sectors, has also witnessed increase in activity in 2012 compared to 2011.

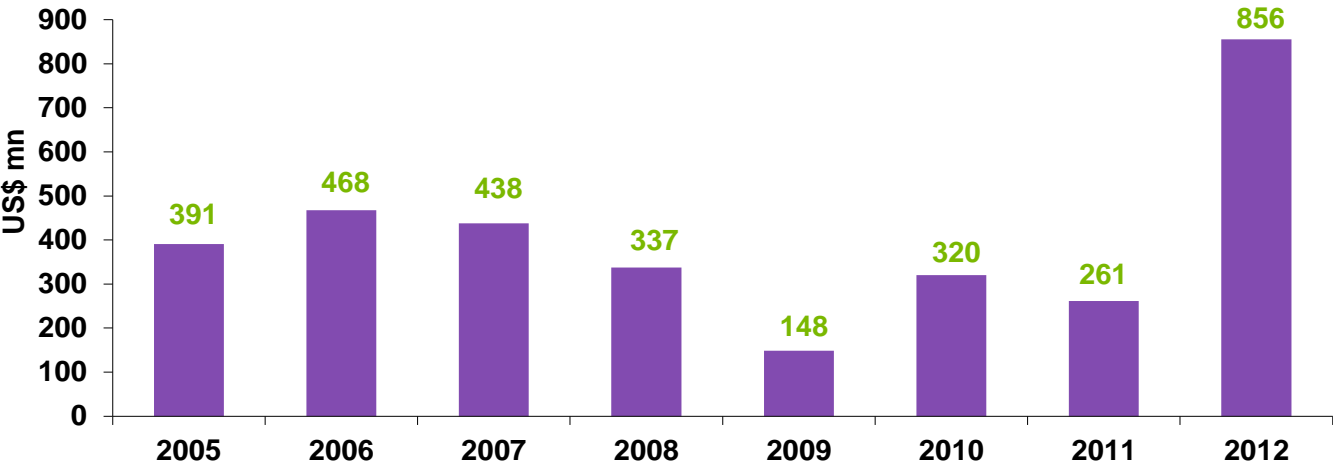
- sectors linked to domestic consumption themes like food, Pharma, Healthcare, Education
- NBFCs in the niche segments like vehicle, education and housing finance.
- services like cash management, logistics and infra/construction ancillary services

**Rakesh Sony**  
Director

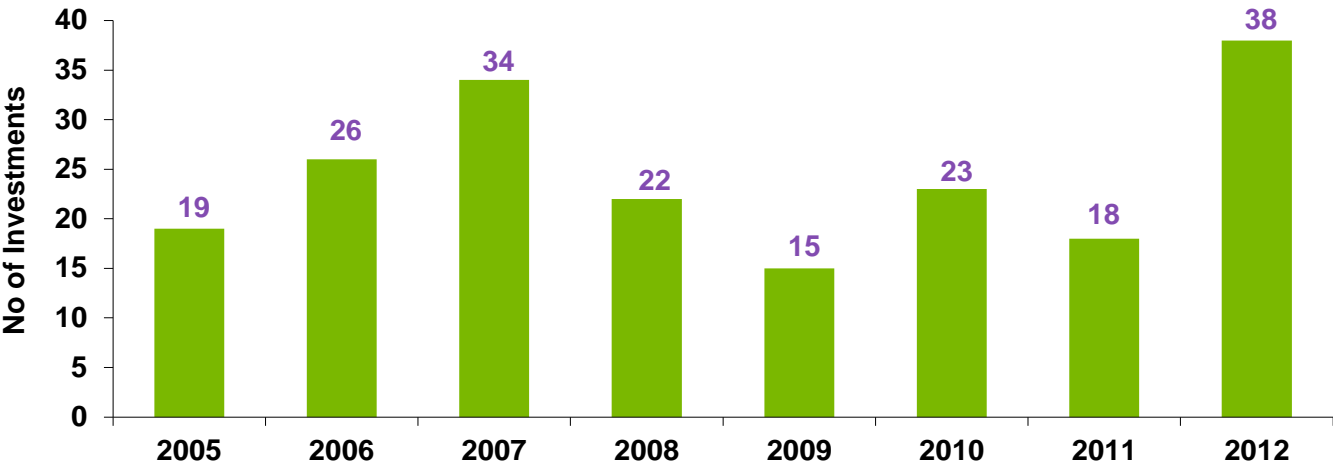
Motilal Oswal Financial Services Limited

# PE: Pharma, Healthcare & Biotech

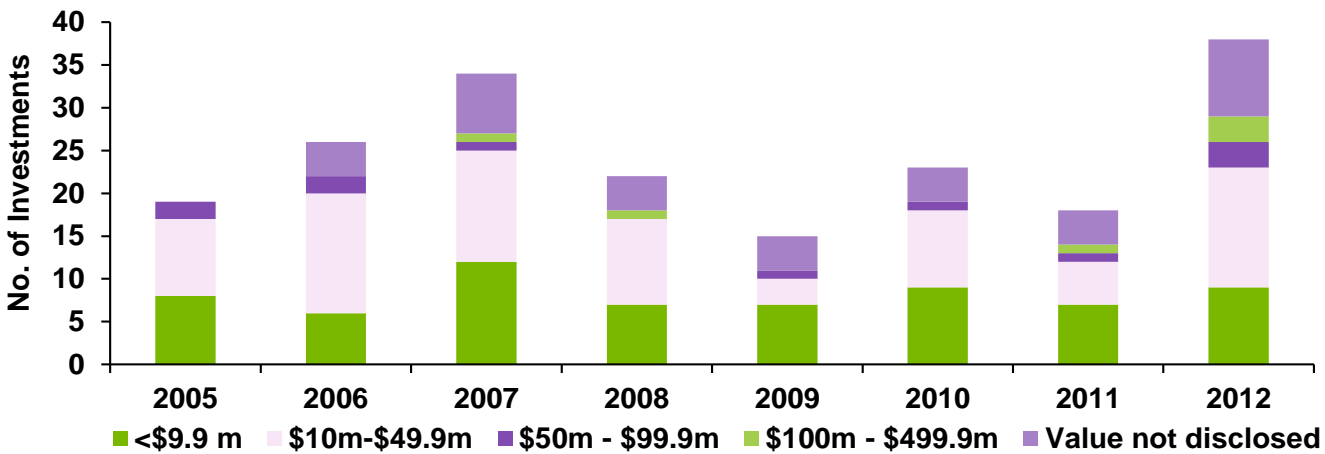
Total PE investments (value) (2005 – 2012)



Total PE investments (volume) (2005 – 2012)



PE investment ranges (2005 – 2012)



Source : Grant Thornton Dealtracker and Grant Thornton analysis

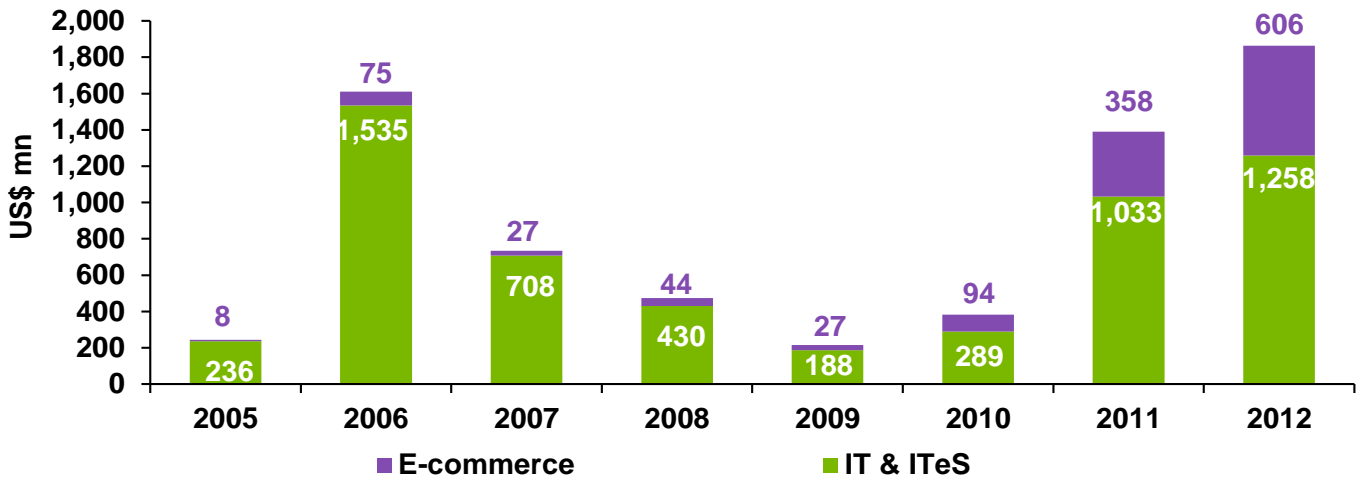
# PE: Pharma, Healthcare & Biotech

Large Deals (2007 – 2012)			
2012	Advent International – CARE Hospital (Quality Care India) <b>US\$105mn</b>	Olympus Capital – DM Healthcare <b>US\$100mn</b>	GIC - Vasan Healthcare <b>US\$100mn</b>
2011	Khazanah Nasional - Apollo Hospitals <b>US\$102mn</b>	NEA, Omani industrial group & GTI - Nova Medical <b>US\$50mn</b>	Avigo Capital - Super Religare Laboratories <b>US\$22mn</b>
2010	Warburg Pincus – Metropolis Healthcare Services <b>US\$85mn</b>	AIF Capital – Famy Care <b>US\$40mn</b>	Cx Partners - Thyrocare Technologies <b>US\$40mn</b>
2009	Global Technology Investment - Nova Medical centre <b>US\$60mn</b>	International Finance Corporation – MAX India <b>US\$33mn</b>	India Venture Advisors – Kavery Medical <b>US\$20mn</b>
2008	American International & JPMorgan – Narayana Hrudayalaya <b>US\$100mn</b>	ICICI Venture – Sahyadri Hospitals <b>US\$36mn</b>	Evolve India Life Sciences fund - Gland Pharma <b>US\$30mn</b>
2007	Apax Partners - Apollo Hospitals Enterprise <b>US\$104mn</b>	International Finance Corporation – MAX India <b>US\$67mn</b>	Citigroup Venture Capital - Unimark Remedies <b>US\$26mn</b>

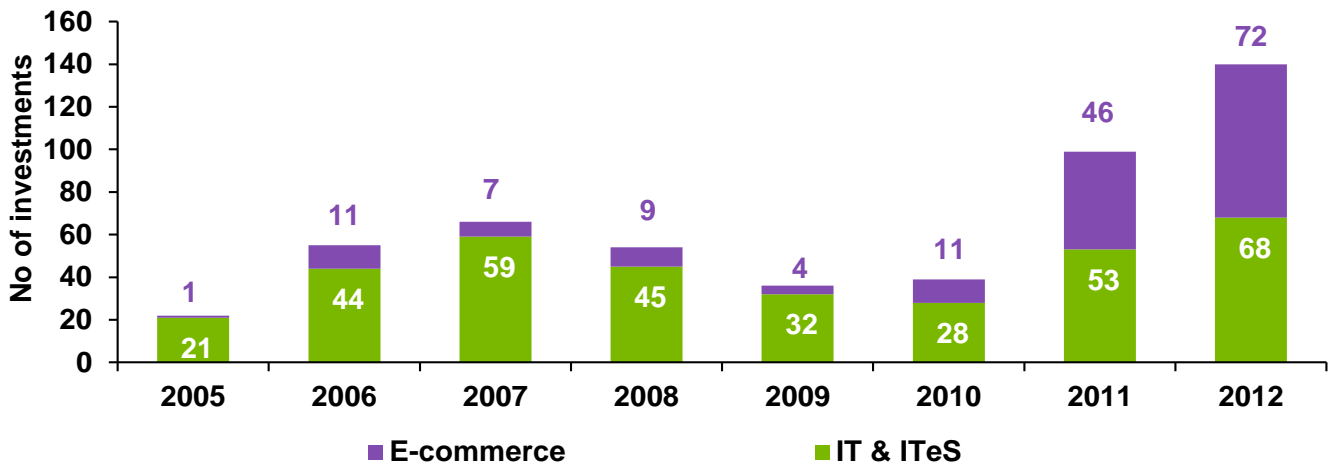
Source : Grant Thornton Dealtracker and Grant Thornton analysis

# PE: IT & ITeS

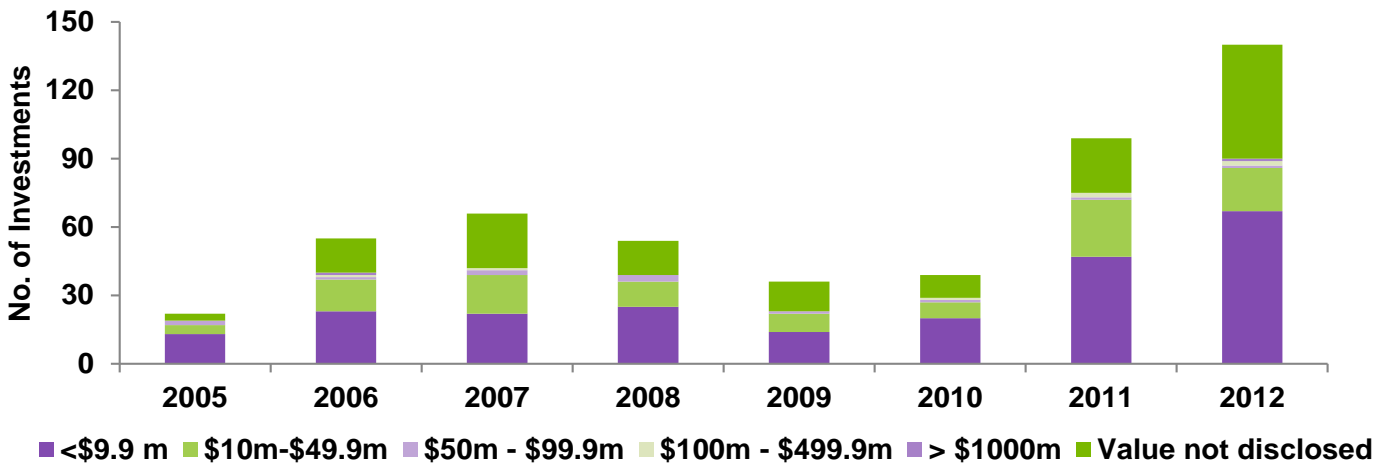
Total PE investments (value) (2005 – 2012)



Total PE investments (volume) (2005 – 2012)



PE investment ranges (2005 – 2012)



Source : Grant Thornton Dealtracker and Grant Thornton analysis

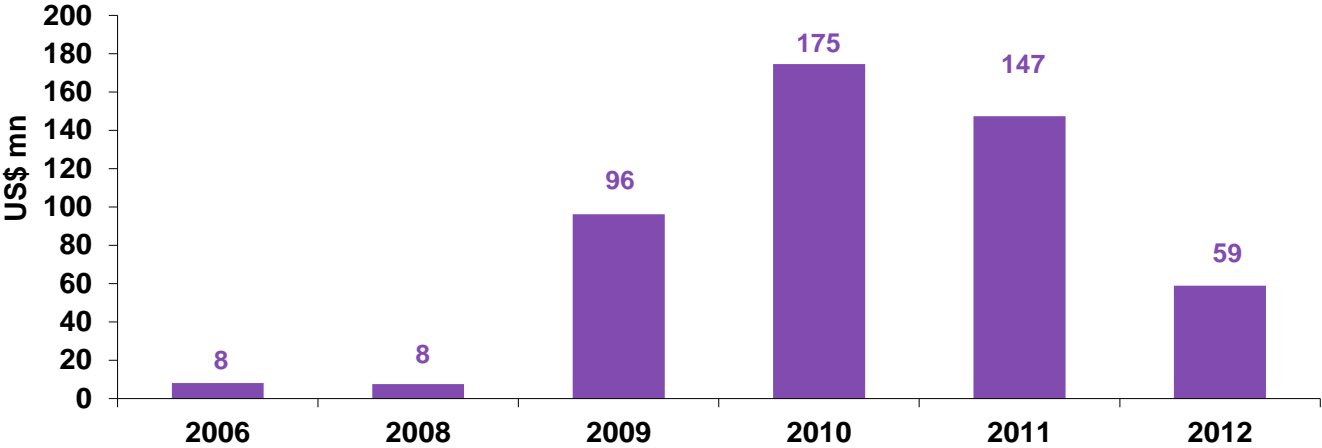
# PE: IT & ITeS

Large deals (2007 – 2012)			
2012	Bain Capital Genpact <b>US\$1000mn</b>	Accel Partners and Tiger Global - Flipkart Online Services <b>US\$150mn</b>	Naspers and Tiger Global - Flipkart Online Services <b>US\$150mn</b>
2011	Apax Partners - iGate Corporation <b>US\$480mn</b>	Cerberus Capital - Regulus Group and J&B Software, <b>US\$137mn</b>	General Atlantic - Mu Sigma <b>US\$93mn</b>
2010	Goldman, Indivision & Oak – Trikona Digital <b>US\$106mn</b>	Warburg Pincus - QuEST Global Services <b>US\$75mn</b>	Sequoia Capital -iYogi <b>US\$30mn</b>
2009	Goldman, Indivision, Oak & Green Lotus – Trikona Digital <b>US\$53mn</b>	Intel Capital - One97 Communication, Global Talent Track & IndiaMART.com <b>US\$23mn</b>	Fidelity, IDG, DFJ, ePlanet - Manthan Systems <b>US\$15mn</b>
2008	Blackstone – CMS Computers <b>US\$56mn</b>	Undisclosed investor - CtrlS Datacenters <b>US\$56mn</b>	Daiwa Securities, Ridgeway Capital & India Knowledge Fund - Soma Networks <b>US\$ 51mn</b>
2007	Blackstone Group– Intelenet Global Services <b>US\$200mn</b>	General Atlantic & Carrier International - Infotech Enterprises <b>US\$75mn</b>	General Atlantic - IBS Software Services <b>US\$60mn</b>

