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Private Investments in Public Equity (PIPE) – Opportunities and Challenges in India

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Abstract

Research on Indian private equity is only beginning to emerge, with most of it focused on development, case studies, and the life cycle of private equity returns A remarkable growth has been observed in the private equity (PE) market in India in the last decade. The two reasons for the growth of Private Investments in Public Equity (PIPE) in India, First, change in organizational innovation, aided by regulatory and tax framework. Second, adoption of limited partnership and general partnership. PIPE have become a vital source of funds for start-up firm, private middle-market firms, firm in financial distress and public firms seeking buyout financing. Given the escalating interest of investors in Indian equity market, the paper is based on the impression that PIPE transactions are set to become its next big instrument of investments. Accordingly, this paper synthesizes the information on PIPE market in India by deliberating on numerous aspects of PIPE and its features. The objective was to identify various opportunities for investments by analyzing the past trend of investments made by the major PE investors during the last few years. The paper also examines the challenge faced by investors in India while executing these types of transactions. Some of the sectors which were examined were of IT & ITES, healthcare, e-commerce, etc. The analysis found certain sectors to attract more PIPE investments in future whereas other factors were identified to be stifling the PIPE deals in India, presently. Finally, given the exploratory nature of the paper, further research can be carried out that corroborates the findings of this paper by engaging in the confirmatory studies.

Keywords

Private Equity (PE), Private Investment in Public Equity (PIPEs), Financial Crisis, Venture Capital Firms, India.

Introduction

Private Investment in Public Equity (PIPE)

A private investment in public equity, often called a PIPE deal, involves the selling of publicly traded common shares or some form of preferred stock or convertible security to private investors. It is an allocation of shares in a public company not through a public offering in a stock exchange. PIPE deals are part of the primary market. In the U.S., a PIPE offering may be registered with the Securities and Exchange Commission on a registration statement or may be completed as an unregistered private placement.

PIPE is a mode of finance, which to some extent can ease the liquidity crunch in the industry. The transaction involves allowing of private investment from investment firms, mutual funds and other qualified investors, usually at a discount to the current market value providing capital to the company. The investments may be in shares, stock or convertible security of the listed company. Once the deal is made, and the securities are issued, steps are initiated for listing the securities to the advantage of the investor.

A PIPE deal saves a company from the complexity of selling shares through a fresh public issue. Instead, the company finds an investor and sells him a block of newly issued shares at an agreed price or a block of debt which can later be converted into shares (a structured PIPE). The transactions involve private investments made by investment firms, mutual funds, and other qualified investors. It is sold by the company at a discount rate in the current market value. The investments may be in shares, stock or convertible security of the listed company.

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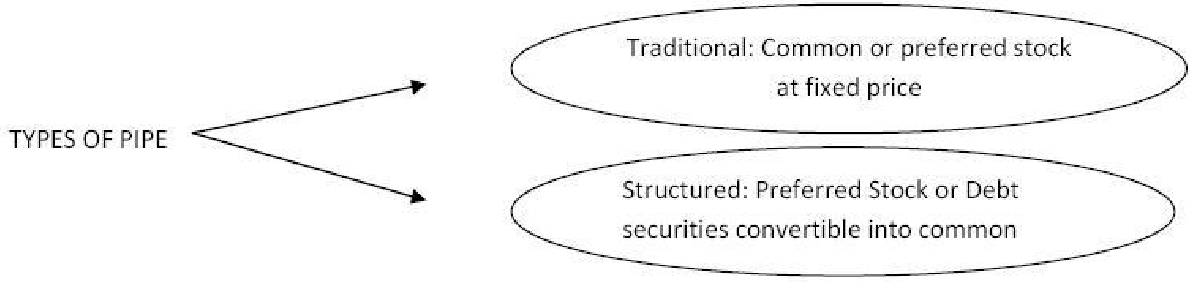
Types of PIPE



They are medium to long term investments with average holding period exceeding three years. Preference is for convertibles and to lesser degree convertible bonds followed by warrants and registered direct equity. In PIPE deals, the primary objective is capital as it has potential to give instant returns

Benefits of a PIPE deal

A PIPE deal allows a company to avoid the complexity of selling shares through a fresh public issue. Instead, the company sells newly issued shares at an agreed price or debt which can be converted later on into shares to an investor. The PIPE process is simple, fast, and inexpensive. Due to the difficulty of exits, private equity firms have progressively begun to invest in listed companies for better returns.

