



Funding Winter Impact on Start-ups

For Prelims: Funding Winter, [Stand-Up India Scheme](#), [Pradhan Mantri Mudra Yojana](#), [Startup India Action Plan](#)

For Mains: Indian Startup Ecosystem, Government's Initiatives for Startups

[Source: TH](#)

Why in News?

Bengaluru, often hailed as the **Silicon Valley of India**, has faced a significant setback in its vibrant [start-up ecosystem](#) due to a **funding crunch** triggered by global events. The aftermath of the **funding winter** has left many regional start-ups grappling with challenges ranging from layoffs to cautious investor sentiment.

What is Funding Winter?

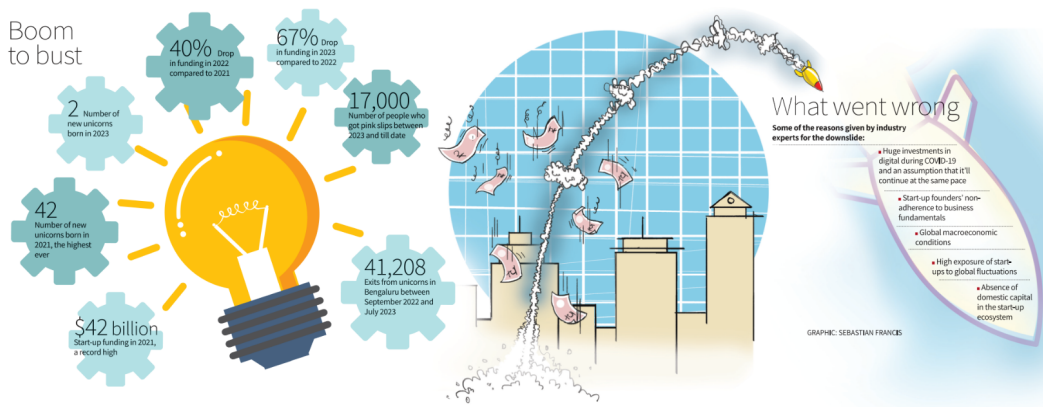
▪ About:

- Funding winter is a term used to describe a **period of reduced capital inflows to startups**.
- During a funding winter, investors and lenders become more cautious and **selective in providing financial support**, leading to a decrease in the overall funding available in the market.
- Funding winters can significantly **impact businesses and entrepreneurs**, particularly those in the early stages of development or those seeking to expand their operations.

▪ Reasons for Funding Winter in India:

- **Fluctuations in Indian Start-up Funding:**
 - In 2021, Indian start-up funding surged to a **record USD 42 billion, creating 42 new unicorns**. However, **2022 witnessed a 40% funding drop**, marking a shift from pandemic-driven optimism.
 - The initial boom was fueled by massive investments in digital ventures during the [Covid-19 pandemic](#).
 - There was an assumption that the [digital trend would continue](#) at the same pace, but as the world returned to normalcy, a reassessment of investments occurred.
 - As per data, tech companies in India saw funding to the tune of **USD 8.3 billion in 2023, a 67% drop from 2022**.
- **Global Macroeconomic Factors:**
 - Global events, including the [Russia-Ukraine](#) and [Israel-Palestine conflicts](#), played a crucial role in triggering the funding winter.
 - The resulting **uncertainty in the global supply chain** and trade outlook contributed to a bleak investment scenario for start-ups.
 - The general [slowdown in global economies](#) had a cascading effect on investor confidence and capital flow.
- **Return on Investments (ROI) Focus:**

- Investors began scrutinizing the **sustainability and profitability of start-ups, leading to a correction in the market.**
- Investors exhibit **decreased confidence in unicorns** and late-stage start-ups that **prioritise growth over profitability.**
- Investor interest and activity have shifted towards **early-stage start-ups**, emphasising caution and a focus on revenue models.
- The absence of **mergers and acquisitions**, coupled with **poor performances** of listed start-ups, left investors without viable exit options.
 - The dearth of exit strategies contributed to a challenging environment for both investors and late-stage start-ups.
- **Absence of Domestic Capital:**
 - Lack of **domestic capital in the Indian start-up ecosystem** worsens the funding crisis.
 - **Domestic Pension Funds** are not investing in technology, venture, and start-ups, which is a missed opportunity for the country.
 - The Union Ministry of Finance and regulatory system are hostile to the tax issues of start-ups.
 - The latest regulations by the **Reserve Bank of India** restrict banks and **Non-Banking Financial Company (NBFC)** from investing in **Alternate Investment Funds (AIF)**, which is seen as authoritarian.
- **Macro and Microeconomic Challenges:**
 - Both macroeconomic conditions and the failure of some start-up founders to adhere to fundamental business principles compounded the crisis.
 - The crisis was not only a result of external factors but also **internal decisions and strategies** within the start-up ecosystem.



