

## **Impact of Private Equity Segment on Capital Market in India**

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**Abstract**

The Private Equity is the most vibrant industry in the monetary markets today. It is the finance provided by professionals who invest in young, swiftly growing companies that have the potential to develop into noteworthy economic contributors. The Private Equity industry in India has really taken off recently. Rather providing monetary resources it also helps the entrepreneur with guidance in formalizing his ideas into a viable business venture. With know-how and expertise based ideas set to drive the global financial system in the coming years, and given the intrinsic strength by way of its human capital, technical skills, cost competitive workforce, research and entrepreneurship, India can unleash a insurrection of wealth creation and rapid economic growth in a sustainable manner. The study found a collision of Private Equity investment and Exits on Capital Market operation which in turn would bring about shifts in the capital market when private equity has been shown prominent significance.

**Key-words:** *Private Equity, Investment, Exits, Entrepreneurship and Capital Market.*

**Introduction**

The globalization of industries has become the norm across the world, and the private equity industry is no exception. The global value of communication related to private equity funds has increased dramatically over the past few decades. Since 2004 the private equity industry fund-raising has practiced excellent growth that has not been matched in the history of this equity sub-class. The fruition in size and influence of the private equity industry has led to increased transparency and awareness with regard to good corporate governance practices, particularly in respect of early stage investments. Private Equity companies got interested in the Indian Market during the mid-1990s when the unfolding of the process of liberalization and globalization generated a lot of global interest in the Indian economy.

India has been the fastest-growing Private Equity market in Asia along with China and Japan. India's fundamentals will continue to attract eager Private Equity investors and strengthen the confidence of limited partners. The pace and strength of the industry's future growth would be accelerated if valuations in India become more attractive and exits continue to build on the momentum established in 2010. Indian promoters are slowly but surely coming to recognize Private Equity as a patient source of active capital that can help builds their businesses.

**Review of Literature**

**Komala. G (2016)<sup>1</sup>** expressed that performance of private equity funds as reported by venture intelligence and prior research is overstated. The two reasons for the growth of private equity and venture capital in India. First, change in organizational innovation, aided by regulatory and tax framework. Second, adoption of limited partnership and general partnership. The Private Equity and Venture Capital markets 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. This study examines and discusses in detail the PE/VC investments in India during 2014 and 2015. Depiction on publicly available data and fieldwork data, it describes the equity investments in Private Equity backed company, investments by industry, investment by stages of development, investment by regions, and top deals of PE in India. She concludes with market response change too quickly from one end to the other. Anticipation next quarter shows a definite direction for investors.

**Rama Seth and Rohan Chinchwadkar (2012)<sup>2</sup>** stated that Private Equity (PE) investors provide capital to private companies, usually for expansion, new product development, or restructuring of the company's operations, management, or ownership. As the firm grows, PE investors sell their stakes in the company either to return the capital to the limited partners or

to find new investee companies. At the same time, owners of the company might either look for other sources of capital for new projects or look for ways in which they can sell off their stake and exit. There are four major exit outcomes for private equity investors: initial public offering (IPO), financial sale, strategic sale and buyback. The major difference between IPO and other mechanisms is that an IPO involves a large number of dispersed investors whereas the other three mechanisms involve a single or very few investors.

### Statement of the Problem

Foreign investment has been on a growing trend for the recent decade. One of the reasons for this high growth was due to availability of private financial capital for expansion and the positive influence of these private equity houses on Indian management practices. There has been phenomenal growth in the value of private equity investment in India. With an expanding home market and supplementary opportunities brought by globalization, the force of private equity on Indian industry is likely to amplify. Further, in the approaching years the Indian government also recognizes the key task of overseas capital for financial development and as an important foundation of technology and global best practices. In this framework the role of private equity as an important component of foreign capital has been very crucial for the development of Indian economy.

Private equity investments have been a part of India's emerging fairy-tale for about a decade in which time we have seen a multitude of events that have shaped the investment climate in India. The country's growing global stature, a far more open economy coupled with positive indications of reforms and insight of value residing within the fabric of the economy, encouraged investments into the country. The Private Equity sector, being shown a growing trend and a constituent supporting in a firm's development through investment for a long-term, might have a substantial collision with the capital market of the country. Further, the process involves the risk factor too on the sides of investor, who raise the capital outside or use his own capital for investment. The return on the investment is very volatile. Hence, with the basis of above settings the present study is made as an attempt to identify the answer for the following research questions;

1. What is the growth and composition of Private Equity Investments and Exits in India?
2. Whether the Private Equity Investment and Exits have the impact on Capital Market in India?