Some of the advantages of a PIPE deal are as follows:

- There is no fear of under subscription as it is fixed beforehand between the investor and investee.
- A PIPE fund raising process is much faster than a fresh public issue of shares which involves a lot of compliance formalities and is an arduous process.
- The due diligence is quick because target company is in public domain, therefore time and cost are saved for the investor
- Since it is a private placement, the information of raising capital can be kept confidential;
- There is less equity dilution since the issue is made to private investors

Drawbacks of PIPE deals

- Control- Unlike private equity investments, PIPE investors will not have a seat on the board or have a say in the business strategy of the company.
- Liquidity- In most instances, PIPE investments offer short-term liquidity through the resale registration process but in some sponsored PIPE deals the investors are restricted from selling for a specified period.
- Transaction Fee -Sometimes transaction fees are paid to the investor from the proceeds of the financing which may be around 1% of the gross proceeds.

The concept of Private Investments in Public Equityin India is very recent, compared to U.S.A, U.K, Europe and Israel etc, where it has been in existence, since many decades and over the period has helped many businesses to grow and expand. One of the main reasons for this is the regulatory and legal framework in India was not conducive for the development of venture capital industry. There are significant differences between the legal landscape applicable to PIPEs in India and that applicable to PIPEs in the U.S. and Europe, however, and this can make an investment in India seem daunting to many foreign investors. Consequently, it is important for investors to develop a good understanding of, and seek guidance about, these differences at the outset of a potential transaction.

Structuring Pipes Investments

Private equity investors in India have traditionally made their PIPEs investments by acquiring shares of a listed company, either from one of the promoters, in a preferential issuance and/or through open market purchases. However, as more global private equity firms enter the Indian market and bring with them deal structures developed in the U.S. and other markets, there has been a small but increasing trend towards private equity firms structuring Indian PIPEs deals to include securities other than just common equity, such as convertible preference shares and warrants.

Convertible Preference Shares

PIPEs transactions in the U.S. typically are structured as a purchase by the private equity investor of newly-issued preference shares (or, in U.S. terminology, shares of preferred stock) that are convertible into equity shares. This structure provides the investor with some measure of downside protection, because the preference shares are senior in the capital structure to the common shares, but the investor also has the full upside potential of an investment in the listed company's equity shares.

There have been some recent PIPEs deals in India that were structured as investments in newly-issued convertible preference shares of the listed company. There are two key differences between these convertible preference shares and U.S. preferred stock. The first key difference is that convertible preference shares in an Indian listed company must be converted into equity shares within 18 months of issuance or they become regular non-convertible preference shares, whereas in U.S. practice the preferred stock issued in a PIPEs deal will remain outstanding and convertible for much longer periods. What this means, in essence, is that the private equity investor has 18 months to evaluate its investment in an Indian listed company and decide either to:

* convert its convertible preference shares into equity shares if the listed company is performing well, thereby capturing the upside potential but foregoing any downside protection; or

* remain as preference shares if the listed company is not performing well, thereby maintaining its downside protection but foregoing the upside potential.

The second key difference is that Indian convertible preference shares, and preference shares generally, do not carry any voting rights other than in very limited circumstances.

Convertible preference shares can carry a dividend, though there are limitations on the amount payable. Under current regulations, the maximum coupon rate payable to foreign investors holding convertible preference shares is 300 basis points above the prime lending rate of the State Bank of India (which today works out to about 13% per annum).

Convertible preference shares in an Indian listed company can also provide a number of other standard protections, like anti-dilution provisions, that are familiar to U.S. private equity investors. The mechanics for these protections can be quite complicated, however, because of various Indian company law limitations, so investors should consult with Indian legal advisors to understand the limits on such protections.