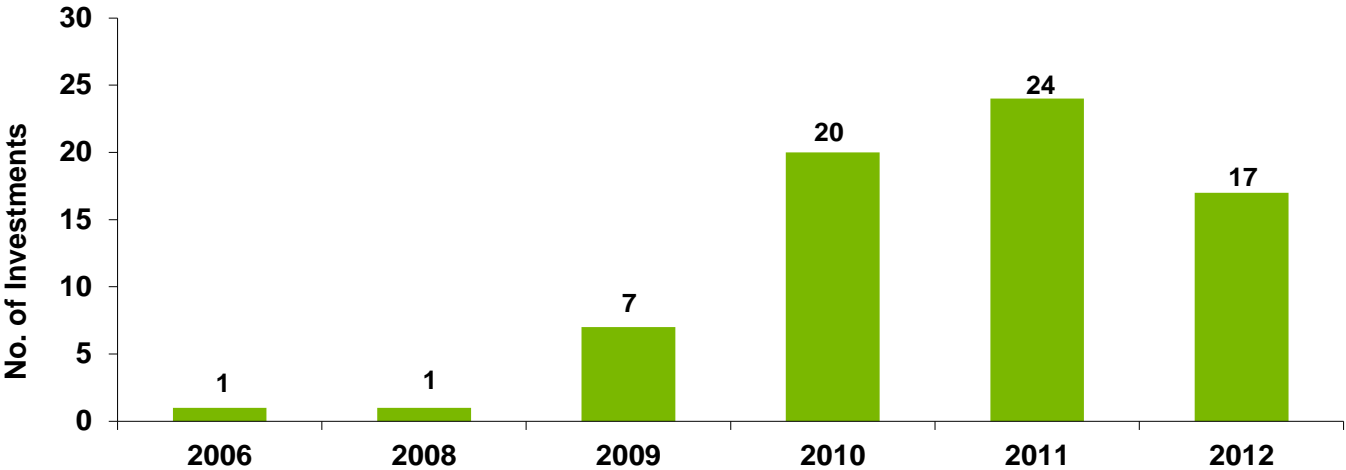
Source : Grant Thornton Dealtracker and Grant Thornton analysis

# PE: Education

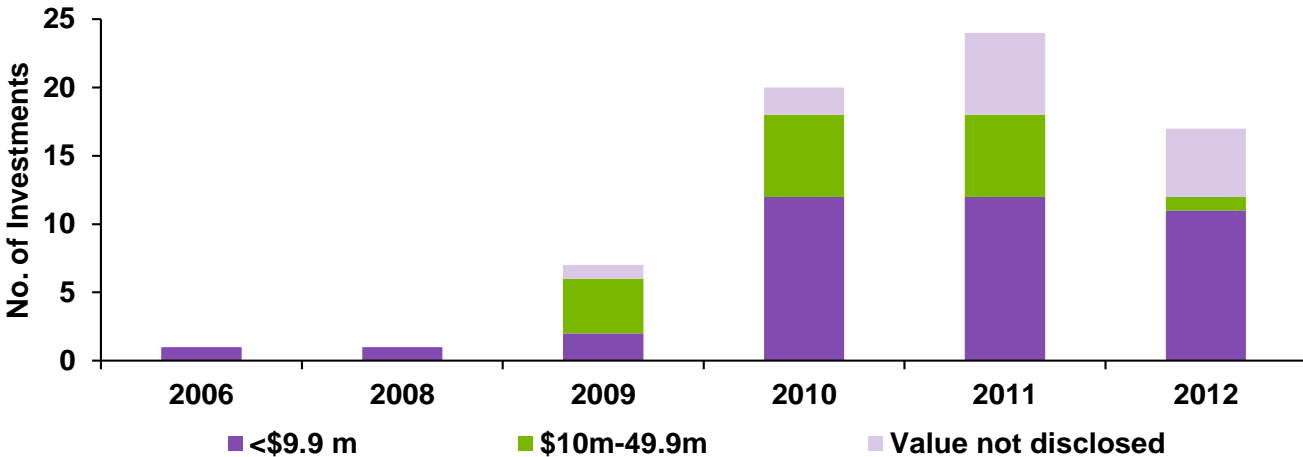
Total PE investments (value) (2006 – 2012)



Total PE investments (volume) (2006 – 2012)



PE investment ranges (2006 – 2012)



Source : Grant Thornton Dealtracker and Grant Thornton analysis

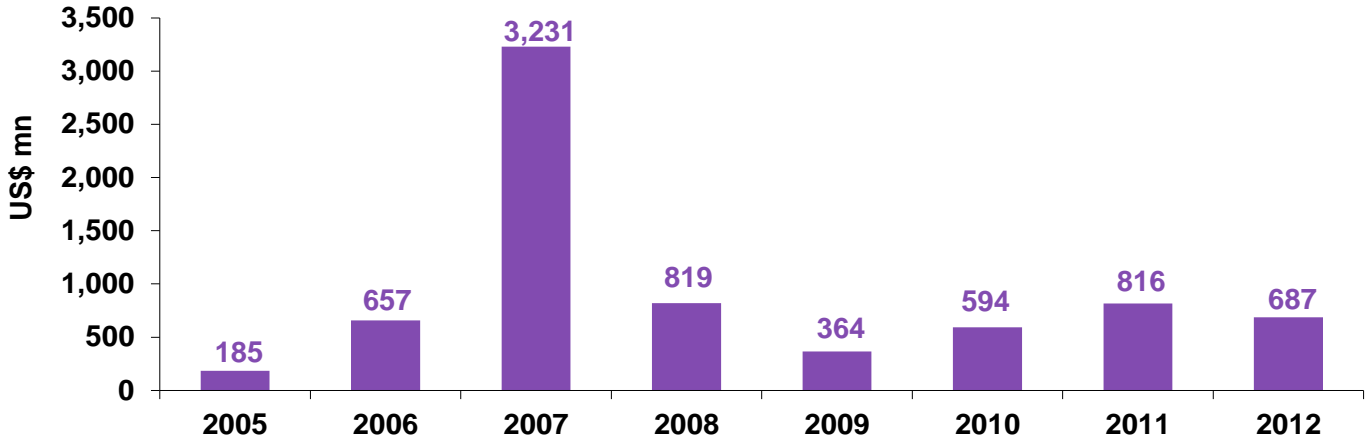
# PE: Education

Large deals (2008 – 2012)			
YTD 2012	New Silk Route Partners - Varsity Education <b>US\$30mn</b>	Sequoia Capital - Edusys Services <b>US\$8mn</b>	Kaizen , Accel, Catamaran & some angel investors - Ace Creative Learning <b>US\$ 5mn</b>
2011	Ascent Capital - Oakridge International School <b>US\$33mn</b>	New Silk Route - Sri Chaitanya Educational Group , <b>US\$25mn</b>	CLSA Capital Partners - Resonance Eduventures <b>US\$22mn</b>
2010	PremjiInvest - Manipal Universal Learning <b>US\$43mn</b>	India Equity Partners - IL&FS Education and Technology <b>US\$37mn</b>	Reliance Capital Pathways World School <b>US\$21mn</b>
2009	Navis Investment Partners - Edutech India <b>US\$30mn</b>	Quantum (M) - Educomp Solutions <b>US\$25mn</b>	Matrix Partners India - FIIT JEE <b>US\$22mn</b>
2008	Matrix Partners India Tree House Education <b>US\$8mn</b>		

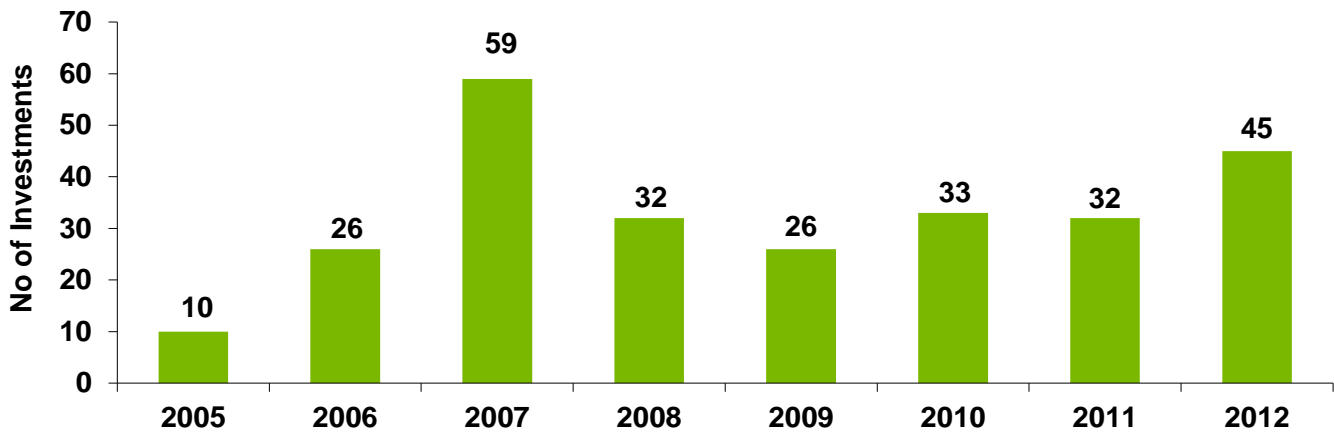
Source : Grant Thornton Dealtracker and Grant Thornton analysis

# PE: Banking and Financial Services

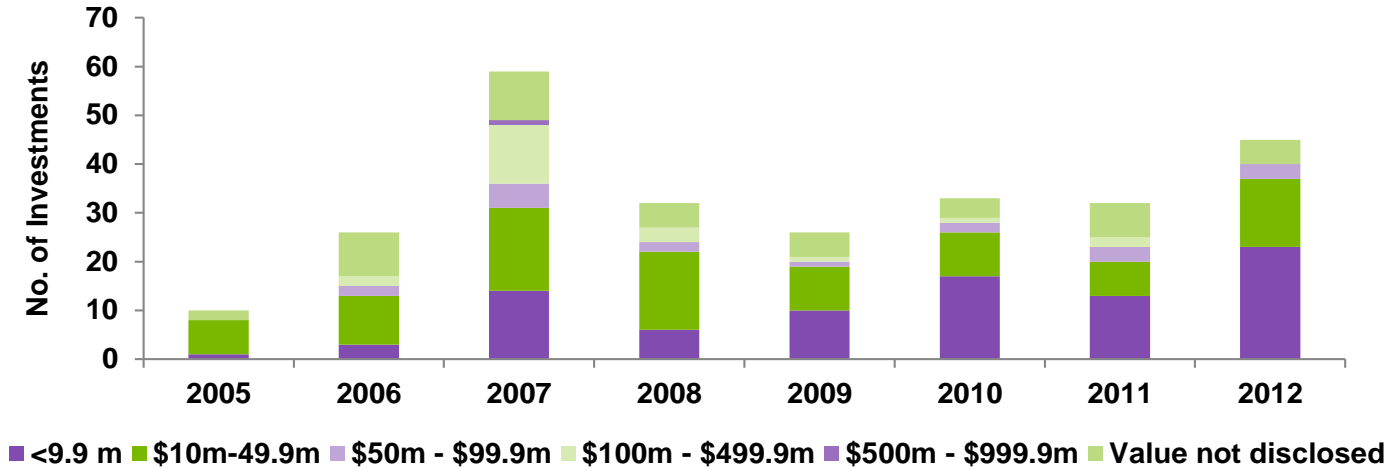
## Total PE investments (value) (2005 – 2012)



## Total PE investments (volume) (2005 – 2012)



## PE investment ranges (2005 – 2012)



Source : Grant Thornton Dealtracker and Grant Thornton analysis

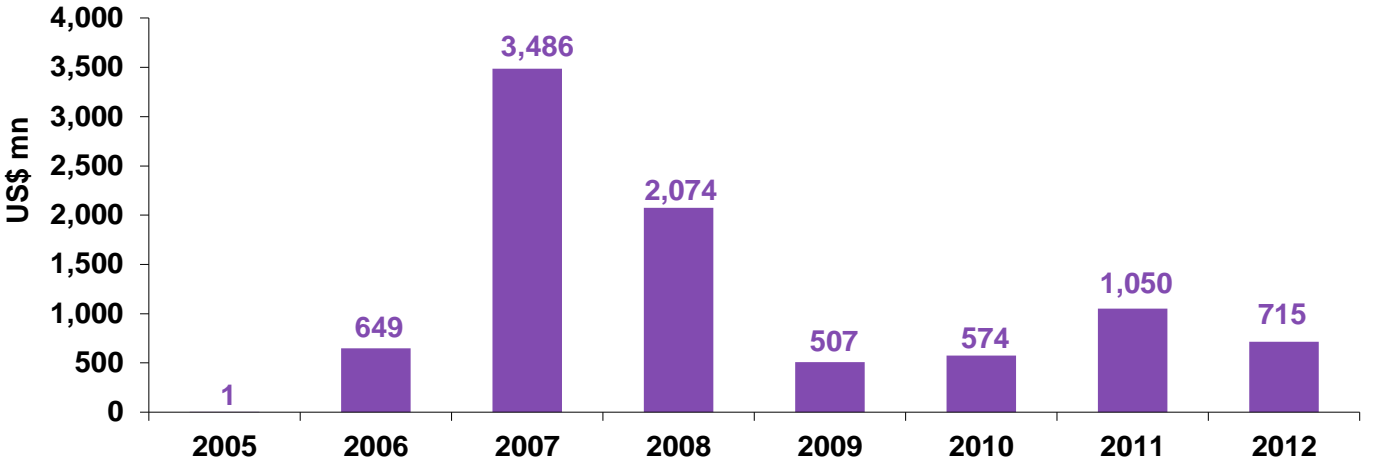
# PE: Banking and Financial Services

Large Deals (2007 – 2012)			
2012	Warburg Pincus - Future Capital Holdings <b>US\$84mn</b>	International Finance Corporation - Religare Enterprises <b>US\$75mn</b>	Warburg Pincus - AU Financiers <b>US\$50mn</b>
2011	Texas Pacific Group - Shriram Capital <b>US\$257mn</b>	HDFC, NVP, Beacon India, Cartica Capital, Faering Capital, Gaja Capital & Samara Capital - Ratnakar Bank <b>US\$157mn</b>	Capital International - L&T Finance Holdings <b>US\$74mn</b>
2010	ICICI Venture, Carlyle & Sequoia Capital - Star Health <b>US\$100mn</b>	Actis - IDFC <b>US\$98mn</b>	Khazanah Nasional Bhd - IDFC <b>US\$81mn</b>
2009	Goldman Sachs -MAX India <b>US\$115mn</b>	New India Assurance and LIC- AXIS Bank <b>US\$80mn</b>	Tube Investments - Cholamandalam Investment & Finance <b>US\$33mn</b>
2008	TPG Capital - Shriram Retail Holdings <b>US\$133mn</b>	TPG-Axon & Standard Chartered - Mahindra & Mahindra Financial <b>US\$104mn</b>	PremjiInvest - National Stock Exchange <b>US\$100mn</b>
2007	Carlyle Group - HDFC <b>US\$650mn</b>	BNP Paribas - SREI Infrastructure Finance <b>US\$180mn</b>	Khazanah Nasional Berhad - IDFC <b>US\$180mn</b>

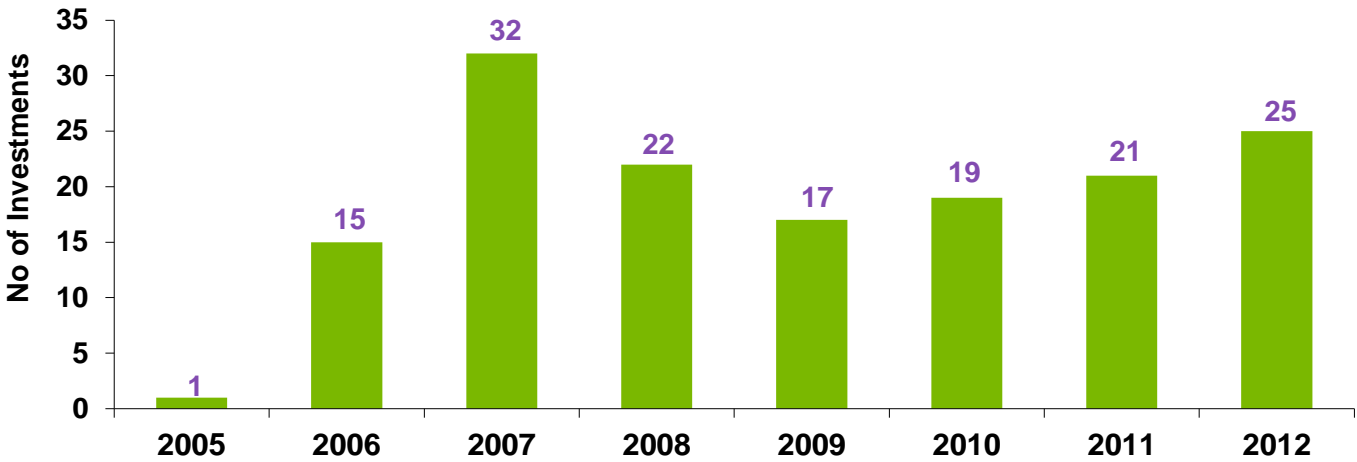
Source : Grant Thornton Dealtracker and Grant Thornton analysis

# PE: Real Estate

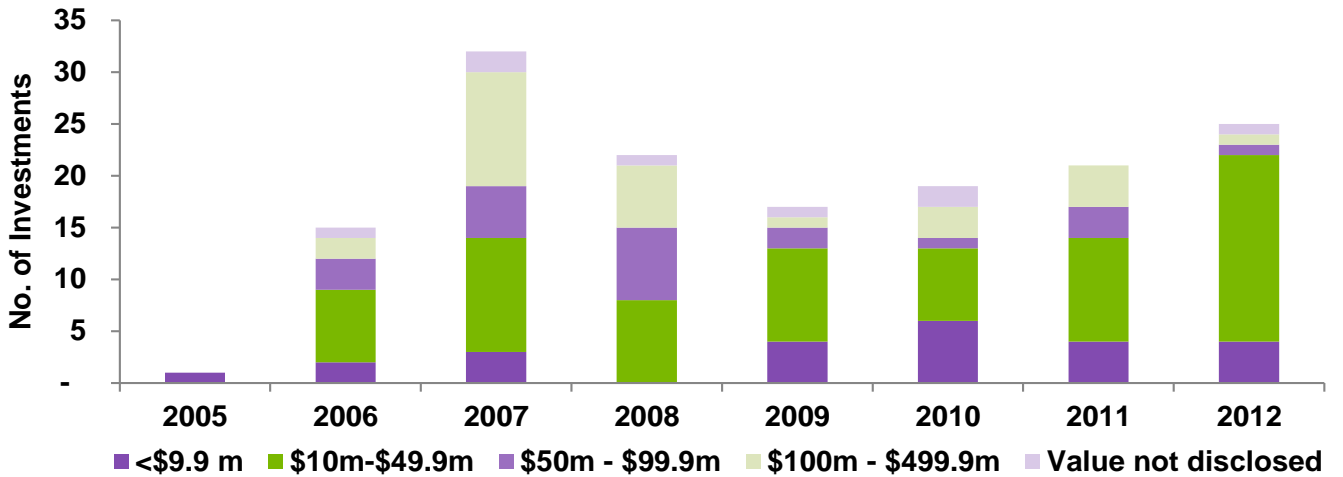
## Total PE investments (value) (2005 – 2012)