### Objectives of the Study

The following are the objectives of the study:

1. To analyze the composition, growth and trend of Private Equity Investments and Exits in India.
2. To analyze the sector wise investments and exits made through Private Equity Investments in India.
3. To examine the impact of Private Equity Investments and Exits in SENSEX movement.

### Hypotheses for the Study

The following hypotheses are framed for testing;

**H<sub>01</sub>**: Unit Root among the Private Equity Investment, Exits and SENSEX Movement in India does not exist.

**H<sub>02</sub>**: Co-integration between Private Equity Investment and SENSEX Movement does not exist.

**H<sub>03</sub>**: Co-integration between Private Equity Exits and SENSEX Movement does not exist.

**H<sub>04</sub>**: Private Equity Investment and Exits have no impact on SENSEX Movement in India.

**Research Design****Sources of Data**

The study is based on secondary data and the required data for the study has been collected and compiled from Venture Intelligence Report, Bain Company Report (MoneyTree) and other Journals and Magazines.

**Period of Study**

The period of study covers the eleven years from 2011 to 2020 (Q1)

**Framework of Analysis**

The study evaluates the sector wise investments and exits of Private Equity in India and focuses the impact of Private Equity investments on SENSEX movements. The collected data will be used for analysis with the help of Statistical and Econometric tools. The Statistical tools, namely Mean, Standard Deviation (SD), Co-efficient of Variance (CV), Compound Annual Growth Rate (CAGR) and Regression Analysis and the Econometric tools namely Augmented Dicky Fuller (ADF) Test and Auto Regressive Distributed Lag (ARDL) will be used.

**Significance of the Study**

The present study will highlight the composition of Private Equity investment in India and its significance on the Indian capital market. The Private Equity investment as a part of foreign capital gained importance in the modern era of globalization in the economic development of the country, hence taken into consideration. The study will highlight the composition and growth of Private Equity Investment and Exits in India. The study would be helpful in understanding the impact of Private Equity Investment and Exits in Indian capital market and further it would render valuable information to the academicians and researchers to develop new ideas for further study.

**Limitations of Study**

The study has the following limitations;

1. The study will be applicable only to Indian Private Equity mode of Investments and Exits and not applicable to any other mode of investments.
2. The study is applicable only to India and may not be to any other part of the globe.

**H<sub>01</sub>:** Unit Root among the Private Equity Investment, Deals and SENSEX Movement in India does not exist.

**Table 1: ADF Test of Private Equity Investment, Exits and Sensex Movements**

Variables	Level		First Difference		Second Difference	
	ADF Test Statistic	Prob	ADF Test Statistic	Prob	ADF Test Statistic	Prob
<b>PE INVESTMENT</b>	-2.807434	0.2029	-5.976347	0.0000		
<b>PE EXITS</b>	-1.710639	0.7264	-1.934111	0.3137	-7.589722	0.0000
<b>SENSEX</b>	-3.207799	0.0971	-2.810374	0.0668	-11.39942	0.0000

**Source:** Calculated and Compiled from Venture Intelligence

The result of ADF Unit Root Test of Private Equity Investment, Exit and SENSEX Movement in India is reported in table 1. The null hypothesis of having no stationarity for all variables is not rejected at their level since the ADF Probability value higher than the critical values. This shows that all the variables are integrated at level. After taking the first difference ADF test statistics are compared with critical values, and found that null hypothesis of Unit Root is rejected for Private Equity Investment. The variables Private Equity Exits and SENSEX Movements have become stationary at second difference having the ADF Probability values higher than the critical values.

**H<sub>02</sub>:** Co-integration between Private Equity Investment and SENSEX Movement does not exist.

**Table 2: ARDL Test Results-Dependent Variable PEI**

Variable	Coefficient	Prob.
PEI	-0.369855	0.0002
SSM	0.0365875	0.9856
C	18.325694	0.0025

*Source: Calculated and Compiled from Venture Intelligence*

**Table 3: Bound Testing for ARDL Co-Integration**

Wald Test			
Null Hypothesis : PEI = SSM = 0			
F-statistic	4.569874	Probability	0.0005
Chi-square	45.369852	Probability	0.0000

*Source: Calculated and Compiled from Venture Intelligence*

Table 3 explains the Bound test results. Probability value of F statistics is less than 0.05, so the null hypothesis is rejected. This result can be indicates from the table 4.35 that the probability value of PEI is 0.0011, which is less than 0.05. Therefore the null hypothesis is rejected that means there is co-integration between the Private Equity Investment and SENSEX Movement. In other words, Private Equity Investment affected SENSEX Movement in the long run between the quarters.