Review of Relevant Literature

Much of the empirical estimation of private investment in developing countries follow an adapted version of the Jorgensen-Hall (1967) neo-classical investment model instead of Tobin’s Q model- for which data is not readily available in most developing countries. Tobin’s Q- the ratio between a physical asset’s market value and it replacement value is hard to measure in most developing countries.

One of the few studies in a developing country using Tobin’s Q is by Solimano (1992) for Chile, which uses a 3-equation model for Investment, Q and Output. In their model Q has a positive effect on investment but an insignificant effect on aggregate demand. Q is strongly affected by the output gap, negatively by the real exchange rate and the real interest rate.

Most empirical studies of investment adapt the Jorgensen-Hall model to developing country conditions. Three adjustments are important. The first is the important role played by government expenditure and investment policy when markets are underdeveloped. High public sector deficits which are financed by public borrowing crowd out the availability of credit to the private sector. Ogura and Yohe (1977) show that public spending can be divided into three categories (a) those that compete with the private sector (b) those that provide services independent of the private sector (pure public goods) and (c) those that are complementary to the private sector.

One of the earliest studies to study the effect of public investment on private investment is by Blejer and Khan (1984). They find that infrastructure investment3 has a positive effect on private investment, but non-infrastructure investment crowds-out private investment. More direct positive effects of public infrastructure investment on private investment were found by Chhibber and Wijnbergen (1992) for Turkey and Shafik (1992) for Egypt. Asante (2000) also finds a positive effect of public investment on private investment and recommend more infrastructure investment.

Wai and Wong (1982) use a modified version of the flexible accelerator theory of investment and apply it to five countries: Malaysia, Greece, Thailand, Mexico and Korea. They find that government investment is the most important explanatory variable in Greece, Korea and Malaysia, bank credit in Thailand, and capital inflow is most important in Mexico. In their model they are able to estimate the net effect of government investment on private investment, that is, the contributory effect less the financial crowding out effect, is positive in Greece, Korea and Thailand. But confirm the existence of financial crowding out effect of government investment for Mexico and Malaysia.

In many developing countries credit is constrained and interest rates are not freely determined. This means that capital is allocated and interest rates do not clear that market, leading to financial repression. Following Mckinnon (1973) and Shaw (1973) there is by now a large body of literature Bruno (1979), Gelb (1989) that have analyzed the implications of financial repression, theoretically and empirically.

In many recent studies of private investment in developing countries the real interest rate does not have a significant effect on investment but the availability of credit to the private sector does. In Egypt (Shafik 1992), Turkey (Chhibber and Wijnbergen 1992), Colombia (Schmidt-Hebbel and Müller 1992) and Morocco (Dailami 1992) credit rationing has a significant effect on investment.

The empirical literature also shows a strong impact of the real exchange rate on investment behavior. Solimano (1992) shows that in Chile the short run effect of the devaluation was negative on investment, but over time, as the economy expanded, its impact on investment was positive. Chhibber and Shafik (1992) show the same effects in Indonesia as a slower devaluation raises interest rates and slows investment. Exchange rate instability also has a negative effect on private investment. Servén (2002) shows the negative effect of exchange rate uncertainty on private investment for 61 developing countries for the period 1970-1995.

For India, there are a host of empirical studies of which we summarize those that have relevance for our study.

Bhanumurthy, Bose and Adhikari (2014) attempt to construct a macroeconomic framework for India to review the macro-fiscal linkages over the 14th Finance Commission period of 2015-19. They estimate private investment functions for four sectors of the economy - Agriculture, Industry, Services and Infrastructure - as a part of a macroeconomic model for the period 1991-91 to 2012-13. The equations are specified mainly as function of public investment of that sector, along with interest rate and/or capacity utilization for some sectors. Results show that public investment crowds in private investment and interest rates negatively affect private investment. Private investment as a fraction of nominal output is positively related to capacity utilization in Industry.

Ang (2009) examines the role of financial sector policies in determining private investment in India (1950-2005) and Malaysia (1959-2005). The private investment equation is a function of GDP, public investment, user cost of capital, interest rate restraint, directed credit programs, reserve and liquidity requirements. The results suggest that, in short, some sort of financial restraint may stimulate private investment. However, directed credit programs and high reserve & liquidity requirements tend to have an undesirable effect on private investment in India.