## Total PE investments (volume) (2005 – 2012)



## PE investment ranges (2005 – 2012)



Source : Grant Thornton Dealtracker and Grant Thornton analysis

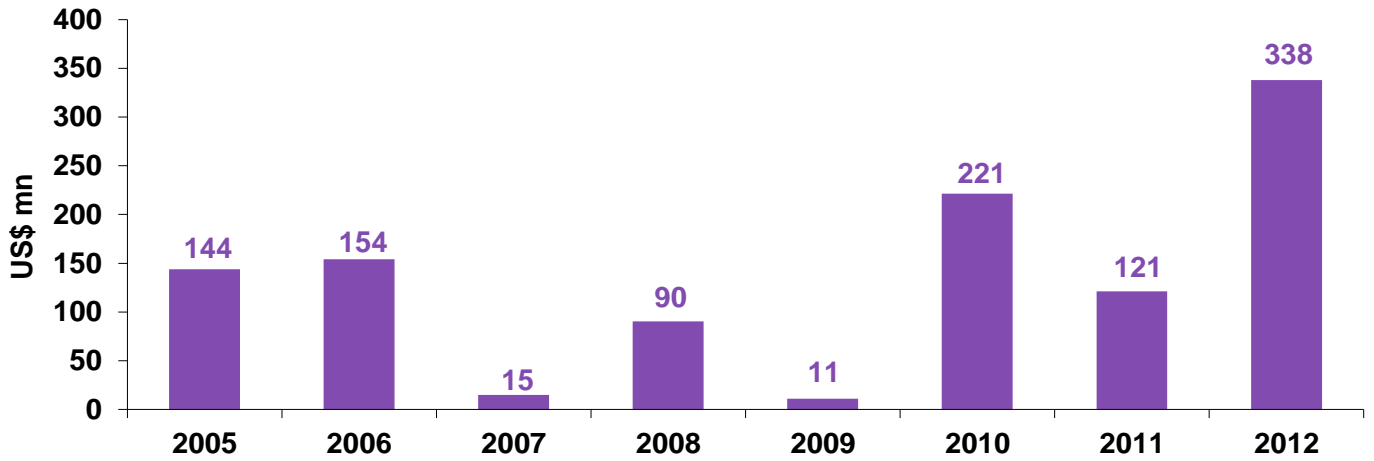
# PE: Real Estate

Large investments (2007 – 2012)			
2012	Blackstone - Embassy Property -portfolio of three business parks <b>US\$200mn</b>	Morgan Stanley RE - Sheth Developer's Mumbai project <b>US\$90mn</b>	Brick Eagle Capital - Xrbia Developers <b>US\$40mn</b>
			Xander Group - Appaswamy RE (Chennai Project) <b>US\$40mn</b>
2011	Blackstone - Embassy Property (Manyata) <b>US\$200mn</b>	Blackstone - DLF Ackruti Info Parks <b>US\$176mn</b>	J.P. Morgan Asset Management - Soma Group <b>US\$110mn</b>
2010	ASK Property - Amit Enterprises (Darode Jog) <b>US\$112mn</b>	Xander Group - Panchshil Realty <b>US\$110mn</b>	HDFC Venture Funds - Lodha Developers (World One) <b>US\$106mn</b>
2009	Oman Sovereign fund - Mohtisham Estates <b>US\$138mn</b>	IL&FS Investment -HBS Realtors <b>US\$67mn</b>	Sun Apollo RE Fund & Mausmi Ventures - Keystone Realtors <b>US\$67mn</b>
2008	Symphony Capital -DLF Assets <b>US\$450mn</b>	MPC Synergy -Phoenix Mills <b>US\$325mn</b>	DE Shaw Group - Mack Star Marketing <b>US\$250mn</b>
2007	Deutsche Bank - Lodha Group (25%in SPV) <b>US\$425mn</b>	DE Shaw Group - DLF <b>US\$400mn</b>	Merrill Lynch & Co - DLF (7 Residential Projects) <b>US\$377mn</b>

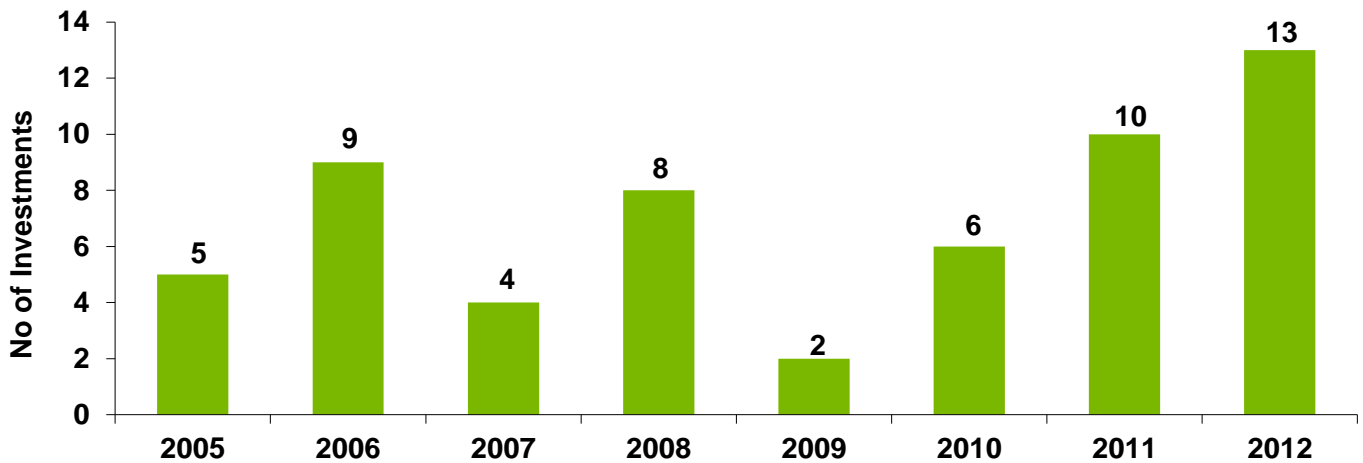
Source : Grant Thornton Dealtracker and Grant Thornton analysis

# PE: FMCG, Food & Beverages

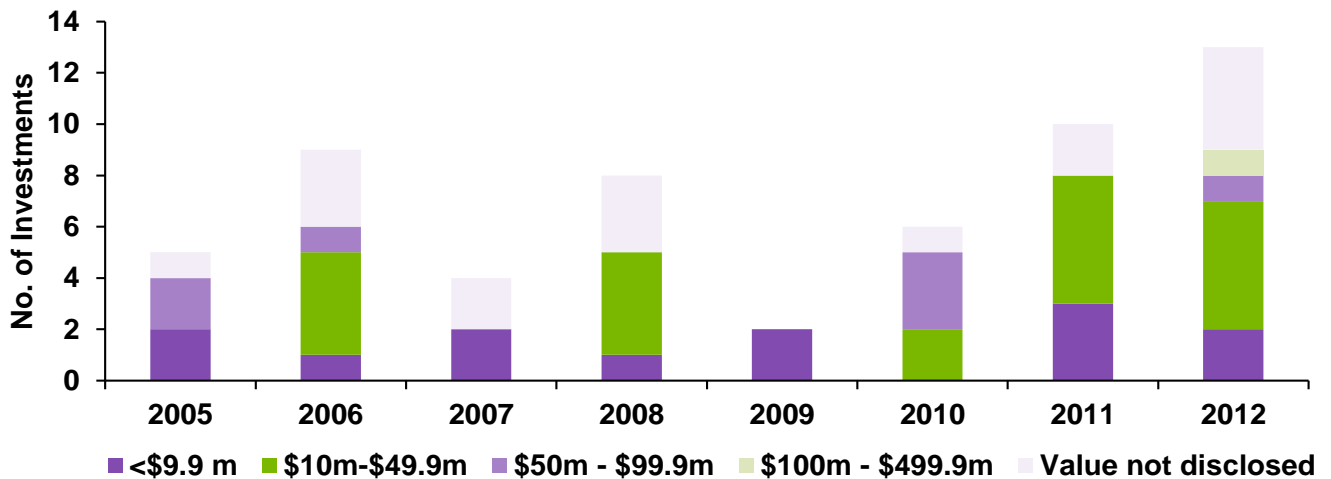
Total PE investments (value) (2005 – 2012)



Total PE Investments (Volume) (2005 – 2012)



PE Investment Ranges (2005 – 2012)



Source : Grant Thornton Dealtracker and Grant Thornton analysis

# PE: FMCG, Food & Beverages

Large Investments (2007 –2012)			
2012	Temasek Holdings - Godrej Consumer Products <b>US\$137mn</b>	GIC - Marico <b>US\$75mn</b>	Blackstone - SH Kelkar & Company <b>US\$44mn</b>
2011	Sequoia Capital - Prakash Snacks <b>US\$30mn</b>	Reliance Equity Advisors - VVF <b>US\$30mn</b>	Standard Chartered PE - Bush Foods Overseas <b>US\$25mn</b>
2010	Kohlberg Kravis Roberts - Coffee Day Holding <b>US\$75mn</b>	New Silk Route - Coffee Day Holding <b>US\$ 75mn</b>	Standard Chartered PE - Coffee Day Holding <b>US\$50mn</b>
2009	Rabo Equity Advisors - LT Foods <b>US\$6mn</b>	Rabo Equity Advisors - Daawat Foods <b>US\$5mn</b>	
2008	Indivision India Partners - Blue Foods <b>US\$33mn</b>	Darby's Asia Mezzanine Fund - Coffee Day Holding <b>US\$25mn</b>	Motilal Oswal VC - Parag Milk Foods <b>US\$15mn</b>
2007	SAIF Partners - Asian Dhall Industries <b>US\$8mn</b>	Argonaut PE - Vallabhdas Kanji <b>US\$7mn</b>	

"The India Agri and Allied sector presents an interesting play for PE investors. The very challenges faced by Indian Agri Sector- dependence on rain; fragmented land holdings; lack of awareness of modern methods of farming; poor infrastructure facilities; all present significant business opportunities.

Earlier investments were made in various established sub sectors like fertilisers, seeds, edible oils and now PEs are looking more towards investment in bio fertilisers, infrastructure and logistics. The allied sectors like horticulture, dairy, fisheries and poultry have also caught the attention of PEs. Capital flows to the various sub sectors are not without challenges. There is the issue of deal size and scalability along with the unorganised nature of operations and inadequate corporate governance. PEs would do well to address these issues to tap into the vast opportunity of the Indian Agri sector."

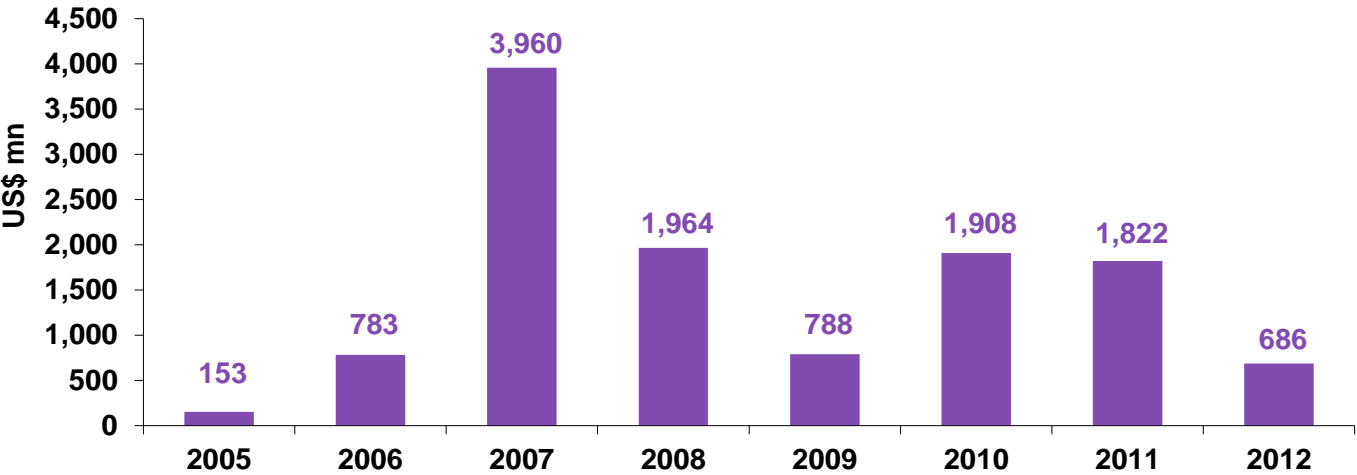
**Dhanraj Bhagat**  
Partner, Transaction Advisory Services  
Grant Thornton –India



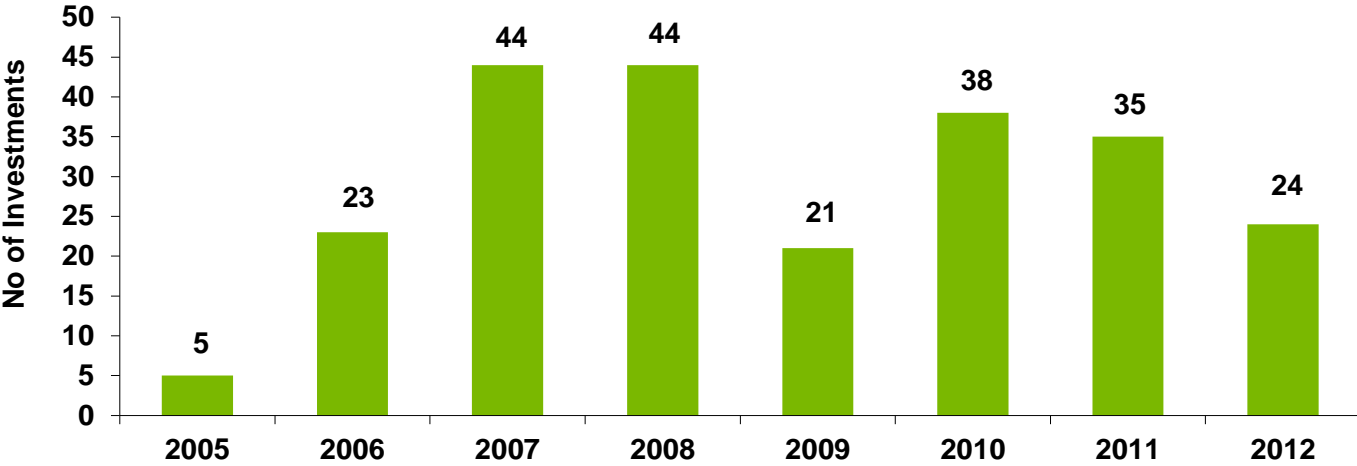
Source : Grant Thornton Dealtracker and Grant Thornton analysis

# PE: Power, Energy and Infrastructure

**Total PE investments (value) (2005 –2012)**



**Total PE investments (volume) (2005 –2012)**



**PE investment ranges (2005 – 2012)**



Source : Grant Thornton Dealtracker and Grant Thornton analysis

# PE: Power, Energy and Infrastructure

Large Investments (2007 – 2012)			
2012	Morgan Stanley - Continuum Wind Energy <b>US\$210mn</b>	Macquarie SBI - Ashoka Concessions <b>US\$150mn</b>	Airro Mauritius, JP Morgan (fund) - Nandi Economic Corridor . <b>US\$65mn</b>
2011	Macquarie SBI Infrastructure - GMR Infrastructure <b>US\$200mn</b>	Standard Chartered PE, JM Financial-Old Lane & NYLIM Jacob Ballas India - GMR Infra <b>US\$200mn</b>	Goldman Sachs - ReNew Wind Power <b>US\$200mn</b>
2010	Blackstone - Moser Baer India <b>US\$300mn</b>	3i India Infrastructure Fund - GVK Industries <b>US\$255mn</b>	Temasek Holdings - GMR Infrastructure <b>US\$200mn</b>
2009	Fire Capital Fund FIRE Arcor Infrastructure Pvt Ltd <b>US\$250mn</b>	CVC, Sequoia Capital & Bessmer Venture - Ind Barath Infra <b>US\$100mn</b>	IDFC- Essar Power <b>US\$78mn</b>
2008	Orient Global Tamarind – Cairn India <b>US\$279mn</b>	Farallon Capital- Indiabulls Group <b>US\$247mn</b>	Lehman Brothers - Unitech- Western Expressway Project in Mumbai <b>US\$185mn</b>
2007	ICICI Venture – Jaypee Infratech <b>US\$800mn</b>	George Soros, Eton Park, Deutsche Asset Mgmt Capital International, Citigroup, T Rowe Price, Credit Agricole, UBS and Kotak Mahindra - GMR Infrastructure <b>US\$767mn</b>	Avenue Capital - SKIL Infrastructure <b>US\$500mn</b>

Source : Grant Thornton Dealtracker and Grant Thornton analysis

# Global PE trends

Extracts from the Global Survey of Private Equity conducted by Grant Thornton International in 2012. \*

\*Write to [contact@in.gt.com](mailto:contact@in.gt.com) for a copy of the report

- Indonesia, Peru, Colombia and Turkey top list of new “high growth” markets where PE is likely to see the most opportunities
- deal activity expected to slow in China and India
- foreign trade buyers seen as most likely exit route, notably those from Japan, China and Korea
- dramatic drop in fundraising confidence and economic outlook

PE firms around the world are bracing for tough conditions for both fundraising and deal-making, according to the 2012 Global PE report. This report is the result of 143 in-depth interviews with senior PE practitioners around the globe.

### Key finding from Grant Thornton International's Global PE report:

#### Fundraising fears

This year's report sees a marked decline in fundraising expectations of GPs around the world, with nearly three-quarters (72 per cent) describing the fundraising outlook as either “negative” or “very negative”. In 2011, the figure was just 46 per cent.

The most dramatic decline in optimism from 2011 is evident in the BRICS: Brazil, Russia, India, China and South Africa. This year, 78 per cent of respondents in these markets described the fundraising outlook as “negative” or “very negative”. In 2011, the figure was 39 per cent.