**H<sub>03</sub>:** Co-integration between Private Equity Exits and SENSEX Movement does not exist.

**Table 4: ARDL Test Results-Dependent Variable PEE**

Variable	Coefficient	Prob.
PEE	-1.3265	0.0041
SSM	-5.0823	0.3658
C	156.2314	0.0223

*Source: Calculated and Compiled from Venture Intelligence*

**Table 5: Bound Testing for ARDL Co-Integration**

Wald Test			
Null Hypothesis: PEE = SSM = 0			
F-statistic	3.258464	Probability	0.0024
Chi-square	32.365841	Probability	0.0033

*Source: Calculated and Compiled from Venture Intelligence*

According to the bound test results illustrated in the table 6, the probability value of F statistics is less than 0.05, so the null hypothesis is rejected. This result can be inferred from the table 5 that the probability value of PEE is 0.0090, which is less than 0.05. Therefore, the null hypothesis is rejected that means there is co-integration between the Private Equity Exits and SENSEX Movement. In other words, Private Equity Exits affected the SENSEX Movements in the long run between the quarters.

**H<sub>04</sub>:** Private Equity Investment and Exits have no impact on SENSEX Movement in India.

**Table 6: Regression Analysis of Impact of Private Equity Investment on Sensex Movement in India**

Variable	Coefficient	Std.Error	t-Statistic	Prob.
PEI	-1.1918	8.2136	-0.6248	0.5238
PEE	-5.0909	1.0002	-3.3698	0.0009
C	-5.1888	1.9080	-3.8302	0.0033
R-Squared	0.4325		Durbin-	1.9232

<b>Adjusted R-squared</b>	0.6685		<b>Watson stat</b>	
<b>F-statistic</b>	9.8942		<b>Prob (F-statistic)</b>	0.0001

**Source:** Calculated and Compiled from Venture Intelligence

The above table 8 shows the regression analysis between Private Equity Investment and Exits with SENSEX Movement. The analysis placed SENSEX as dependent variable and Private Equity Investment and Exits Worth as independent variable. The analysis shows ( $R^2 = 0.4325$ ), which states that the Private Equity Investment and Exits contributed significantly for the changes SENSEX in India. It can be inferred from the table that Adjusted R-square value is 0.6625. This indicates that 66 percent of the variations in the SENSEX Movements are explained by Private Equity Investment and Exits. The F-statistic is significant at all levels indicating that the hypothesized relationship between the Private Equity Investment and Exits and SENSEX Movements is validated. The value of Durbin-Watson statistic is 1.2932 indicating that the model is not suffering from auto correlation problem. The calculated F value is more than the table value and hence, the null hypothesis is rejected and there is a significant effect by Private Equity Investment and Exits on SENSEX movement in India.

### Suggestions

1. The investments in other sectors namely Manufacturing, Food and Beverages, Engineering and Construction etc., apart from the sectors considered in the study shall be improved to acquire equanimity.
2. Deploying themselves in the board of the companies invested the investors can bring in more accountability, transparency and corporate governance in companies.
3. Apart from financial assistance the investors by becoming the board members can assist in strategic planning, marketing of products, technical, funding, branding, operations, manpower recruitment and training.

### Conclusion

Today, Private Equity (PE) funds have become a crucial source of finance for corporate and has earned the status of an important asset class. It is the provision of capital and management expertise to companies in order to create value and subsequently, with a clear view to an exit, generate capital gains after a medium to long holding period. With an expanding domestic market and additional opportunities brought by globalization, the impact of private equity on Indian business is likely to increase in the coming years. However, the rapid growth and globalization of the PE industry has raised demands for increased regulation and disclosure within the sector due to concerns regarding anti-competitive behavior, excessive tax benefits and stock manipulation. With growth in the European markets almost becoming stagnant and other countries in the globe in equally tight economic conditions, India and parts of Asia and Africa are believed to be experiencing the next phase of the growth.

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