Mitra (2006) provides empirical evidence for India (1969-2005) that in the short run government investment crowds out private investment, whereas over medium to long term government investment complements private investment.Bahal, Raissi and Tulin (2015), on the other hand, found public investment “crowding out” private investment in India over the period 1950-2012. But found support for crowding in of private investment over 1980-2012, attributing it to the policy reforms which started during early 1980s and gained momentum after the 1991 crisis.

Recent empirical literature has worked on understanding the role of profitability as a key determinant of capitalist investment behavior in developing countries. Basu and Das (2015) empirically analyze the contemporaneous and long run impacts of rate of profit and its components profit share, capacity utilization rate, and capacity-capital ratio – on investment for 19 major Indian states. Using three investment functions based on Keynes (1936) and Robinson (1962), Bhaduri and Marglin (1990), and Foley and Michl (1999), their results show that rate of profit has both short and long run positive impacts on investment, while profit share and capacity – capital ratio have only long run positive impacts, and the capacity utilization rate has only a contemporaneous

Private Investments in Public Equity (PIPE) in India

Why PE Investments in India?

Indian economy is one of the fastest growing economies of the world. The strong fundamentals of India such as average GDP growth of 8.5% for last five years, increasing saving and investment rate, its stable democratic government, well educated population, abundance of English language speakers have caught the attention of the PE players and have brought it on the priority list of all PE funds. On the one hand, Indian growth story has lured the Private equity investors and on the other the Indian economy has gained significantly from the PE Sector. PE firms have shared their global exposure and has had its spillover effect on various fronts such as as- corporate governance standards, knitting global connectivity, building executive teams, improving/raising organizational capability, enhancing evaluations and creating liquidity. Further, PE firms also provide the domestic entities the necessary mentoring and advice without having to go to public markets.

Private equity as an asset class has grown substantially in India in the past two decades. The Indian private equity industry has been transformed from state-sponsored venture capital funds to include more private and foreign private equity players. The main research consists of studies that examine the evolution and the current status of the industry (Pandey [1996, 1998]; Verma [1997]; Dossani and Kenney [2002]; Singh et al. [2005]); multi-country studies that include India (Lockett et al. [1992], Subhash [2006], Ippolito [2007]); survey studies of VCPE industry practices in India (Mitra [1997], Kumar [2002, 2005], Kumar and Mohinder [2003], Mishra [2004]); and studies that can be considered case studies of VCPE investments (Kulkarni and Prusty [2007]). Post2007, efforts have been made to study the life cycle of private equity in India (Rajan [2010, 2011]), but no attempts have been made to study the returns generated by private equity funds on exited investments. This article is an attempt to meet this gap in the research on private equity returns.

A PIPE transaction in India has to comply with the conditions stipulated under SEBI guidelines for preferential issues. Further, the SEBI Insider Trading Regulations has restricted share trading by the investor or his advisor if they have clandestinely utilized any unpublished price sensitive information during the PIPE transactions.

Domestic Indian PE funds are increasing in number, size and sophistication. Capitalising on their extensive networks of connections in industry, banking and government, they are absorbing the investment and portfolio management skills of their global counterparts. Leading Indian-headquartered firms like ChrysCapital, ICICI Venture, TVS Capital and UTI Ventures are building high-quality capabilities that are attracting the attention of foreign investors looking to participate in the Indian PE and VC story.

Overall Equity Investments in PE-backed Companies in India

From the following graph, the first quarter of 2015 saw 130 private equity deals worth 2.77 billion USD, and was the best performing first quarter since 2011. BFSI segment displaced the IT & ITES sector from its top slot, attracting 891 million USD in 14 deals. The IT&ITES segment attracted investment of 836 million USD