#### How do you view the current fundraising environment?

Outlook	2012	2011
Very Positive	1%	4%
Positive	11%	24%
Neutral	15%	26%
Negative	33%	33%
Very Negative	39%	13%
Very Positive	1%	4%

Source: Global PE Report 2012, Grant Thornton International

PE firms are expecting to have to turn to a greater number of new investors – or limited partners – and rely less on their existing LPs to make follow-on commitments to their next funds. This year, 40 per cent of respondents said they expect their next fund to be majority funded by first time investors. In 2011's report, this figure was only 24 per cent.

“Though fundraising remains a key challenge, for those firms with a successful track record, a coherent strategy and a quality team that can deliver that strategy, fundraising will be more straightforward. This evolution will see a widening of the gap between the successful & less successful firms and inevitably winners & losers in the industry, as raising funds for those underperforming firms becoming increasingly challenging, if not impossible,”

**Martin Goddard**  
Global service line leader, Transactions  
Grant Thornton International

# Global PE trends

## Global exit routes

PE firms are looking across borders for exit routes, in particular to overseas trade buyers. More than half of the respondents (52 per cent) expect the majority of the trade buyers they transact with in the near term to be foreign, while 28 per cent expect to deal mostly with domestic trade buyers. The remaining 20 per cent expect the trade buyers to be either foreign or domestic (50-50).

Globally, China-Japan, Europe-North America are the regions from which most GP's expect non-domestic strategic buyers to originate.

“Of particular interest is the expected significance of Japan, reflecting the fact that the strong Yen coupled with sluggish domestic demand is encouraging international expansion. PEs globally expect to see Japanese buyers, and this is particularly the case in Europe, India and Asia Pacific.” – **Global PE Report 2012, Grant Thornton International**

## Indonesia tops list of new “high growth” markets

PE firms based in high growth markets, such as those in Latin America, South Africa and the Asia Pacific, most frequently cited Indonesia when asked to identify foreign markets with the most potential for PE investment.

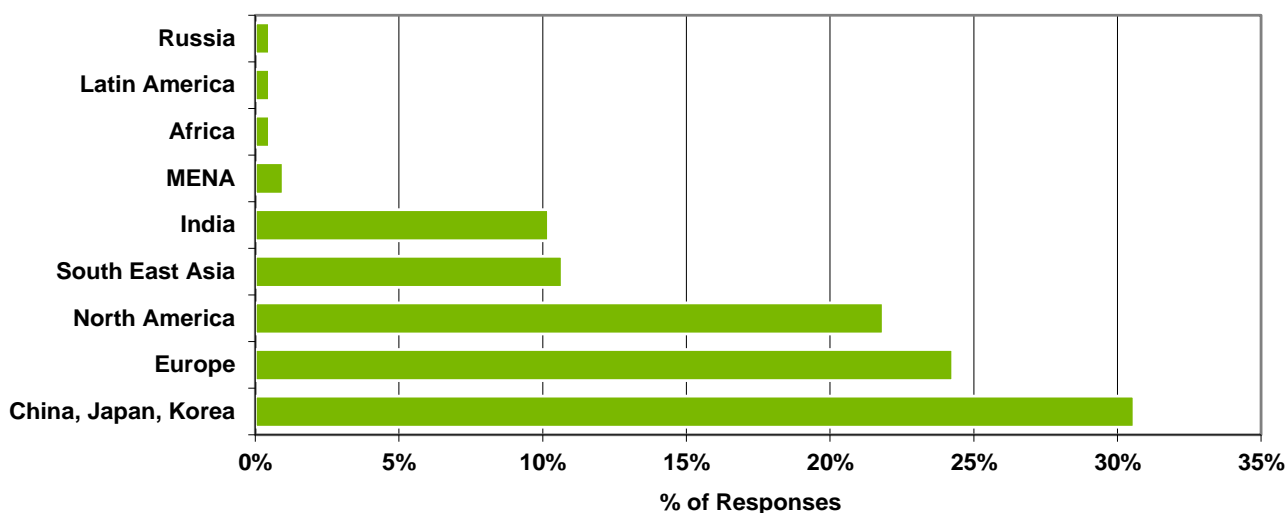
### Top 10 new “high growth” markets

1	Indonesia
2	Peru
3	Colombia
4	Turkey
5 =	Myanmar
5 =	Egypt
5 =	Saudi Arabia
8 =	Mexico
8 =	Ghana
8 =	Malaysia

Source: Global PE Report 2012, Grant Thornton International

Which new geographical markets do you consider to be the most likely source of acquirers for your portfolio businesses?

### Regions Expected to be Source of Non-Domestic Acquirers



While growth in “high-growth” countries outstrips that seen in western markets, the search for growth leaves local PE firms to keep a watchful eye on where tomorrow’s deal flow will originate, particularly as some of their home markets show signs of overheating.

“Whereas a move to new unknown territories may be a risk too far for many western funds, investors based in high-growth regions typically have good visibility of the next frontier markets within their region.” – **Global PE Report 2012, Grant Thornton International.**

### Economic sentiment worsens

The drive to harness growth is set against a backdrop of deteriorating sentiment around the global economy. Nearly half (48 per cent) of this year’s respondents have either a negative or neutral economic outlook for their portfolio businesses. This compares unfavourably with last year’s survey, in which only 38 per cent of respondents held these views.

### Economic outlook for portfolio companies

Outlook	2012	2011
Very positive	6%	10%
Positive	46%	53%
Neutral	29%	30%
Negative	15%	7%
Very negative	4%	0%

Source: *Global PE Report 2012, Grant Thornton International*

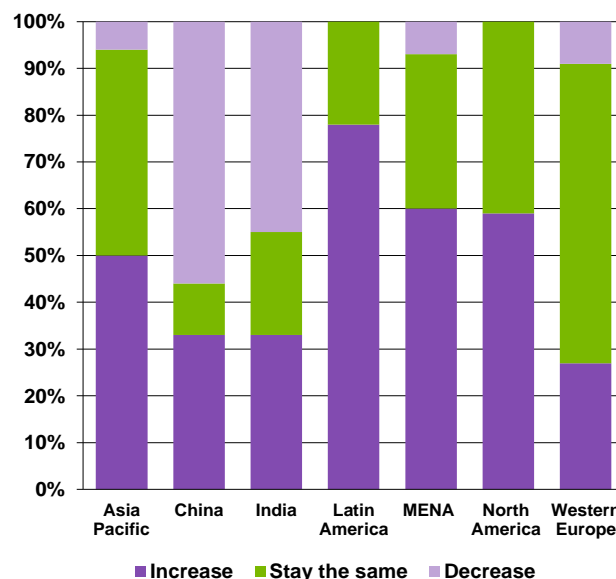
### Deal slowdown in China and India

While respondents globally expect PE investment activity to increase over the coming year, expectations are more cautious than they

were in 2011 and differ significantly from region to region.

New deal activity in Western Europe is widely expected to remain subdued, with only 27 per cent of respondents predicting an increase in the next 12 months. This contrasts with North America, where 59 per cent of respondents predict an increase, and MENA, where the figure is 60 per cent.

### Expected investment activity by region



MENA (Middle East & North Africa)

Even in some of the markets which have expanded rapidly over recent years, the speed of growth has slowed noticeably and practitioners are increasingly realising that these economies are not immune to the impacts of the global downturn.”

– **Global PE Report 2012, Grant Thornton International.**

# Global PE trends

There is enormous expectation for growing new deal activities in Latin America (78 per cent expect this), which represents only a slight dampening of last year's sentiment; in 2011, 89 per cent of respondents expected deal activity to increase in the region.

Many PE executives expect both China and India to suffer a decline in deal activity in the next 12 months. This represents a dramatic turnaround in sentiment for both countries. In 2011, 78 per cent of respondents expected investment activity in India to increase, with the remaining 22 per cent expecting it to remain steady. This year, 45 per cent expect it to decline.

## Sample and methodology

Between July and September 2012, 143 interviews were conducted with top executives from PE firms. Respondents included general partners in five principal regions/categories:

32%	Western Europe
21%	North America (USA and Canada)
26%	BRICS (Brazil (and broader Latin America), Russia, India, China, South Africa)
11%	Asia Pacific
10%	MENA (Middle East and North Africa, including Turkey)

Interviews included a mixture of quantitative and qualitative questions. Arbor Square Associates, an independent research firm, conducted the research.

“Private equity in emerging markets is challenging because of the governance risks and the absence of deep capital and M&A markets to enable exits. An understanding of the local situation is key to success in these markets.”

**Harish HV**

**Partner, India Leadership Team**

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# PE lifecycle



# Commercial due diligence

**Vivek Vikram Singh**  
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## What is it really about?

An 'ideal deal' would more often than not, include most of the following characteristics:

- a target company that operates in an industry that is projected to grow at a rapid rate
- a target company that differentiates itself from its competitors
- a diverse universe of customers
- synergies with operations already part of the buyer's portfolio

And, most importantly...

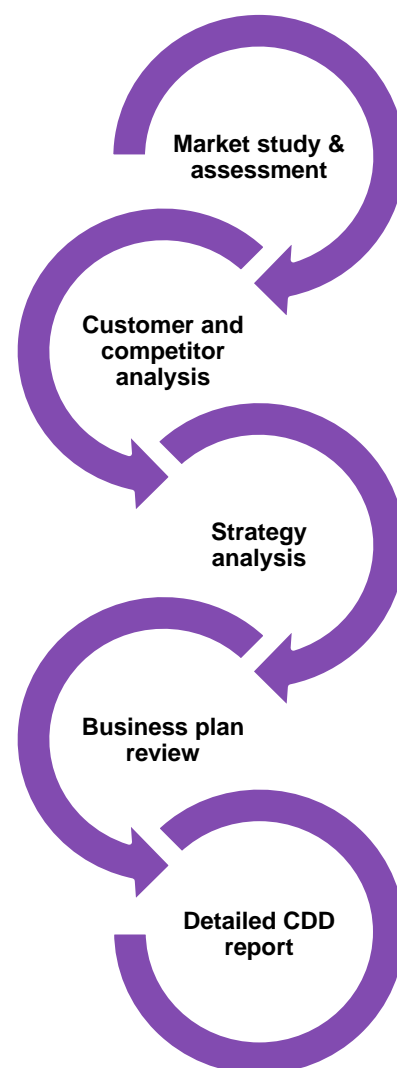
- a justifiable price

Outside of a utopian world, seldom would these factors ever occur together and if they do the seller's definition of a justifiable price might be significantly different from yours. Commercial Due Diligence (CDD) in its simplest form, is the process of appraising a target with reference to its external environment and taking a call on the achievability of its future projections, given current and the likely scenarios of supply-demand, competition and regulations.

## The broad definition of a CDD

A CDD can be defined as 'the investigation conducted by a potential acquirer in order to ratify that it is buying what it thinks it is buying.' A CDD report should therefore aim to answer some of the major questions pertaining to the company's business proposition and how it is poised to fare against market forces such as:

- what business is the company in? Is the business itself attractive to investors?
- is the market competitive enough? If so, how are we different?
- how is my brand and product/service perceived by my customers/end consumers
- is the product/service able to satisfy the customer's stated and/or latent needs?
- are the forecasts backed by market demand, in the current scenario and also in the future?
- is the target's business plan, with all its underlying assumptions viable in the current market scenario?



# Commercial due diligence

## What can you expect?

The objective of a CDD is about decreasing the risk associated with an acquisition by filling the information gaps that are crucial to the acquirer's understanding of the target. This risk can come from four broad sources; market, customers, competitors and business strategy. Each of these factors is examined independently at first, to provide a micro level assessment of the target's operations. Subsequently the endeavor is to link all these elements to provide quantified impacts on forecasts of company level financials.

## Market assessment

The risk here is that the market may not be as vast as assumed or growing as rapidly as projected or might be unsuited to deliver expected returns.

Questions we can answer:

- is this the right time to buy?
- what is the immediate and long term impact of changes to the regulatory environment?
- what is the immediate and long term impact of changes in technology, product innovation or changes in distribution model (e.g. the advent of e-retail)?
- how large are the market segments which the target serves today and how fast are they growing?
- is the company positioned in a growing market which supports management projections?

## Customer analysis

The main objective of customer referencing is to establish customers' key buying criteria and their future expectations.

Questions we can answer:

- who is the company's target market?
- are there unfulfilled customer requirements?
- can we prove the stability, longevity and growth potential of their customer base?
- is there a risk that the type and volume of business, the existing customers have with the company may change?

## Competitor analysis

The main purpose of surveying the competition is to assess the competition's relative strengths and weaknesses.

Questions we can answer:

- who are the chief competitors for the target?
- is there a threat of substitutes / new entrants to the target's market?
- what is the sustainable competitive advantage of the business and can it achieve its forecasts?
- what is the impact of competitors' activity on the target's market share?

"We do a lot of due diligence on the companies and the entrepreneurs before making any investment. We also do a lot of reference checking before, to make sure there is a high standard of ethics in the company."

**Samir Kumar**  
Managing Director  
Inventus Capital

# Commercial due diligence

## Business strategy review

In its fullest form a CDD must assess the target's capability to deliver in the future. It is necessary to review all the major assumptions of the five year business plan on products, pricing, volume, market share, key costs, new business opportunities, geographies/regions served etc.

Questions we can answer:

- what is the difference between the past and future business strategy?
- what is the synergy between the future strategy and the expected market conditions?
- is the target company's expansion strategy viable?

## Conclusion

Acquisitions can be fairly risky if the buyer does not make an informed decision. More acquisitions fail than succeed, because they focus on short term gains rather than long term successes.

To prevent this, a CDD provides the much required awareness on the future of the target and the merged entity. A comprehensive CDD should also assess the target's strategic fit and synergy to help ensure smoothness in post-merger integration.

The result of this investigation then becomes fundamental in defining the target company's value to the acquirer, and eventually determining the 'justifiable price'.

"Independent accounting diligence has gained grounds as an imperative action prior to an investment or acquisition. It has gained significance and strength with a few reported disillusionment on some transactions. What is obvious in those transactions was possibly discounting of the diligence process, which has primarily lead to an impairment of the investment or not providing the desired synergy value. Moreover, accounting standards are complex in an equally complex business environment.

Hence diligence should be tailored to have a clear understanding of the business model of the investee or the acquired and the adopted accounting standards to assess if they are appropriately applied to reflect fair value of the financial performance."

**Sridhar V**  
**Partner, Transaction**  
**Advisory Services**  
**Grant Thornton –India**



# Financial Frauds – Risks and challenges



**Anil Roy**  
Partner & Leader, Forensic & Investigation Services  
Grant Thornton - India

Fraud has something in common with God! They are both omnipresent, waiting for the right environment and an opportunity to manifest themselves. Here we will focus on fraud and leave God at the mercy of religious leaders and politicians.

There are two key elements in fraud – opportunity and the probability of getting caught being low. These are the two elements that differentiate a secure and safe organisation from a porous and an easy target for fraudsters. These are also the two elements which an organisation can control, easily.

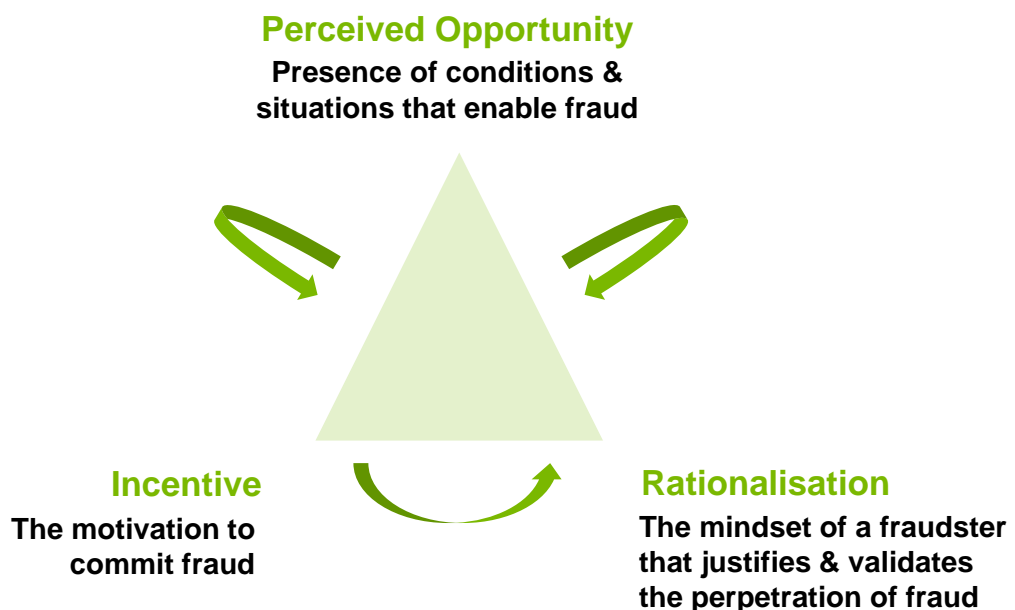
Incentive and rationalisation are influenced by a number of factors which extend beyond the confines and control of an organisation, these could be – economic, social, cultural, bad habits, peer pressure, to name a few.

In the globalised economy of the 21st century the relationship between risk and reward is tighter than ever – while opportunities are arising at an unprecedented rate, so are the risks.

While we often address our transaction risks, it's the fraud risk that is often ignored having larger ramifications including reputation.

In today's fraud ridden environment, PE firms operating in the Indian market face an increasing number of risks. These can be classified into financial, operational and reputational risk and are summarised below.

Corporate Resolutions, Inc. polled CFOs of U.S. PE and venture capital funds for a survey. It was revealed that 39 per cent of all respondents had encountered fraud at some point



# Financial Frauds – Risks and challenges

during their tenure as CFOs within their own firms or at a portfolio company, 81 per cent had not invested in a company because of suspected fraud or integrity issues.

The nature of the PE industry makes it susceptible to various frauds at different stages of operation as set out below:

## Pre-investment

### Fraudulent or misrepresented data

The value of the portfolio company is based on the financials and other data provided by it. PE firms face the risk of basing their investment decision on inflated or misrepresented data by the promoters of the target company.

### Inadequate background checks

A PE firm not only invests in the company but also its promoters and key personnel. With scarce information about the

company or the promoters, the PE firm faces the risk of being associated with unethical practices and people. If the firm fails to carry out stringent and adequate background checks, it may impact its business negatively and damage its reputation.

Important information which may be deliberately hidden from the PE firm includes litigation history of the company or its promoters, potential illegal activities, links with politically exposed people, or credentials and reputation of the promoters.