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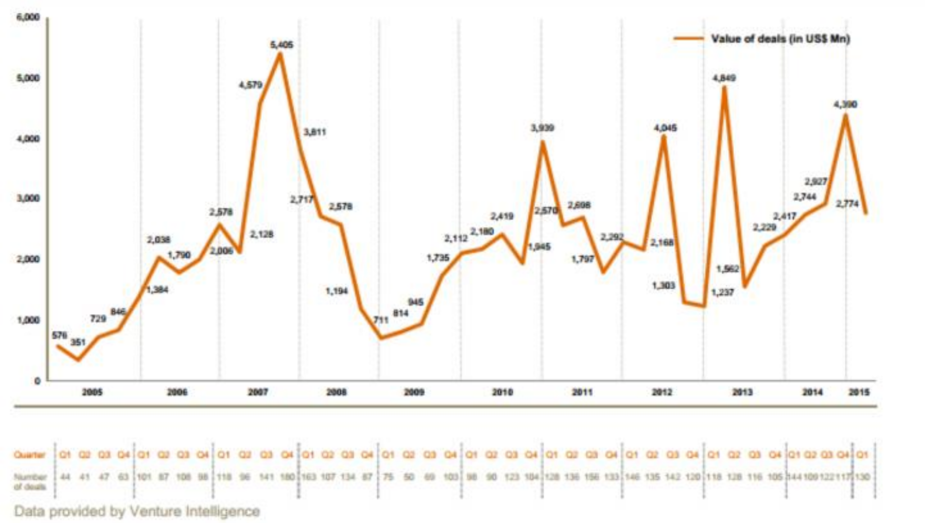
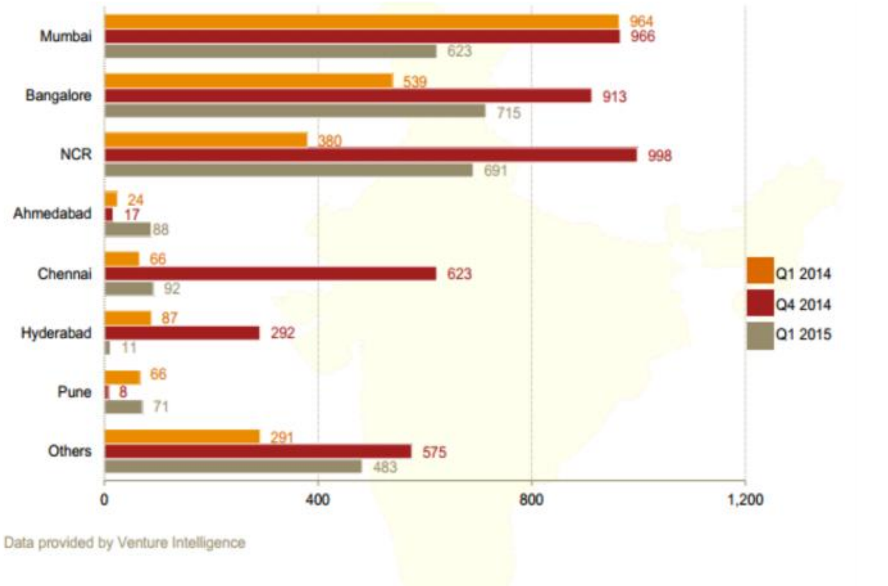
in 71 deals this quarter. Bangalore made a return to the top slot with regard to Private equity investments-both by value and volume of deals seeing 715 million USD invested in 35 deals.



India's strong economic growth, of course, is a major factor propelling PE activity. But the rush to India is also fuelled, in large measure, by a somewhat slower pickup in deal activity in the mature markets of North America and Europe coming out of the recession. The favourable outlook still appears to be based more on India's vast potential than on concrete evidence that private equity in India is poised for a dramatic leap forward. Indeed, it is likely that absent some fundamental changes, private equity in India will fall short of achieving its full promise. PE investors will continue to compete for small deals, accepting passive roles in their portfolio companies rather than bringing their talents to bear to realise their growth opportunities. Promoters and entrepreneurs will continue to view private equity as just another source of capital, and a costly one with unattractive strings attached, at that. Add to this a regulatory environment that constrains deal making, and it is clear that private equity in India is still very much a work in progress.

Investments by region



The above Graph shows Bangalore was once again the busiest investment destination with 715 million USD values of investments in 35 deals. Whereas the National Capital Region (NCR) received 691 million USD in 33 deals, Mumbai has been pushed to third place with 623 million USD investments in 26 deals

Since 2007, the banking and financial services sectors have mostly constituted a majority of the PIPE deals. For example, in 2015, banking and financial services had comprised over 45% of the total PIPE investments. However, in 2012, IT and ITES (Information Technology Enabled Services) accounted for 45.5% of the PIPE investments. PIPE deals had crossed the $1-billion mark in the first half of the calendar year 2015. This was higher than the total PIPE investments in 2013 and 2014. Private investment in public equity has increased 40% in 2015, according to data available from VCC Edge, a database of PE deal activity, and JM Financial Ltd. According to SanjeevKrishan, leader of private equity and transactions at Pricewaterhouse Cooper, a majority of PIPE deals are led by a handful of large private equity funds which invest in financial services firms as well as healthcare sectors.

Private investment in public equity (PIPE) involves the selling of securities issued by companies that have publicly traded stocks to private investors and represents an increasingly important avenue for raising equity capital

Many promising Indian businesses have learned from hard experience that rushing to the public equity markets prematurely can be a mistake. Although the capital they raise in an IPO can help finance an initial growth spurt and enrich the promoters, many newly public companies discover that their shares languish once they are listed. Lacking a strong track record for revenue and profit growth, their shares are thinly traded. Many discover that they cannot go back to the public markets for more capital without seriously diluting existing shareholders. Working with private equity backers, instead, enables these companies patiently to build their businesses outside of the public glare. They are better able to choose a more propitious timing of their IPOs when their balance sheets and income statements are strong enough to withstand public shareholder scrutiny.

India will need to tap every potential source of capital to continue to achieve its growth aspirations, and private equity is an important asset class that can play a critical role in enterprise value creation.

Private Equity investments in India touched a record high of $16.8 billion in 2015 (across 661 deals), 16% higher than the previous high of $14.5 billion (across 529 deals) recorded in 2007 and a whopping 50% higher than the $11.2 billion (across 530 deals) invested during the previous year.

India's Ranking in PE Investment according to various parameters India has carved out a niche for itself in the Global private equity market. India ranks number one in terms of the compound average growth rate of 79% followed by Malaysia (67%) and Denmark (56%). The CAGR for US was 12% while for UK it was 19%. India ranked 3rd in terms of funds raised and investment value after USA and UK. In terms of ranking based on high-tech investment, India was ranked 3rd after USA and UK while in terms of expansion investment trends India was ranked 2nd after USA. The table below gives a snapshot of India's ranking according to various parameters.

India witnessed some significant macroeconomic and policy changes in 2016, which include the passing of the Goods and Services Tax (GST) Act and “demonetisation,” which on November 8, 2016, rendered Indian 500- and 1,000-rupee currency notes, about 85% of the total bank notes in circulation, illegal. However, most surveyed investors in India believe these changes are a positive step and an opportunity. They believe that while demonetisation may affect short-term growth due to a sudden liquidity squeeze and long waiting periods for cash withdrawal, it should have a long-term benefit. The intended benefits and outcomes of demonetisation include turbocharging digital payments, boosting traditional banking by increasing the base money in the system and reducing the cash economy, which should result in higher tax compliance.

Today, the implications of demonetisation are still being determined. However, despite these policy changes, the Indian stock market (Sensex) also remained more or less stable during this period. To attract investment, India will need to continue making it easier to do business in the country, a large part of which involves a regulatory environment that is more conducive to business growth. Towards this goal, the government has encouraged investments through policies such as Make in India, tax regime rationalisation and Startup India, and it has set up the National Investment and Infrastructure Fund (NIIF) to enhance infrastructure financing in India. The government is also fast-tracking approvals for industry and infrastructure projects, as well as relaxing Foreign Exchange Management Act (FEMA) rules to provide easier access to capital for domestic investment funds.

Opportunities and Challenges of PIPE in India

Opportunities

Strong market fundamentals make India an attractive destination for PE investment. However, the rush to India is also fuelled to some extent by a lack of attractive investment opportunities in the mature markets of North America and Europe, where deal activity remains sluggish and credit conditions are tight. India's PE market will continue to grow at a healthy double-digit rate over the next few years. But absent some fundamental changes on the part of promoters and regulators, its long-term growth potential could be constrained. Each of the major parties to private equity's fate-PE firms, promoters and regulators- can take steps today to put in place conditions that will ensure that the benefits of private equity's potential are achieved.