### Inadequate controls for combating corruption

PE firms face the risk of basing the value of the portfolio company on key revenue generating contracts or relationships which were acquired through corrupt and unfair means such as side deals, bribes and/ or kickbacks. In such a situation, while the investment might look profitable, the firm may find the company's value to deteriorate post investment when anti- corruption controls are put in place.

#### Financial Risk

- investing in a company with inflated or misrepresented financials
- risk of losing key revenue generating contracts which were acquired through bribes and kickbacks
- embezzlement/ misallocation of invested funds by the portfolio company
- incurring expenses associated with engaging in a legal battle with regulatory authorities, paying fines and penalties and related litigating costs

#### Operational Risk

- risk of staying invested in a company where the management is indulging in corrupt practices
- failure to make a successful exit or divest due to fraudulent and unethical operations of the portfolio company
- PE firm and its directors inherit the liabilities for any fraudulent activities carried out by the portfolio firm
- risks associated with having limited access to portfolio company's operations

#### Reputational Risk

- the damage to the reputation of a PE firm by being associated with an unethical and corrupt company makes it difficult to attract capital for future investments
- permanent damage to the reputation of not only the PE firms but also to its directors and senior management

# Financial Frauds – Risks and challenges

Further, PE firms are liable under FCPA and UK Bribery Act, if it is found that their portfolio company is in violation of the Acts. Violations attract hefty fines and criminal charges for the corporation and the management.

PE firms are increasingly becoming the targets of law enforcement agencies for potential anti- corruption violations.

PE firms inherit the legal liability even if the corrupt acts were committed by the portfolio company prior to investment.

## Post investment

### **Embezzlement of funds by portfolio company and/ or its promoters**

With limited participation in the day to day activities of the portfolio companies, PE firm faces the risk of having its invested funds being mis-utilized by those in control. Promoters of the company or the management may utilize the funds for purposes not mutually agreed upon. This can include embezzlement of funds by the promoters or investment in non-profitable projects.

### **Fraudulent activities in the portfolio company**

By entering into a contract, the PE firm is vulnerable to every fraud the portfolio company may encounter and faces the risk of having its investment diminish in value post occurrence of fraud. These frauds can be in the form of employee fraud; financial fraud such as inflated

profits, fictitious assets, ghost vendors/clients/ employees; market fraud such as insider trading, securities scam etc. fraud can take on many forms, but whatever the form, the consequence is the same- adverse effect on the viability, growth and reputation of an organisation.

## Disputes and litigations

PE firms looking to exit the company may find themselves embroiled in a legal battle over the completion of accounts, financial and economic value owed to the firm and performance of the portfolio company.

In order to manage the fraud and associated legal risks of your portfolio or prospective investment, begin with accepting the reality that fraud exists. The perceived risk of fraud can easily be managed by adopting a fraud management strategy. The components of your fraud risk due-diligence of a company should entail inquiry against the following key aspects:

### **Management acceptance and commitment –**

- has ‘fraud risk’ been discussed as a business imperative at senior management level;
- has the management established priorities;
- has the management communicated clearly both internally and externally their position on the issue of fraud.

Senior management needs to lead the initiative against fraud, by setting examples.

# Financial Frauds – Risks and challenges

"Good governance is good business, as reflected by the valuation premium earned by well-governed companies and the trust they have earned with customers, suppliers, and regulators. Investors must see eye-to-eye with entrepreneurs on governance and transparency, and post their investment, they must lead by example as directors and shareholders."

**Nitin Nayar**  
Managing Director

**Warburg Pincus India Private Limited**

## Assess your fraud risks –

- identify where are you most vulnerable with your prospective investment;
- determine the likelihood of their occurrence;
- determine the financial and reputational impact of such an occurrence;
- prioritise and classify these risks and determine how to manage and mitigate the identified fraud risks.

## A fraud response plan –

Be prepared to respond to a fraud

- regularly monitor the fraud mitigation/prevention process set up
- put in place processes to be adopted in case a fraud is unearthed;

The key is to evaluate and modify as you move along.

## Fraud prevention is cost effective –

The impact of fraud should not be assessed purely in financial terms; there are intangibles whose value, even in financial terms far outweighs the actual amounts lost due to fraud – what is the value we put on the reputational loss of an organisation hit by fraud; what is the value of the time senior management spends in handling fraud and add to it the loss of morale of the employees of an organisation which has been a victim of fraud.

As fraudsters are always looking for easy targets which provide them the opportunity and an environment where the probability of getting caught is low, all the organisation needs to do is to tighten up these two areas to make things difficult for fraudsters.



# PE Exits - Challenges and opportunities

**Munesh Khanna**  
Senior Partner, Lead Advisory Services  
Grant Thornton - India



Between the years 2006 - 2008 a period of a dynamic growing world economy, 9% + Indian GDP growth, India attracted US\$ 37bn as PE investments into the country. Across sector and industries, the who's who of the PE community and other investment vehicles such as Hedge funds etc invested into India led by the alluring promise of continued growth and a booming stock market. However, the dramatic collapse of the world economy, accentuated by the continued Euro crisis has left the Indian PE investments in a quandary. A significant amount of the investments made in 2006-2008, have now been invested for 4-6 years, and consequently there are exit and redemption pressures on quite a few PE funds operating in India.

In spite of a problematic world economic scenario, in early 2011, the level of exits by PE's operating in India was high. This was enabled by a continued belief and faith that in spite of the global crisis the Indian story remained largely intact. Marquee exits included landmark transactions such as investments in Paras Pharma, Patni Computers, Lilliput, SKS Micro finance, Intelenet and many others. These exits were a combination of IPO's, strategic sales and in some cases sale to other PE firms.

However, a delay in policy making and implementation, a vigorous scrutiny of some of

"The most common type of exit in India is the open market sale. Open market exits accounted for nearly 38 per cent of total PE exit volume over the period January 2005-September 2011. This can be attributed to the fact that once a company is listed on a stock exchange, it is fairly easy for a PE investor to sell off in one shot or dribble its stake, depending on the liquidity in the company's stock. When IPO market shut and it became difficult to exit through listing on the bourses a number of deals opted for an exit through secondaries, PE firms selling to other PE firms. Next in popularity were strategic sales that accounted for 32 per cent of total PE exit volume over the mentioned period."

**JM Trivedi**  
Partner; Head South Asia  
Actis

the key decisions taken by the UPA government, an unfriendly foreign investment climate and a political deadlock, greatly impacted the India growth story. As a result, the GDP growth steadfastly dropped to the 6% level, the rupee weakened by 20% plus and a lack lustre stock market, largely remained range bound. These factors impacted the exit plan of the existing PE players.

With the government now demonstrating policy initiative and implementation, addressing some of the retrograde foreign investments deterrents, the

"Successful exits in India would be driven by quality and profile of the assets. Apart from listing, M&A (inbound) would always remain a very attractive option for the PE portfolio companies."

**Shweta Jalan**  
Director  
Advent International



# PE Exits - Challenges and opportunities

stock market showing signs of revivals, we expect a substantial increase in the level of PE exits. These will be facilitated to a large extent by strategic Merger and Acquisitions and also secondary sales to newer PE firms, who have raised money in recent years or want to now increase exposure to the Indian growth story.

A sustained stock market which is also showing signs of increasing activity will add to the option that existing PE players have for exiting.

Therefore having gone through a tumultuous period of uncertainty, we now expect an increased level of activity and therefore significant new opportunities for existing and new PE Players.

"We strongly believe that exits are a function of the quality of company that the entrepreneur is building and the attractiveness of the sector. We believe that if you build an admirable company with a unique customer facing proposition, exit is a natural event that occurs at the right time. Our experience in the last many years has only reinforced this belief."

**VT Bharadwaj**  
**Managing Director**  
**Sequoia Capital**

"Exits and the returns earned on them, are the true measure of a PE fund's success – with valuations playing a very critical role at the time of exit. Valuations, in turn, are influenced by volatile market sentiments which hold considerable sway, apart from the past performance and future opportunities of the investee company. It therefore follows that, apart from value creation by the PE investor, the timings of entry and exit are also of paramount importance in determining the returns made by PE funds. Typically, PE funds invest with a horizon of 3 – 5 years, going up to 7 years in some cases. Assuming a typical business cycle of five years for an emerging economy like India, the ideal PE cycle would involve entering at the trough of the business cycle and exiting at the peak, leading to extremely good returns. However, such timing may not be achieved in every case, and a company lifecycle may not coincide with the larger macro-economic cycle completely. In such cases, a careful (and realistic) evaluation of various exit modes has to be done by fund managers, depending on extant macro and micro circumstances."

**Darshana Kadakia**  
**Partner – Valuation Services**  
**Grant Thornton - India**



## Valuation

"Periodic fair valuation of portfolio companies by independent valuer's add great value to funds and their investors as it not only provides information on how their investment values are moving but also provides pointers to what's driving the value be it internal factors like company operating and financial performance or external factors like stock market valuations, economic environment. Regular third party valuations also helps in avoiding surprises and potential disputes at the time of exit of the fund."

**David Panna**  
Partner & Practice Leader- Valuation Services  
Grant Thornton - India



## New Companies Bill 2012

"The Companies Bill 2012 brings in several changes aimed at improving governance in companies, both listed and others, together with severe penal provisions for non-compliances, whether intentional or otherwise. The changes impact a wide range of areas, including board functioning, related party transactions, internal controls, fraud, etc.

With the Bill's increased focus on listed companies, and their governance and compliance matters, it's quite likely that a lot of companies may choose to remain private for a longer period and look at other avenues for funds, including PE funds. On the other hand, there are several changes targeted towards directors and the management of the Company, with the more well defined duties for directors, including independent directors. This significantly alters the risk profile of directors on Boards of companies, including nominees of private equity investors.

All of these are likely to bring change to the areas of focus of company managements and also their relationships with key stakeholders, including investors."

**Sai Venkateshwaran,**  
Partner & Practice Leader,  
Financial Reporting Advisory Services  
Grant Thornton - India



# Tax and Regulatory **impacts on PE funds**



**Pallavi Bakhru**  
Partner & Leader, Tax & Regulatory Services  
Walker, Chandiook & Co.

PE has over the past decade, financed opportunities in nearly every business sector in India. As its role has increased in significance, PE's have adapted themselves along the contours of the Indian economy and its unique business culture with reasonable success.

All PE deals tend to lend certain weightage to tax costs and structures even though tax is not the main motive for the transaction. In the recent past, India has unveiled certain tax and regulatory policies that could directly impact PE funds investing in Indian companies and push them to factor these additional considerations and resultant costs into their decision making. There is a widespread belief and not without reason, that PE funds have stalled their investment plans till there is greater clarity on the implications of some of these tax and regulatory changes already imposed or on the anvil.

We provide herein a quick update on certain key tax and regulatory policies directly impacting PE funds:

## **Retrospective taxation of offshore transactions with underlying assets in India**

The tax department initiated tax litigation against Vodafone in 2007 which went up to the Supreme Court for a final verdict in 2012. The dispute was all about incidence of tax in India in a share transfer deal consummated between two non-residents outside India involving India-based assets. The Supreme Court decided in Vodafone's favour and held that there were no specific provisions to tax such transactions and set-aside the tax liability of Vodafone.

The Court advocated legitimacy of participative investments into India and consistency in tax policy.

The Supreme Court's decision was nullified through the amendments vide the Finance Act, 2012 that provided for taxing transactions involving transfer of offshore company's shares between two non-residents where the company's shares derive their value substantially from assets located in India.

Though this amendment did not surprise many, given the Government's past actions of introducing laws to obviate Court rulings, this amendment was criticized more for its retrospective operation dating back to 1961.

As a result of these amendments in the Income Tax Act, 1961 (the IT Act), the tax administrators can now enforce retroactive tax claims on Vodafone-styled deals.

This amendment will impact all exits on the anvil and given its retrospective nature does cast a shadow on exits already made in the recent past which could still be reopened!

In effect, where an overseas PE funds is transacting abroad with a non-resident and their transaction involves indirect transfer of Indian assets, such transacting companies will have to factor in the impact of retrospective enactments in their exit deals.

The Prime Minister of India constituted an Expert Committee under the Chairmanship of Dr. Shome to address the concern raised by various stakeholders in respect of new policy changes.

# Tax and Regulatory **impacts** on PE funds

Expert Committee has been entrusted with the task of examining the applicability of the amendment on taxation of non-resident transfer of assets where the underlying asset is in India, in the context of all non-resident taxpayers. The Expert Committee in its draft report on retrospective amendments relating to indirect transfer has concluded that retrospective application of tax law should occur in exceptional or rarest of rare cases, and with particular objectives such as to correct apparent mistakes/anomalies in the statute, remove technical defects and “protect” the tax base from highly abusive tax planning schemes that have the main purpose of avoiding tax, without economic substance, but not to “expand” the tax base.

The Expert Committee has also dealt with the concern expressed by the PE investors about likely taxation of gains arising to such investors outside India on account of redemption of their investments in the pooling vehicle or inter se transfer amongst such investors. The Expert Committee has recommended that PE investors should fall outside the ambit of taxation of indirect transfer where:

- i. the investment by the non-resident investor in a PE fund is in the form of units which do not result in participation in control and management of the fund;
- i. the investor along with its associates does not have more than 26% share in total capital or voting power of the company;
- iii. the fund or asset holding entity does not have more than 50% assets in India as compared to its global assets;
- iv. the investee company is a listed company on a recognized overseas exchange and its shares are frequently traded; and
- v. the transfer of share or interest in a foreign company or entity results due to reorganization within a group.

The reactions to the recommendations of the Expert Committee are still awaited but our initial understanding is that these recommendations if implemented should at least provide some clarity and relief to the investors looking to ride the India growth story.

## **Introduction of GAAR**

GAAR, as envisaged in the Direct Taxes Code, 2009 and 2010 and subsequently introduced by Finance Act, 2012, drew a lot of criticism for being unduly stringent and draconian. The introduction of GAAR, along with retrospective amendments has created a negative sentiment around the Indian investment climate. The last couple of months post the change of guard at the Finance Ministry, saw positive signals being sent, both by Ministry of Finance and the Prime Minister’s Office.

The constitution of the Expert Committee under the Chairmanship of Dr. Shome, was a part of this change in stance and the report submitted by the Expert Committee would add further impetus to the efforts of the Government.

# Tax and Regulatory **impacts** on PE funds

Continuing with the positivity, the Finance Minister on 14th January 2013 declared, in a press statement, his Ministry's acceptance of major recommendations made by the Expert Committee's report, albeit with certain modifications. The Finance Minister stated that required amendment would be brought into the IT Act to incorporate the Government's acceptance to the legislative changes. The Government has decided to defer the implementation of GAAR to year 2015-2016.

Broadly, recommendations of the Expert Committee, accepted, either completely or with certain modifications, are as follows:

- the scope of an impermissible avoidance arrangement (IAA) will be restricted to include an arrangement whose main purpose is to obtain a tax benefit as against the "one of the main purposes". Thus, an arrangement would be IAA if its main purpose is to obtain a tax benefit.
- opportunity will be given to the taxpayer to prove that the arrangement is not an IAA.
- double taxation in the hands of the same taxpayer in the same year or in different assessment years shall be avoided.
- grandfathering of investments made before 30th August 2010 allowed (i.e. GAAR would not be applicable in case of arrangements with respect to such investments).
- monetary threshold of Rs. 3 crores of tax benefit will be set for GAAR invocation.

- obligation is casted on the tax auditor to report any IAA.
- factors such as duration for which the arrangement has existed, payment of taxes by taxpayer, and provision of an exit route may be considered by the Approving Panel as relevant but not necessarily sufficient considerations for deciding upon the commercial substance.
- inter-play of Specific Anti Avoidance Rules vis-à-vis General Anti Avoidance Rules clarified.
- where a part of the arrangement is IAA, GAAR will be restricted to the tax consequence of that part only.

It appears that some of the recommendations of the Expert Committee have either been ignored or are still under consideration by the Government. Some of these notable recommendations conspicuous by their absence in the Finance Minister's statement are:

- abolition of capital gains tax on listed securities.
- exemption of cases where the relevant tax treaty has a Limitation on Benefits clause (such as in India-Singapore tax treaty) from GAAR.
- specifying an illustrative list of tax mitigation or a negative list for the purposes of invoking GAAR.
- not to resort to GAAR for examining authenticity of the residency of an entity set up in Mauritius.

# Tax and Regulatory **impacts** on PE funds

One most important aspect which has been clarified by the Finance Minister in his recent press statement is applicability of GAAR not only on foreign institutional investor (FIIs) but also its non-resident who are investing in India through such FIIs. GAAR will not apply to FIIs, which choose not to take any benefit under India's tax treaties and non-resident investors using FII route.

The Government, by and large, has accepted a number of recommendations made in the report based on the stake holders' input. Though there are some creases yet to be ironed out, the overall impact of this Ministerial statement is likely to be positive.

The basic intent being to alleviate the rigours of GAAR and mitigate subjectivity in its application, set a tolerance limit for the Revenue authorities and to avoid the indiscriminate application of GAAR. These steps would also bring in consistency in approach and build in adequate safeguards before GAAR is invoked by the Revenue authorities.

The Government's stance on grandfathering investment prior to August 2010 will also mitigate the downside of GAAR implementation for a lot of structures set up before GAAR were even envisioned to stand the test of substance at the time of exit. However, investments after August 2010 still run chances of being tested 'red' at the time of exist. Tax costs if any that were not factored at the time of investment may affect the return on investment.

Funds are structured to pool funds and deploy the same across geographies and have hence always endeavoured to be tax efficient to ensure best returns to their investors. They will need to reassess that motive and revalidate their structures and tax positions and align the same and mitigate risk.

## **Requirement for obtaining Tax Residency Certificate (TRC)**

Another development has been the requirement for any person availing tax treaty benefits to now obtain a TRC from the Government of their home country/territory. Such TRC must contain certain particulars as prescribed by the Government of India. This amendment though emphasises on the importance of TRC, yet it could be difficult to obtain the same in the prescribed format in case the Government of the home country questions the acceptability of such format. Nonetheless, it imposes an additional burden on the person before it can avail tax treaty benefits, however, will go a long way to mitigate certain tax challenges by the tax authorities at a lower level.

PE funds might face a challenge in remitting fees, royalty and such related payments from Investee companies while availing the preferential treatment under the DTAA if they do not have a TRC.

# Tax and Regulatory impacts on PE funds

## Payments to entities located in jurisdictions with whom India does not have a tax treaty or Tax Information Exchange agreements (TIEA)

This is a way for the Revenue to show their displeasure towards using jurisdictions that do not have a treaty or a TIEA with India. It is important for PE funds while setting up structures to ensure that their funds/ IAC are not set up in such jurisdictions.