PE firms need to sharpen their capabilities along each phase of the investment life cycle, from deal sourcing to exit. As competition among PE firms in India heats up, it will be those that can differentiate themselves through sector specialisation, enhanced due diligence and an ability to identify value-creating opportunities that will be positioned to make the right investments at the right price.Learning how to steer from a backseat position requires PE investors to adopt a different mind-set-one of quiet coaxing and coaching rather than command and control. Promoters can get far more value out of their relationship with PE investors by choosing partners who are aligned with their vision for the future of their business and have the expertise to help them realise it. Indian businesses that have not yet worked with VC and PE investors-or have been reluctant to accept funding from these sources-may want to give private equity a fresh look.

Regulators can have a major influence in advancing the potential benefits of private equity in India by lifting the cap on the open-offer rule and liberalising disclosure norms when potential investors need confidential information to conduct their appropriate due diligence. Overall, Indian businesses and regulators need to take visible steps towards removing the barriers-legal, cultural and attitudinal-that continue to block private equity from delivering its full potential.

The increasing impact of private equity on Indian business is a dual effect of indigenous factors such as an expanding domestic market and globalization which would further scale up the PE Segment. However, at the same time, there are various opportunities and challenges that are faced by private equity players in India. According to Dossani (2006), there were various advantages for running a PE firm in India such as cost competitiveness which may be vanishing fast; development of a strong capital market environment which is capable of providing capital for the next stage growth.

Opportunity for SMEs

The Small and Medium Enterprises (SMEs) in India is an emerging segment and look for various avenues for raising funds. In such a scenario, PE investments are an alternative and viable source of financing the SMEs not only because of the financial support that they can provide but also because of the global exposure that can be provided to the SME sector. This is in form of deploying members of their team on the boards of directors of their investee companies and taking active part in their governance and activities. This would bring more accountability, transparency and corporate governance. Further, the portfolio companies would also get exposure to global standard practices in operations, human resources management, financial planning, reporting and investor relations.

Opportunity in Key sectors

Sectors like back-end retail, logistics, infrastructure, power, renewable energy, hospitality, transportation and telecommunication have gained favour among the private equity firms. Even the Research and Development sector has caught momentum. Initially, lack of capital to invest in R&D held back corporate India. Private Equity capital is helping address this issue. Growth in R&D investments at PE-backed companies is over twice that at their non PEbacked counterparts.

Other new investment avenues with huge potential for PE investments are education and agriculture sector in India. According to the Venture Capital Intelligence report on 'Private Equity Pulse-Education', over 80% of the fund managers are looking forward to invest into education companies in India . Kaizen is India's first private equity (PE) fund being raised to focus on investing in education businesses. Rabobank Group, launched the India Agri Business Fund, the first PE fund to focus on investing in agribusiness in India. The $100 million fund aims to boost the growth of the sector by making value-added equity investments, with a focus on small and medium enterprises and companies in rural areas. Even Microfinance and Clean Technology are some emerging sectors for PE players.

Key challenges

Before Indian private equity can fully realise its potential, our survey found, promoters seeking PE capital and regulators will need to address several major legal, cultural and business challenges that currently impede the industry's development. Respondents cited five barriers that they consider the most problematic over the next two years. According to Dossani (2006), there were various problems associated with the PE firm in India. They are, lack of well-established domestic network of entrepreneurs, financiers, firms and research institutions; poor operating environment including poor corporate governance at the smaller firms and an inefficient legal system; tax environment and a costly process to create a tax-efficient structure for international investors.

Mismatched expectations: Reluctant to cede control over their companies at anything below a high premium price, Indian promoters have been cool to approaches from PE firms unwilling to meet their valuation expectations It will take a long, robust economic expansion and a levelling off in price-to-earnings multiples to bring the two sides closer together.

Tough competitive environment: As the Indian economy rebounds from the downturn, promoters will be hungry for capital to finance growth. They have a variety of sources to tap for funds, including bank loans, Qualified Institutional Placements and initial and follow-on public stock offerings. Private equity is near the bottom of the list, because it comes with higher costs and more strings attached. They will also need to focus on helping the companies in which they invest meet, or exceed, earnings growth targets if they want to realise PE-type returns. Postdeal value creation will therefore take on increasing importance even in minority-holding situations.

Non-supportive regulatory environment: A lack of clarity about rules and delays by agencies with overlapping responsibility to issue clearances to operate under the Foreign Venture Capital Investment regulations burden the industry. Onerous registration requirements on offshore VC investors dampen the flow of foreign capital into India. To improve the overall investment environment, these investment-distorting tax policies need to be re-examined.

Promoters' reluctance to allow PE investors to exert direct management oversight: Promoters and CEOs are generally not comfortable selling large equity stakes to outside investors. PE funds are often seen as a source of capital and not as an added source of expertise and best business practices. With low stakes, many promoters expect PE firms to be passive investors rather than activist owners that can provide business guidance.

Underdeveloped corporate governance: Many privately held Indian companies lack the transparent reporting and appropriate board oversight PE and VC general managers insist upon in the companies in which they invest. While having nothing to do with PE investments, the fraud and manipulation of accounts at

Satyam Computer Services shook investor confidence and increased calls by shareholders for independent, tough governance standards. Most observers expect that pressure for additional measures to strengthen corporate oversight will continue.

Challenges

Complex Regulatory Issues and Fiscal Challenges

The main barriers to entry for PE's in India are complex regulatory issues relating to sector investment and ambiguities in the Indian interpretation of the tax codes as well as the regulatory costs. Moreover, what aggravates the problem is that there are multiple regulations and little harmonization of guidelines across government agencies (SEBI, RBI, CBDT, Ministry of Company affairs). As on date there are no clear cut guidelines for Private Equity investment.

Future Prospects

Private equity in India has delivered higher returns over a longer time frame and has outstripped other investment avenues. Over the eight year period (2000-2008), on an average, sales of PE backed companies grew at 24.9%, a significantly higher rate than non PE backed companies which grew by 15.5%, Nifty (19%) and CNX Midcap (20.6%).

Further, PE backed companies showed annual Profit After Tax (PAT) growth of 34.6% for the period (2000-2008), significantly higher than non-PE backed companies which showed PAT growth of 25.30%, Nifty 50 companies posted 26.4% PAT growth and CNX Midcap companies showed profit after tax growth of 25.4 %

Private equity has entered the economic mainstream and has gained a lot of momentum over the past few years. As the report of the Planning Commission on 'Technology Innovation and Venture Capital" mentions, VC/PE funding is a percentage of our FDI inflow, it should be nurtured and encouraged further as it creates new ventures and new employment and is invested for the long term and is not that can be pulled out at short notices.. Therefore, PE investments can significantly contribute to forex reserves and also reduce the rupee volatility and be one of the factors towards contribution of financial stability. Further, a simple well defined regulatory regime with no scope of confusion can help the private equity industry to grow further.

Conclusion

PIPEs are increasingly becoming popular to finance growth, acquisitions and for working capital need of smaller firms. The PIPE transactions give access to capital at a lower cost than typical underwritten offerings, while simultaneously also increasing institutional investment in the company and improving the public float of securities. As the PIPE market continues to grow, there are multiple opportunities for private equity investors to invest in a range of companies. PIPE deals give access to capital at a lower cost to finance growth and working capital requirements. PIPE investments offer investors a chance to acquire a block of shares in one go coupled with the prospect of profitable exits with high gains as seen in the above examples. As the government pushes its agenda of foreign investment and ease of doing business in India as well as abroad availability of good companies available in the listed space and access to foreign funds, PIPE deals offer a plethora of funding opportunities for large as well as SME companies.

Signs that Indian private equity may be reaching an important milestone in its path to a more mature phase of development are evident in investors' expectations that deal value will grow, and that the number of buyouts will increase faster than acquisitions of small minority stakes.

Before Indian private equity can fully realise its potential, our survey found, promoters seeking PE capital as well as regulators will need to address several major legal, cultural and business challenges that currently impede the industry's development.

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