## Regulatory change - introduction of AIF Regulations

Another important legislation which has a direct impact on the private equity funds operating in India has been the introduction of the SEBI

(Alternative Investment Funds) Regulations, 2012 (hereinafter referred to as (“AIF Regulations”). These regulations were notified on May 21, 2012. AIF regulations seek to regulate all pooled investment vehicles including private equity funds, venture capital funds and hedge funds. SEBI has kept the mutual funds, Collective Investment Schemes (CIS Schemes), family trusts, employee welfare trusts, holding companies, funds managed by asset reconstruction companies, securitization trust or any other trust directly regulated by any other regulator out of the purview of AIF regulations.

## Categories of Funds

SEBI has categorised the funds into 3 specific categories:

Types	Where applicable	Restrictions
Category I	AIF with positive spill over effects on the economy for which incentives or concessions from SEBI, the Government or other regulatory may be considered. Funds that qualify under this category include venture capital funds, small and medium enterprises (SME) funds, social venture funds and infrastructure funds. These funds are required to be close ended funds with minimum tenure of 3 years.	The investment restrictions on Venture Capital Funds is similar to restrictions in the existing SEBI (Venture Capital Funds) Regulations, 1996
Category II	This category intends to cover all funds which do not have either significant positive or negative effects on the economy (i.e. all funds other than Category I & Category III AIF) It includes PE funds, debt funds, fund of funds and such other funds that are not classified as category I or III. These funds too will be close ended.	No investment restrictions
Category III	Funds that employ diverse or complex trading strategies and may undertake leveraging including investment in listed or unlisted derivatives like hedge funds. These funds can be open ended or close ended. The minimum tenure shall be 3 years.	Investment Restrictions apply.

# Tax and Regulatory impacts on PE funds

With these AIF regulations, SEBI has tried to bring in more transparency in the functioning of the fund and has also tried to safeguard the small investors by increasing the minimum investment amount from INR 5 lakhs to INR 1 crore. Further, the minimum corpus of the fund has been revised to INR 20 crores as against earlier INR 5 crores. The fund and the fund manager are now obligated to share the financial information with respect to the fund investment with the investors. Further, the fund also needs to disclose the fees charged by the fund manager or sponsor, any legal inquiries or proceedings against the fund, any change in control of the fund, any breach of a provision of the private placement memorandum. The fund also has to share the valuation procedure and methodology adopted for valuing the assets of the fund. In this respect, Category I & II AIF have to undertake a valuation exercise at least once every six months through an independent valuer.

Further, to ensure that the fund manager manages the investor funds with more responsibility and caution, the regulations provide that the fund manager or sponsor has to contribute a minimum of 2.5% of the initial corpus, or Rs 5 crore, whichever is lower. The contribution is required to be made in cash and cannot be through the waiver of management fees which is charged by the fund manager. Globally, the general contribution by the fund managers or sponsors is approximately 1-2% of the fund size with a management fee of 2% of the fund corpus on an annual basis for running the investment firm.

This is a mixed bag as while it brings a significant class of investors into SEBI's net of regulation to keep investors within the straight and narrow of sound investing principles, it does take away the Funds flexibility to follow different strategies of investment with varying risk appetites.

Another welcome step introduced in the AIF regulations is that the funds can now get their schemes listed any time after the final close of the fund or the scheme. The units of the fund can be traded subject to a minimum tradable lot of INR 1 crore. This would provide flexibility to the investors to exit from the fund without actually waiting for the fund to be wound up.

The regulations also provide for the transitional provisions for the existing funds. The existing SEBI (Venture Capital Funds) Regulations, 1996 are repealed. However, the existing VCF's continue to be regulated under the old regulations till the time the fund or scheme is wound up. As part of the transitional provisions, existing VCFs are not allowed to raise any fresh funds except commitments already made by investors as on May 21, 2012 i.e. the date of the notification of these regulations. The existing funds not registered under VCF Regulations are not allowed to float any new scheme without registration under AIF Regulations. However, existing schemes continue to be governed till maturity as per the terms agreed.

It remains to be seen how the cumulative effect of these changes pan out but given that the India growth story still offers opportunities for investors one would be inclined to believe that these are temporary hiccups.

# Sector Insights – Healthcare & Life sciences

**Mahadevan Narayanamoni**  
**Partner & National Leader,**  
**Healthcare and Life-sciences Advisory**  
**Grant Thornton - India**



## **Is Indian medical devices and equipment sector finally coming of age?**

Transactions in the healthcare and life sciences sector have historically revolved around pharmaceutical companies, multi-specialty hospitals, diagnostics chains and single-specialty hospitals. This year may well be a defining period, in adding medical devices and companies to the growing list of areas within healthcare and life sciences attracting PE or strategic transaction interest.

We have already seen some of the largest PE transactions in the hospitals space this year and are following that up with transactions in the Indian medical devices and equipment sector this year. Fidelity Growth Partners' US\$ 75mn investment in Trivitron Healthcare Pvt Ltd (medical equipment and medical devices company) and CX Partners' US\$ 37mn investment in Sutures India Pvt Ltd (medical devices company focused on the wound closure segment) were the largest PE transactions in the medical equipment and medical devices sectors respectively; and interestingly, both deals involved a sale of shares by exiting PE investors. There have been a couple of other transactions as well in this segment, such as Peepul Capital's investment in Cura Healthcare (a medical imaging equipment company) and IDG and Accel Partners' investment into Forus Healthcare (a med tech company currently focused on ophthalmology instruments).

Investments into Trivitron and Sutures India were reasonably large transactions for a sector that has not seen significant deal activity over the years. This is because there are a limited number of businesses that have been able to achieve reasonable scale in this segment in India, which is dominated by multinational companies. The key driver behind transactions in this segment appears to be the opportunity to build businesses that can compete effectively with multinationals in the domestic market, through a combination of strong distribution capability, relevant products for the local market and cost competitiveness.

## **What lies ahead for this sector, in terms of deal activity?**

While there is significant market opportunity driven by underlying growth in healthcare spend, the sector needs to see a few years of venture capital investment into early stage companies, before being ready for medium to large scale transactions (PE or strategic). We therefore believe maximum deal volume should be in the venture capital space (< US\$ 10mn in deal size), over the next 2-3 years. We also expect to see strategic transactions in this sector, given that one of the major hurdles for growth for medical technology companies is access to technology itself, which can only be provided by a strategic partner.

# Sector Insights - Education

**Prashant Mehra**  
Partner, Transaction Advisory Services and  
Leader, Education sector  
Grant Thornton - India



Regulatory challenges governing the education sector which prohibit investors from making a profit have retarded the free flow of transactions in this space historically. Another challenge faced is finding and retaining the human capital required to run these institutions. Having said that, the funding has been restricted to non-formal education buckets like vocational education and private coaching centres, as these sub-sectors within the larger sector, are unregulated.

However, absence of government funding, parents' readiness to pay for eminent education and the government's position on sector reforms have been driving private investment in this sector. With government inspiring skill and vocational education, this drift is expected to draw even more investments. The sector, not just with its future growth potential in terms of scale but even with the areas of improvement within the current set up such as lack of quality formal education, technology based education, professional K12 management, faculty training and finishing schools offers high inherent growth possibilities. Moreover, since the education sector is less sensitive to economic cycles, the investment opportunity in this sector appears even more lucrative.



# Sector Insights - Education

**Sandeep Aneja**  
Managing Director

**Kaizen Management Advisors Private Limited**



## **General comments on the historical trend of PE investment in the Indian Education sector.**

Over the past several years and especially since the global financial crisis, investors have sought out investment opportunities in sectors that have historically shown resilience to market shaping forces because these opportunities are driven by core consumption by a well-distributed and fast-growing middle class. Education remains at the core of an individual's and a family's spend and has, therefore, attracted growing interest from VC and PE investors in India. Based on Kaizen PE's research, approximately 100 VC/PE transactions, totaling to more than US\$ 600mn have been consummated in India. Between 2008 to 2010, much of the investment activity was in the test preparation, tuition and content-driven companies. The focus appears to have shifted to pre-schools, daycare chains, school management companies, and technology-driven opportunities.

## **General comments on the outlook of PE investment in the Indian Education sector.**

PE investments in education will continue to grow over the next three years as there is a convergence of three market shaping forces:

- shift of new entrepreneurial talent to education
- increasing role of technology in education content creation, education delivery and community collaboration, and;
- increasing clarity on some regulations in the sector.

A significant majority of investments will remain focused around US\$ 5mn to US\$ 7.5mn range. However, there will be increase in the number of companies receiving very early stage funding and also late-stage growth funding as the market matures further.

Business models that promise scalability beyond the typical "brick and mortar" will find favor with investors. Education has historically delivered between 3x to 5x returns to PE investors and this trend is also likely to continue especially as PE investors enhance their focus on harvesting their investments.

## **How have PEs managed the relationship with the Indian promoters? and what are the challenges faced?**

In general, the PE fund-promoter relationship requires a fine balance between managing expectations, maintaining transparency and adhering to agreed upon relationship parameters. By design, it is a time-bound relationship that thrives if there is a sense of true partnership between the two parties. A transactional approach to this partnership-driven relationship may cause discord. In general, PEs and promoters in India have maintained healthy relationships. For PEs the relationship works starts before the investment is made and extends beyond the promoter and it should because of the depth and longevity of this partnership.

# Sector Insights - Education

However, challenges remain and they mostly relate to finding a balance between providing value-add and interference; transparency and completeness of information flow from the company; adherence to agreed upon governance parameters; and, willingness on part of the promoter to bring a strong and qualified professional management team.

**With respect to the Indian Education sector, what are the biggest challenges for PE investors operating in India, e.g.**

**Opportunities, Fund Raising, People etc.?**

For PE investors investing in education, the biggest opportunities lie in segments that are scalable and provide high quality yet low touch service to their customers. The number of opportunities is surprisingly large as Kaizen continues to see several new companies a week. However, the quality of many of these opportunities is, at best, described as emerging. This is a function of the lack of a large number of tested business models in the sector. Therefore, the best returns are to be realised by investing in opportunities that have figured out profitable and scalable business models, which has an implication on the stage at which investors should consider investing. Most of the value creation and value capture is likely to occur at the venture capital and early growth stages. Fund raising remains a challenge for most PE funds raising capital. Global

investors are still the only source of serious institutional capital and many are waiting for returns from previous commitments. Pace of exits has been healthy in the last 12 months and therefore it is likely that new fund raising is likely to speed up after FY 2012-13. Fund raising for niche, sector-focused strategies, requires the ability to climb a higher hurdle. PE is still at a nascent stage in its evolution in India and it is evident from the first set of AIF rules from SEBI. Experienced and carried-interest driven talent is scarce. Over the next few years, there is likely to be a gradual consolidation as talent will seek out funds that have the ability to deliver returns as carried-interest will play a significant role in personal wealth creation.



# Sector Insights - Logistics



**Siddhartha Nigam**  
Partner, Lead Advisory Services  
Grant Thornton - India

Logistics sector is the link between infrastructure and consumption and serves a lifeline of a robust economy. Development of the sector requires a balance of capital, technology and regulatory support. Over the last 5 years, this has been one of the more active sectors for both Private Equity investment and M&A.

In January 2012 the sector witnessed one of the largest PE transactions in 2 years when General Atlantic invested US\$125 million in Mumbai-based Fourcee Infrastructure Equipments Ltd. Other prominent PE transactions include IDFC investment of US\$30 million in Star Agri Warehousing and Collateral Management, KKR and Goldman Sachs investment of US\$55 million in TVS Logistics, New Silk Route investment of US\$35 million in VRL Logistics and an investment of US\$40 million by various investors in Reverse Logistics Company.

There has been increased M&A activity in the sector as well with global players such as Kintetsu acquiring strategic stake in Gati's Express Distribution, Supply Chain and 3PL business, Fairnair Switzerland acquiring stake in Quikjet Cargo Airlines and Deutsche Post DHL acquiring minority stake in DHL Lemuir. Unlike PE investments which have generally been asset heavy in nature, M&A activity has been in asset light models.

Despite such a huge stake and investment, the industry is far from consolidated and companies are struggling to secure handsome returns on their investments.

Challenges such as poor infrastructure, inconsistent tax system, rail haulage rates, wastages in truck transport due to congestion and no tax incentives plague the industry. All these factors have stunted the growth of companies in this sector.

Going forward, the growth in the industry will be driven by moving up the value chain such as 3PL Logistics, multimodal solutions, supply chain solutions and specialist logistics (liquids, cold chain etc.) which is still at a nascent stage in India. The value addition in these segments is also expected to improve margins in comparison to pure play single service providers.

# Insight from an **entrepreneur**

**Phanindra Sama**  
CEO  
[redBus.in](http://redBus.in)



## **What are the advantages of bring in PE /VC investors?**

Besides the money, our investors contributed quite a lot in a variety of situations. They helped us with our business strategy when we were formulating our plan, helped us connect to the right people which helped us build business networks, taught us how to build strong teams and provided emotional support during tough times.

Being a first generation entrepreneur, I needed help in all the above mentioned areas. Our investors played a very vital role in helping us.

## **How has been your experience in raising funds from PE/VC, challenges and opportunities?**

The first round, roughly 5 years ago, was quite easy. We had raised a seed round. Since the amount was not high, and there were investors (early stage investors) whose business model allowed to invest in very early stage ideas (usually with very high risk on all dimensions – business idea risk, market risk, execution risk etc), we could raise it pretty easily.

The second round, just after the collapse of Lehman Brothers, was very tough. Though the business had grown multifold since our first round, we could not attract good valuations as the money in the market had dried up.

The third round, which we raised 18 months back was quite easy as the market was good and we continued growing well.

## **PE /VC Funds are partners in business progress?**

Absolutely! I think entrepreneurs also must look at PEs as partners in business rather than ‘they’ versus ‘us’. We have gained much by partnering with our investors and considering that their opinions also matter as much as our opinions because we are all partners and share holders.

## **What are some of the areas that PE /VC funds should focus with portfolio companies?**

I believe investors should be a strong pillar of support to the entrepreneurs. Once they invest in an entrepreneur they trust, there should be no looking back in the confidence they have on him. In my case, the faith my investors had in me, helped me face adversities with confidence.

# Investor views

The views of the investor are their personal views and may not necessarily reflect the views of the organisation.

# Investor views



**JM Trivedi**  
Partner; Head, South Asia  
Actis

## **What are the key sectors of interest and themes you see providing attractive investment opportunities for PE Funds in India?**

Actis invests in mid-market growth businesses with limited leverage. Our sector based approach helps in sourcing opportunities efficiently. Actis concentrates on four sectors in India: consumer, healthcare, financial services and industrials. We make investments which cater to the needs of the growing Indian consumer class – for example, personal care products, healthcare, retail and auto parts.

We have a strong track record in industrials reflected in our investments in Avtec, Sandhar and recently Endurance; and also in the Consumer space with our current portfolio of Nilgiri's and the exited Paras. In financial services we are very interested in specialised services. This is reflected in our investments of US\$ 40mn in AGS Transact Technologies Ltd (AGS), India's leading ATM outsourcing and payments company. In healthcare our current portfolio of Sterling hospitals gives us expertise in this subsector. This is reflected in our recent investment in Sri Lanka's Asiri Central Hospitals.

Actis works across the emerging markets and we are always aware of opportunities to introduce our Indian portfolio companies to consumers in other parts of the world, for example, markets in Africa and Brazil. We were able to do this with Paras, introducing its products to parts of the Middle East and North Africa. Our expertise in control strategy allows interventions to improve operating performance. Our proactive value creation group

is closely involved from due diligence to exit to identify value levers.

## **How do you view Indian entrepreneurship in recent times. What are some of the challenges in managing the relationship with Indian promoters?**

An emerging trend is a change in the perception of promoters towards fund managers. The perception of promoters for PE investors has evolved from just being a provider of funds to being partners in growth and value creation. Promoters are being selective regarding whom they would like to be associated with. A good fit with the investor has in some cases even superseded the valuation expectation. Promoters have started leveraging their investors for developing and introducing new product/ service offerings, distribution, geographical footprints and entering new markets, targeting new customer segments, brand building, building a professional team, strengthening corporate governance and finally raising follow-on rounds of capital.

Promoters have also understood the functioning of funds and their restriction on investment period and mode of returns therefore they select their investors on the basis of their alignment with the investors exit route.

As India moves from an emerging market towards a developed market, the promoters have begun to understand the need for globalisation through professionalisation. Strategic buyouts are more acceptable and the typical idea of owning and controlling a company is slowly changing for example our exit of Paras to Reckitt Benckiser.

# Investor views

## What are in your view some of the key challenges and opportunities facing the PE Industry in India .

### Delivering PE type return has been a challenge:

India is a growth capital market and in past the PE industry has relied on revenue growth (and the consequent earnings growth) and multiple arbitrage to deliver returns. A recent KPMG report says that EBITDA growth and multiple expansion represented 87% of the value creation for the PE industry in the past. After the financial crisis, the earnings growth has been much lower than what was expected before the financial crisis and the multiple arbitrage ( between entry and exit multiple ) has vanished; in fact in many deals done before the financial crisis the arbitrage is likely to be negative.

### Operational improvement is an opportunity:

Earnings growth: while the revenue growth in the period after the financial crisis may not be as strong as was in the last cycle, we expect the growth to be much higher than the GDP growth rate in the fast-growing sectors PE investors focus on. The question is whether c. 15% revenue growth will deliver PE-style +25% IRR returns? Not by itself. However, there has been a fundamental shift in the industry in favour of operational improvements over the last few years. Low returns compelled GPs to look for an additional source of returns beyond top line growth and multiple arbitrage. A number of GPs now have operational partners in their teams supported by a network of industry advisors. These industry specialists are working with the

management teams of the portfolio companies to expand margins by streamlining operations and optimizing costs. PE in India invests in mid-sized companies, many of which have significant scope for such improvements.

### Excess capital drying up and deal flow improving:

Multiple arbitrage: The excess un-deployed capital (Dry powder) raised in the years preceding the financial crisis has substantially reduced over 2010 and 2011, as more capital has continued to be invested over this period than raised. According to a recent Bain study, dry powder in Indian PE at the beginning of 2012 was about US\$ 17bn, against a backdrop of US\$ 15bn invested in 2011. This is 12 to 18 months supply after taking in to account the US\$ [8-9]bn of new capital being raised every year over the last two years. The demand for capital is on account of new money/growth capital and secondary money or capital required to provide exits to PE investors who had invested in the previous cycle and are now nearing the end of their fund lives.

**Growth capital:** Even a 6 to 7% GDP growth will result in demand for growth capital increasing at a 20% rate every year; in fact, growth capital invested in 2011 was more than triple than was invested in 2009, a y-o-y growth rate of +80% over 2010 and 2011. **Secondary capital:** The US\$ 40bn invested between 2005 and 2008 is ripe for exit and a lot of these deals are already in the market, boosting demand for capital.

# Investor views

Given that IPO market continues to remain unfavourable, PE is likely to be the dominant source of capital. The imminent consumption of excess dry powder and the likelihood of capital markets remaining unviable should dictate receding valuations as demand for capital outstrips supply. In fact, valuations are far more reasonable compared to the last cycle and will perhaps correct further. Multiple arbitrage in this cycle will be neutral if not positive. In summary, this cycle should bring back credibility for the Indian PE industry.

## **What are the key challenges for PE from Regulatory framework and what in your view should be the changes in the Regulatory Framework**

India's growth story is the thesis for investment attractiveness. However for this thesis to play out, clarity is required with respect to the regulatory framework with the role of the government to include favourable policy announcements designed to attract investments into the country.

For India to grow at 8%, the government led initiatives for FDI need to be prompt, as there are limitations to alternative sources of funds because debt market is not very matured in India, equity investment remains a primary option. With the changing investment requirements of companies, the role of the government is to ideally advance from merely a standalone policy maker to a facilitator of these investments. As the economic cyclical downturn corrects and policy makers refine policies in line with global macroeconomic shifts, India's growth story is likely to stay with rebounding investor confidence

A spate of bills, intended to ease restrictions on natural resources and make the tax system more efficient languish on the floor of the parliament. chief among them are the proposed common Goods and Services Tax, the new Land Acquisition Bill, and the restructuring of state power board debt.

There has been recent acknowledgment of the urgent necessity to enact reforms. Key initiatives that have received attention include the unblocking of infrastructure projects and raising the FDI cap in modern retail.

Uncertainty as to how the new GAAR regulation will impact capital gains tax has been a cause for concern. However, the key recommendations of the recently convened Shome Committee, including the deferment of GAAR implementation by three years, and setting out the parameters where GAAR can be applied, are comforting and if the government adopts them soon, it would provide a fillip to PE investing in India by allaying uncertainty around exits.

Some changes that could facilitate more buyouts:

- Reserve Bank of India relaxing restrictions on lending: currently domestic banks are restricted from providing loans for the purchase of shares, the only exception is to promote international ownership when domestic banks lend for purchasing equity in foreign joint ventures

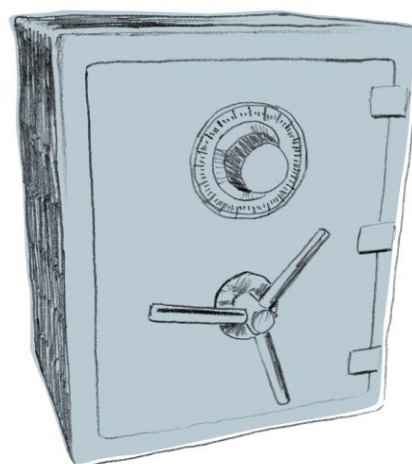
# Investor views

- amending delisting guidelines to allow the PE acquirer to buy-out minority shareholders at an agreed upon price rather than the discovered price (bound to be higher after buy-out announcement) during the Open Offer process, akin to squeezing out provisions in other markets.

## How are you addressing challenges in portfolio company exits ?

The most common type of exit in India is the open market sale. Open market exits accounted for nearly 38 per cent of total PE exit volume over the period January 2005-September 2011. This can be attributed to the fact that once a company is listed on a stock exchange, it is fairly easy for a PE investor to sell off in one shot or dribble its stake, depending on the liquidity in the company's stock. When IPO market shut and it became difficult to exit through listing on the bourses a number of deals opted for an exit through secondaries, PE firms selling to other PE firms. Next in popularity were strategic sales that accounted for 32 per cent of total PE exit volume over the mentioned period.

Interestingly, while open market sales are directly related to sentiments in the capital market, M&A transactions are less impacted by conditions in capital market due to their strategic nature. We have a number of control deals and this exit route is available to us irrespective of market conditions.



# Investor views



**Raja Kumar**  
Founder & CEO  
Ascent Capital Advisors

## **What are the key sectors of interest and themes you see providing attractive investment opportunities for PE Funds in India?**

Given the challenging macro-environment, fund managers have become highly selective in making investments. In general, PE funds have started to focus on sectors which are relatively insulated from the volatile macro environment such as healthcare, education and technology. The focus of our fund continues to be on backing quality businesses with good management teams. We already have investments in sectors such as infrastructure, healthcare and education, and are actively scouting for opportunities in the technology, life sciences and consumer facing businesses. Also, a number of PE firms are looking at taking majority positions in niche businesses that can be eventually sold to larger strategic buyers and surprisingly, promoters have embraced this phenomenon.

## **How do you view Indian entrepreneurship in recent times? What are some of the challenges in managing the relationship with Indian promoters?**

Most of PE investments in India are minority investments in which entrepreneurs own significant majority of their company. Operating as minority shareholders and influencing entrepreneurs to create value is not an easy task.

Majority of Indian entrepreneurs expect PE funds to be passive investors and that has been the case in majority of PE investments until recently.

However, lately PE funds have started to take a more hands-on approach especially in matters of corporate governance, human resources and exit management. Entrepreneurs should focus on forging win-win relationships with their PE partners. Entrepreneurs also have to be reasonable in their valuation expectations and try their best to ensure that investors make returns to ensure the sustainability of PE capital flowing into the country.

## **What are in your view some of the key challenges and opportunities facing the PE Industry in India?**

These are challenging times for the Indian PE industry. During the expansionary phase of India's growth during 2005-2007, excess PE capital was committed to India and the number of fund managers had moved from 30 to 300. Limited Partners were drawn to India's macro-economic growth story. Sadly, PE firms have not been able to deliver the returns that Limited Partners expected from India leading to restraint among investors to commit more capital to India. The investments made during the boom years of 2006/2007 have turned out to be high cost investments and there is a general lack of traction in portfolio companies of most funds over the past 4 years. The lacklustre equity markets have not helped either with exits being deferred indefinitely until the markets improve. Therefore fund raising will be a challenge in the medium term and the industry is ripe for consolidation. However, the silver lining is that there are still plenty of good opportunities to

# Investor views

invest with quality entrepreneurs. Also, the PE industry in India is a lot more mature with a number of fund managers who have been through the entire lifecycle of PE investing, and that bodes well for the future.

## What are the key challenges for PE from Regulatory framework and what in your view should be the changes in the Regulatory Framework?

The industry was expecting a lot of clarity on the regulatory framework with the introduction of AIF regulations. However, these regulations introduced by SEBI are a mixed bag. On the positive side, SEBI has accommodated some of the suggestions of the industry such as ability to make secondary purchases in listed securities, investment in Non Banking Financial Services Companies and grandfathering of existing funds. However, some of the provisions of the regulations impinge on the operational freedom of PE fund managers and their investors.

Globally markets have become more volatile and uncertain, in such a scenario investors would like to have unhindered freedom to change the strategy of the underlying funds. Also, AIF regulations in their current form are only applicable to VCPE funds that pool their capital in India, which represent less than 10% of VCPE capital committed to India, while funds that pool their capital offshore do not come under the gambit of these regulations. This has created a uneven playing field between funds pooling in India as compared to the funds pooling overseas.

By providing clarity on tax treatment, encouraging the pooling of PE capital domestically, ensuring limited partners and fund managers have operational freedom, improving reporting/disclosure norms, and facilitating domestic institutional investor participation, authorities can build a robust PE eco-system in the country.



# Investor views

**Jayanta Banerjee**  
Managing Partner

ASK Pravi Capital Advisors Private Limited



## **What are the key sectors of interest and themes you see providing attractive investment opportunities for PE Funds in India?**

Socio-economic drivers like improving demographics, increasing affluence and urbanization are leading to changing lifestyle, consumption patterns and savings/investment decisions. We see attractive investing opportunities in businesses that benefit from these drivers.

## **How do you view Indian entrepreneurship in recent times. What are some of the challenges in managing the relationship with Indian promoters?**

We are seeing an increasing number of entrepreneurs from Tier 2 and 3 cities aspiring to become regional/national players. We are also seeing an increase in first generation entrepreneur-run businesses. This leads to an increase in the supply of businesses to fund.

Challenges in managing promoter relationships usually stem from lack of clarity in mutual expectations. Open communication from both parties to develop a shared vision for the business and clear expectations based on the value each one can provide would create a strong relationship between the promoter and the fund.

## **What are in your view some of the key challenges and opportunities facing the PE Industry in India**

There are several positive factors that are systematically creating exciting opportunities for the PE industry in India: a growing economy, vibrant entrepreneurial culture,

socio-economic changes and demographic dividend. Recent reform announcements provide further boost to these drivers and should open up even more opportunities for the PE industry to invest.

At the same time there are challenges facing the PE industry like valuation expectations and IPO exit potential. Also, there are many funds with very little differentiation which leads to winning deals based on valuation only, which in turn can lead to subdued returns.

## **What are the key challenges for PE from the regulatory framework and what in your view should be the changes in the regulatory framework?**

Recent SEBI AIF Guidelines provide clear guidelines for the PE industry addressing regulatory issues that were facing the industry.

## **How are you addressing challenges in portfolio company exits?**

One of the main challenges for portfolio company exits is the timing of financial markets, especially when going for an IPO exit. At ASK Pravi, we invest in lower mid-market companies and plan to exit mainly through non-IPO routes (for e.g., stake sale to strategic or financial investor). These alternative exit strategies are discussed and agreed upon with the promoters prior to making the investment.

# Investor views

## How are you addressing challenges of corporate governance in India which is an emerging issue faced by investors?

We follow an “Active Investing” philosophy wherein we establish a partnership with portfolio companies. As an “Active Investor” we take over 25% equity stakes in companies and become a partner as opposed to a mere investor. We seek portfolio companies that are interested in improving corporate governance practices and scale-up the business. We have an operating team with over 200 years of cumulative experience that works together with portfolio companies to partner with them in enhancing corporate governance and adding value to the business.



# Investor views

**S. Harikrishnan**  
Managing Director

Avigo Capital Partners Private Limited



## **What are the key sectors of interest and themes you see providing attractive investment opportunities for PE Funds in India?**

We continue to focus on engineering and niche manufacturing sectors including pharma and specialty chemicals.

## **In your opinion what are some of the key challenges and opportunities facing the PE industry in India?**

Challenges: There are few good quality deals and promoters in the market. Therefore, most of the time, money chases few quality deals and drive valuation upwards.

Opportunities : Emerging of new sectors and professionally managed companies.

## **What are the key challenges for PE from the regulatory framework and what in your view should be the changes in the regulatory framework?**

We need complete clarity on regulation. Any changes in the tax front would affect foreign investors.

# Investor views

**Ashley Menezes**  
Managing Director  
Chryscapital



## **What are the key sectors of interest and themes you see providing attractive investment opportunities for PE Funds in India?**

A number of sectors seem attractive - especially those related to consumer spending including pharma, financial services, consumer durables. Further, some other sectors like IT services and manufacturing where there are niche businesses, could seem attractive.

## **In your view what are some of the key challenges and opportunities facing the PE industry in India?**

The biggest challenge is the need for consolidation amongst PE players. There are many capital providers today and sometimes oversupply causes irrationality in paying too high an entry price that impairs the return on an investment for a long time. Over time, one would expect the industry to consolidate itself.

## **What are the key challenges for PE from the regulatory framework and what in your view should be the changes in the regulatory framework?**

There is a need for a sound, stable and consistent regulation. Knee jerks and reactive changes in regulations, especially retroactive ones, are a cause of concern as funds are raised for a 10 year period and if the rules of the game are changed mid-way, it hampers the investor confidence.

## **How are you addressing challenges in portfolio company exits?**

We need to constantly monitor opportunities and be able to take chips off the table regularly without waiting for the last dollar.

# Investor views

**Arun Gupta**  
**President - Business Development & Investments**  
**Future Ventures India Limited**

## **What are the key sectors of interest and themes you see providing attractive investment opportunities for PE Funds in India?**

Future Ventures is a big believer in India consumption story. We believe in brands. So fashion, footwear, packaged food, personal care, FMCG, edutainment are our focus sectors.

## **How do you view Indian entrepreneurship in recent times? What are some of the challenges in managing the relationship with Indian promoters?**

Indian entrepreneurs in general are very smart. If they recognise the true value of things that the PE is attempting to implement and the depth of knowledge, we have in general seen them receptive whether it is entering new channels, new markets, new categories, improving corporate governance etc.

## **What are in your view some of the key challenges and opportunities facing the PE Industry in India?**

The biggest challenge we think is:

- lack of diversity of knowledge in PE partner
- lack of domain expertise
- lack of ability and willingness to help the promoter build genuine long lasting value

## **How are you addressing challenges in portfolio company exits?**

- a longer hold cycle i.e. 6-12 years
- benchmark each company with the best of breed worldwide and across all operating parameters
- secondary market is picking up now so that is encouraging.

# Investor views



**Abhishek Sharman**  
Principal  
IEP Fund Advisors Private Limited

## **What are the key sectors of interest and themes you see providing attractive investment opportunities for PE Funds in India?**

PE funds in India, depending on their style and expertise, pursue a variety of options for generating returns. We find the space of mid market buy-outs quite compelling, particularly where you have the ability to take control of a platform and help build a consumer brand or a differentiated service in a PE horizon (typically 4-7 years). We see a lot of opportunity in sectors which target consumer spends- healthcare, education, packaged foods/ food services, financial services etc as well as the services sector – in particular logistics and business services. There exist lots of niches in these sectors and you still have the opportunity, given where India is in its life cycle, to build companies which are leaders in certain sub segments.

## **How do you view Indian entrepreneurship in recent times? What are some of the challenges in managing the relationship with Indian promoters?**

Indian entrepreneurship stays intact and in our view is becoming more rational. Entrepreneurs are gradually understanding that 2006 and 2007 were aberrations and they need to be realistic in their expectation of value. Certain entrepreneurs understand the concept of building a business with the right partner who can support them with expertise and capital and are therefore becoming more realistic about the upfront value they can expect for what they have created thus far.

Also, there is gradually a realisation that the life of a business and the professional career of a founder need not be the same and it might be in the best interest of the business to pass on the baton to a PE firm- this has helped us in executing to our control focused strategy. In companies where we have a minority stake, we have been selective in choosing who we partner and have excellent relationships across our portfolio companies.

## **What are in your view some of the key challenges and opportunities facing the PE Industry in India**

Key challenge in my view is the lack of proof of concept that Indian PE has created value for LPs – which is also a function of the vintage during which a large amount of PE investment was made in this country. The other big challenge is the low bar for IPOs in this country which has resulted in a large number of businesses which should have been private actually trading as public stocks. The opportunities are immense- there are great entrepreneurs to back, market opportunity to create leading businesses, the huge demographic dividend which ensures that even on a bad day we are one of the fastest growing economies in the world and structurally high return on capital businesses in many segments of the economy.

# Investor views

## **What are the key challenges for PE from the regulatory framework and what in your view should be the changes in the regulatory framework ?**

The biggest challenge is instability and the lack of a reliable framework which provides investors (and in particular foreign investors) the assurance that their going in hypothesis is not going to be violated during the investment horizon. The enablement ( or the lack of it!) which any regulatory framework provides, is more often than not, a function of the execution – I think we have a robust regulatory framework and we will do well to not change it very often and be pragmatic while executing to it.

## **How are you addressing challenges in portfolio company exits ?**

The Fund has a young portfolio and exits are not an area of concern. We see a lot of interest for businesses the Fund has invested in and believe that there will be buyers for quality companies, one obviously needs to time them well to maximise value for investors.

## **How are you addressing challenges of corporate governance in India which is an emerging issue faced by investors?**

The Fund is an active investor – it takes significant stakes in most of its investments and is able to drive a transformation agenda across various aspects of the business including corporate governance. The idea is to have best in class standards, the guiding principles of which are agreed at the time of the investment and necessary steps are taken within a defined time frame of investment. IEP also reviews corporate governance practices on a regular basis and the aim is to ensure that no compromises are made on this front.

# Investor views

**Samir Kumar**  
Managing Director  
Inventus Capital



## What are the key sectors of interest and themes you see providing attractive investment opportunities for VC and PE funds in India?

Key sectors of interest are technology & tech-enabled companies, which includes software products, services, embedded software, internet and mobile

## How do you view Indian entrepreneurship in recent times? What are some of the challenges in managing the relationship with Indian promoters?

We have seen a big boost in entrepreneurial activity over the past few years – both in quantity of entrepreneurs, and more importantly in their quality. Key challenge would be in the mind-set to create very large corporations, given that there has not been much history of this taking place.

## What are in your view some of the key challenges and opportunities facing the VC and PE Industry in India ?

Uncertain laws / taxation issues (recent issues on GAAR, angel investing, etc.)

## How are you addressing challenges in portfolio company exits?

We are focused on investing in companies that can scale rapidly, and create rapid value – thus paving the way for either M&A or IPO exits.

## How are you addressing challenges of corporate governance in India which is an emerging issue faced by investors?

We do a lot of due diligence on the companies and the entrepreneurs before making any investment. We also do a lot of reference checking before, to make sure there is a high standard of ethics in the company.

# Investor views

**Kumar Shiralagi**  
Managing Director  
Kalaari Capital



## **What are the key sectors of interest and themes you see providing attractive investment opportunities for PE Funds in India?**

Considering we are an early stage fund investing about US\$ 5mn in the first round, we keep away from asset intensive business and look for capital efficiency in the companies we invest in. Generally we seek companies that have technology as an enabler in their business model. This could be across various sectors such as IT, software products, telecom, E-commerce, internet, healthcare, education and clean technologies. We continue to see attractive opportunities in all these sectors although at any given time, market vagaries could significantly affect sector sentiment.

## **How do you view Indian entrepreneurship in recent times? What are some of the challenges in managing the relationship with Indian promoters?**

Over the last decade, in the early stage investment category, entrepreneurial ecosystem continues to grow strongly. The quality of entrepreneurs, their readiness and aggressiveness and the support system to help them all continue to mature at a good pace. We have seen significant increase in both the quality and quantity of business plans seeking capital. There are a good number of successes even in India that entrepreneurs can model their businesses after.

On the challenges issue, foremost, it is extremely important for the promoters and the investor to build a strong relationship in which there is mutual trust. That enables one to overcome many of the challenges that they come across time and

again. The challenges can be quite different in each case but ability to communicate, rationally discuss issues and solve them is paramount for company's growth.

In most cases challenges affect the company, consequently both the promoter and the investor and hence necessarily addressed together. That is what teams should spend most time on. Harder ones are - when to raise capital, how much to dilute, when and how to exit etc. where there may be diverging views and solutions need to take into account the needs of both parties but more time spent on this is time away from business.

## **What are in your view some of the key challenges and opportunities facing the PE Industry in India**

At a company level, issues faced by investors are no different than what investors deal with around the world. Helping companies build teams, companies winning first customers, managing delays and cash flow while developing and selling solutions etc. India's attractiveness and hence opportunity is the large and growing market that is hungry for various products and solutions and in addition a large educated workforce.

Challenges primarily are two, and even those are interrelated. First is the lack of clarity and support from government and regulatory bodies and entrenched corrupt practices which take a heavy toll on productivity and hence company performance. Second, is the prevailing attitude of poor and at times unethical practices which pervade the entire organisation and even the corporate world forcing even small companies to think of non-straightforward ways to "get things

# Investor views

done”. These issues indirectly affect all investors and their ability to make great return despite fantastic opportunity. Further, these do not bode well for the company or for the country which is why India, unfortunately ranks very poorly on the corruption and business friendly environment indices. PEs while interacting with companies come across challenges as a result of this and it also affect PEs ability to raise capital for investment in India.

## **What are the key challenges for PE from regulatory framework and what in your view should be the changes in the regulatory framework?**

There are (too) many frameworks and laws in the country but clarity, enforceability and timely resolution are missing. Lack of a strong will to address those affects PE and for that matter all aspects of doing business in India.

## **How are you addressing challenges in portfolio company exits?**

For early stage funds, many of who started post 2005 the next 2-3 years are crucial in terms of exits to demonstrate fund performance. Unless investors are able to prove that returns in India are what were promised, no matter what the opportunity or challenges, interest in India will fade. Firstly the market buoyancy has to support exits especially when it comes to IPOs and trade sales. Secondly the company performance and the promoters efforts to realise liquidity is important to ensure exits for the investors. Since the ability and nature of exit can be significantly different for each company, we explore early on, how to position each company and work toward a plan. In the end, full credit should go to the promoter and the team for facilitating the investor exit which is the promise and hope on which the entire relationship would have started.

# Investor views

**Rakesh Sony**  
Director  
Motilal Oswal PE



## What are the key sectors of interest and themes you see providing attractive investment opportunities for PE funds in India?

- sectors linked to domestic consumption themes like food, Pharma, Healthcare, Education
- NBFCs in the niche segments like vehicle, education and housing finance.
- services like cash management, logistics and infra/construction ancillary services

## How do you view Indian entrepreneurship in recent times? What are some of the challenges in managing the relationship with Indian promoters?

The Indian entrepreneur has come under significant pressure of late. Largely due to the general slowdown which has impacted the demand of key product segments. The projects have also got delayed due to lack of approvals from the government authorities and non availability of key resources at various points.

The relationship with the Indian promoters have been a roller coaster ride. The relationship is great till the time both parties are on the same page. The things starts to become sour once you object or has a difference of opinion.

## What are in your view some of the key challenges and opportunities facing the PE Industry in India?

The biggest challenge is the exit. The businesses have not performed the way they were projected to perform and left a lot to be desired.

The slowdown, inflation and govt inaction has led to the dynamics of business going topsy-turvy. The investors are looking more control owing to non performance and promoters are not willing to accept the reality of life.

## What are the key challenges for PE from regulatory framework and what in your view should be the changes in the regulatory framework?

The biggest challenge is the ever changing foreign exchange policy of RBI. There is a lot of investment made by foreign funds which is in the range of non clarity from regulator.

This has led to slow down in the investment flows in a big way.

## How are you addressing challenges in portfolio company exits?

We are continuously working on them. Trying to built competencies and see how we can be different from the market. There is always a suitable buyer for an asset which is well managed.

## How are you addressing challenges of corporate governance in India which is an emerging issue faced by investors?

There is a lot of experienced talent available in the country who is willing to lend an helping hand to companies by sharing their experience and also building best practices for companies.

We are trying to built a strong boards for our companies with independent directors who actively participate to improve the corporate governance practice.

# Investor views

**Prakash Nene**  
Managing Director

**Multiples Alternate Asset Management Private Limited**



## **What are the key sectors of interest and themes you see providing attractive investment opportunities for PE Funds in India?**

I believe that maximum opportunities are linked to domestic consumption led growth stories in a variety of sectors including healthcare and financial services.

## **How do you view Indian entrepreneurship in recent times? What are some of the challenges in managing the relationship with Indian promoters?**

A large number of Indian communities and entrepreneurs are in early growth phase given the fact that India entered into high growth momentum only during the last decade.

Challenges involved include changing the mindset of the entrepreneurs which makes them believe that employee incentives, business transparency and high governance would be value accretive.

## **What are the key challenges for PE from regulatory framework and what in your view should be the changes in the regulatory framework?**

PE has an opportunity to transform the Indian industry by bringing in their deep insights. Challenges are linked to regulatory issues. Investor friendly tax and regulatory regime is a prerequisite for sustained PE interest in India.

Currently there is a disincentive for the Indian fund managers to operate on shore. We need to have a tax and regulatory framework which

encourages local talent operating within the country.

## **How are you addressing challenges in portfolio company exits?**

Over a period of time it is increasingly difficult to go for IPO in Portfolio companies since the minimum size for a successful IPO is going up. However given the fact that a large number of PE Investors are coming into the country,

Peer to PF exit is a new possibility seriously being considered by funds.

## **How are you addressing challenges of corporate governance in India which is an emerging issue faced by investors?**

These challenges are being addressed by encouraging entrepreneurs to opt for persons of repute as independent directors on their boards. Secondly as a PE Investor, we have a vast network of advisors in different fields whom we encourage to work with our portfolio company on governance issues.

## **Any other comments that you may like to provide?**

Management By Objectives as a concept hasn't still caught on in a big way in India. The industry should give special focus and encourage professionals to become entrepreneurs and create wealth for all stake holders.

# Investor views

**Ramesh Venkat**  
Chief Executive Officer & Managing Director  
Reliance Equity Advisors



## What are the key sectors of interest and themes you see providing attractive investment opportunities for PE Funds in India?

Consumer demand, infrastructure related and skilled services

## How do you view Indian entrepreneurship in recent times? What are some of the challenges in managing the relationship with Indian promoters?

Indian entrepreneurship is partly opportunistic, partly defensive, selective on governance. Challenges are principally around alignment of expectations, and timelines for outcomes.

## What are in your view some of the key challenges and opportunities facing the PE Industry in India?

Recognition of PE as an intermediate, pre capital markets, growth strategy is still limited. Scalability of companies is a challenge in exits.

## What are the key challenges for PE from regulatory framework and what in your view should be the changes in the regulatory framework ?

Clarity and stability of the taxation regime - pass through aspects, and applicability of DTAA.

## How are you addressing challenges of corporate governance in India which is an emerging issue faced by investors?

Careful selection of promoters/managements to ensure reasonable alignment on governance standards, agreements prior to investment on key corporate governance issues and veto and consent rights.

# Investor views

**VT Bharadwaj**  
Managing Director  
Sequoia Capital



## **What are the key sectors of interest and themes you see providing attractive investment opportunities for PE Funds in India?**

We continue to look for interesting opportunities in consumer, healthcare and technology sectors, like we have in the past we are seeing many interesting and attractive opportunities in the space.

## **How do you view Indian entrepreneurship in recent times? What are some of the challenges in managing the relationship with Indian promoters?**

We continue to view Indian entrepreneurs – with the same lens that we have in the past which is as business partners. We have had the benefit of partnering with some of the most exciting entrepreneurs in India, and are thrilled about it.

## **What are in your view some of the key challenges and opportunities facing the PE Industry in India ?**

We see ourselves as our entrepreneurs' partners. The challenges and the opportunity that we faces is no different from what the Indian entrepreneur is facing today – how to make sure that you grow fast through a compelling value proposition in a competitive market, how do you manage growth, and how do you ensure that the dash for growth is profitable and if relevant how do you finance the growth.

## **How are you addressing challenges in portfolio company exits?**

We strongly believe that exits are a function of the quality of company that the entrepreneur is building and the attractiveness of the sector. We believe that if you build an admirable company with a unique customer facing proposition, exit is a natural event that occurs at the right time. Our experience in the last many years has only reinforced this belief.

# Investor views

**Nitin Nayar**  
Managing Director

Warburg Pincus India Private Limited



## What are the key sectors of interest and themes you see providing attractive investment opportunities for PE Funds in India?

Warburg Pincus has invested in eight companies over the past two years. These investments illustrate the sectors and themes that Warburg Pincus finds interesting. For example, domestic consumption stories are attractive, as evidenced by the firm's recent investments in financial services (AU Financiers, Future Capital), health care (Metropolis) and the internet (Quikr).

Differentiated stories in infrastructure also are appealing. Examples there include the firm's investments in power (DB Power) and logistics (Continental Warehousing, IMC). And, of course, there are still themes within export-oriented industries worth considering, as is the case with the firm's investment in QuEST Global, a Singapore-based company whose Indian arm provides high-end R&D and engineering services.

## How do you view Indian entrepreneurship in recent times? What are some of the challenges in managing the relationship with Indian promoters?

Choosing the right entrepreneur with whom to work is critical to the success of any deal. It is probably more so than in mature markets given the relative dearth of control transactions. High integrity and track record are necessary and there also needs to be agreement amongst the partners on the future direction for the company. Further, incentives need to be aligned to ensure the fruits of value creation are shared equitably across all partners. For example, Warburg Pincus typically takes a long-term view of the relationship with an

entrepreneur, investing in equity securities alongside the promoter, not taking deal fees, not viewing an IPO as strictly a liquidity event, etc.

## What are in your view some of the key challenges and opportunities facing the PE Industry in India?

It is no secret that the PE market in India is very competitive; however, this is equally true in markets such as the US and Europe. Macro-economic slowdowns, market volatility and regulatory uncertainty are also not unique to India. Nonetheless, the structural tailwinds, especially relating to domestic consumption and demographics, are powerful long-term trends, and should continue to create opportunities. Further, new sectors will inevitably emerge, either through regulatory discontinuity (e.g., modern retail), or technological discontinuity (e.g., internet).

## What are the key challenges for PE from regulatory framework and what in your view should be the changes in the regulatory framework?

PE firms value clarity, stability, and consistency in any regulatory framework. Given the positioning of PE firms as long-term equity investors, any medium-term shifts in the regulatory environment could impact existing investments and deter some firms from undertaking new investments. Ultimately, PE firms are looking for an economic environment that will promote growth for all stakeholders.

# Investor views

## How are you addressing challenges in portfolio company exits?

Warburg Pincus has invested over US\$ 3bn in India over the past 15 years. Key exits for the firm include Bharti, Kotak Mahindra Bank, HDFC, Gujarat Ambuja, Nicholas Piramal, Max India, and Sintex. This track record has enabled the firm to build credibility amongst its limited partners as successful India investors. In addition, Warburg Pincus globally has a history of 45 years of PE investing across 13 PE funds. Due to these reasons, the firm faces considerably less pressure to exit relative to either first time India investors or first time funds. This enables Warburg Pincus considerable flexibility with respect to timing of exits. The firm's strategy to be patient, long-term investors allows it to hold investments up to 10 years if required.

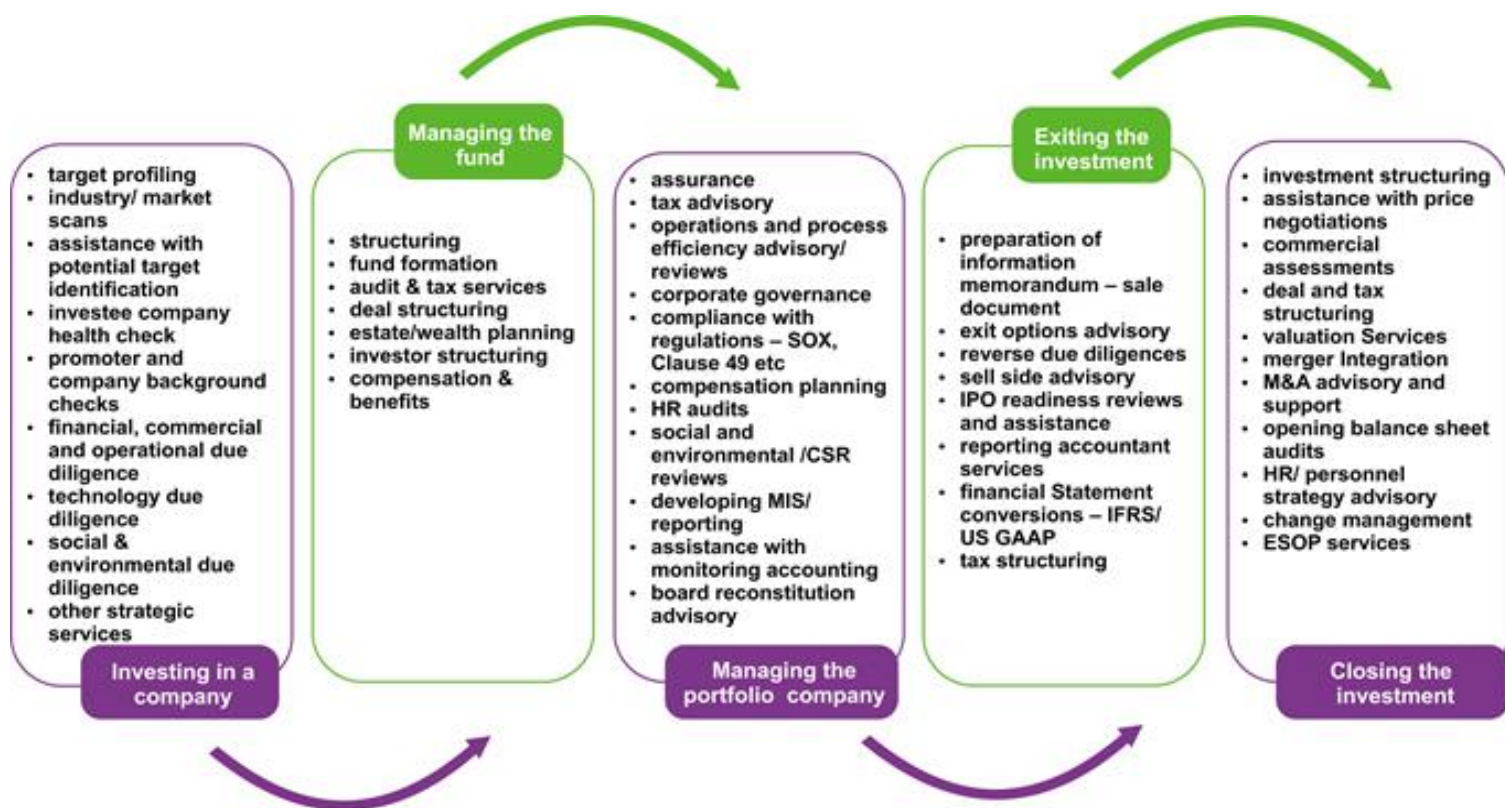
As long as the underlying businesses are well positioned, profitable exits will naturally present themselves.

## How are you addressing challenges of corporate governance in India which is an emerging issue faced by investors?

Good governance is good business, as reflected by the valuation premium earned by well-governed companies and the trust they have earned with customers, suppliers, and regulators. Investors must see eye-to-eye with entrepreneurs on governance and transparency, and post their investment, they must lead by example as directors and shareholders.

# Grant Thornton Private Equity advisory services

Technical excellence and distinctive client service



## About Grant Thornton India LLP

Grant Thornton India LLP is a member firm within Grant Thornton International Ltd, one of the six largest global accountancy organizations, and the global leader in serving the needs of dynamic privately held businesses. From its origins in 1935, the firm has today grown to be one of the largest accounting and advisory firms in India with over 1,200 professional staff based out of 10 locations in the country.

The firm's mission is to be the advisers of choice to dynamic Indian businesses who have global ambitions- raise global capital, expand into global markets or adopt global standards. The firm specialises in providing compliance and advisory services to growth oriented, entrepreneurial companies and adopts best in class international tools, methodologies and risk management standards for all its services

Grant Thornton India LLP has a vast experience of over 1000 due diligences and 1200 valuations and 50 completed transactions in the past decade and has provided assurance, business risk, valuation, consulting and business transformation services to PE Funds, their investee companies and other clients.

From identifying the right strategic fit to structuring and closing the deal, we can support you in all aspects of your transaction to maximise value. Select transactions that Grant Thornton India has advised are set out below.

 <p>acquired</p>  <p>USD 750 mn</p> <p>Financial Due Diligence advisor</p>	 <p>acquired</p>  <p>USD 230 mn</p> <p>Financial Due Diligence advisor</p>	 <p>acquired</p>  <p>USD 150 mn</p> <p>Financial Due Diligence advisor</p>	  <p>acquired</p>  <p>USD 105 mn</p> <p>Financial Due Diligence advisor</p>
 <p>acquired</p>  <p>USD 75mn</p> <p>Financial and Tax Due Diligence advisor</p>	 <p>Valuation for merger of Siemens VAI Metals Technologies with Siemens Ltd</p>	 <p>Valuation of the branded nutrition business of Wockhardt for a transaction</p>	 <p>private equity</p> <p>US\$ 37million</p> <p>Sole Financial Advisors</p>
 <p>Consumer Products Ltd.</p> <p>Valuation of group companies for merger</p>	 <p>Valuation for demerger of regional channels business into Zee Entertainment Enterprises Ltd.</p>	 <p>acquired</p>  <p>USD 310mn</p> <p>Sole Financial Advisor</p>	 <p>invested in</p>  <p>USD 38mn</p> <p>Sole Financial Advisor</p>
 <p>acquired</p>  <p>USD 22 mn</p> <p>Sole Financial Advisor</p>	  <p>invested in</p>  <p>USD 43mn</p> <p>Sole Financial Advisor</p>	 <p>acquired</p>  <p>USD 33mn</p> <p>Sole Financial Advisor</p>	 <p>acquired stake in</p>  <p>US\$ 598 million</p> <p>Due Diligence advisors</p>

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