What is the Impact on Start-ups and Employees?

- **Mass Layoffs:**
 - A major repercussion of the funding winter has been mass layoffs. According to data from the **international layoffs.fyi (tracks tech startup layoffs)**, tech companies gave the **pink slip to around 17,000 people in India from 2023 to January 2024.**
- **Silent Layoffs:**
 - Companies resort to '**silent layoffs**' by **giving lower ratings**, nudging employees to leave, rather than explicit layoffs.
- **Attrition Rates:**
 - Between September 2022 and July 2023, 111 Indian unicorns experienced an **attrition rate (rate at which employees depart an organisation) of 4.72%**, with 41,208 employees exiting in Bengaluru alone.

Startup Ecosystem in India

- India has emerged as the **3rd largest ecosystem for startups globally** with over 1 Lakh **Department for Promotion of Industry and Internal Trade (DPIIT)**-recognized startups across 763 districts of the country as of 3rd October 2023.

- **India ranks 2nd in innovation quality with top positions in the quality of scientific publications and the quality of its universities among middle-income economies.**
 - The innovation in India is not just limited to certain sectors it spans in 56 diverse industrial sectors with 13% from IT services, 9% healthcare and life sciences, 7% education, 5% agriculture and 5% food & beverages.
- **Indian Startup Ecosystem has seen exponential growth in past few years (2015-2022):**
 - **15 times increase in the total funding of startups.**
 - 9 times increase in the number of investors.
 - 7 times increase in the number of incubators.
- As of October 2023, **India is home to 111 unicorns with a total valuation of USD 349.67 billion.** Out of the total number of unicorns, 45 unicorns with a total valuation of USD 102.30 billion were born in 2021 and 22 unicorns with a total valuation of USD 29.20 billion were born in 2022.
 - 2023 saw the emergence of **Zepto as the latest and only unicorn in the year.**

What are the Indian Government's Initiatives for Startups?

- [Pradhan Mantri Mudra Yojana.](#)
- [Stand-Up India Scheme.](#)
- [Atal New India Challenge 2.0.](#)
- [National Initiative for Developing and Harnessing Innovations \(NIDHI\).](#)
- [Startup India Action Plan \(SIAP\).](#)
- [Ranking of States on Support to Startup Ecosystems \(RSSSE\).](#)

Way Forward

- The entire ecosystem must **prioritize business fundamentals**, maintaining the right ratios and balances, and planning for future cycles.
- There is a need for **structural-level reforms in financing**, including collateral-free loans for start-ups, to ensure sustained growth.
- Continued government support, like **Karnataka's ELEVATE program** can play a crucial role in preventing start-up failures and fostering a resilient ecosystem.
 - Karnataka's ELEVATE program gives a **one-time grant of up to ₹50 lakh to early-stage start-ups.** Under preferential market access, the government aims to promote public procurement from start-ups.
 - The government should implement **policies to incentivize domestic investments**, especially from pension funds.
- Start-ups need to **adapt to market dynamics** by embracing frugality, efficiency, and organic business leads.

UPSC Civil Services Examination, Previous Year Question (PYQ)

Prelims

Q1. What does venture capital mean? (2014)

- (a) A short-term capital provided to industries
- (b) A long-term start-up capital provided to new entrepreneurs
- (c) Funds provided to industries at times of incurring losses
- (d) Funds provided for replacement and renovation of industries

Ans: (b)

Q2. Which of the following statements is/are correct regarding Smart India Hackathon 2017? (2017)

1. It is a centrally sponsored scheme for developing every city of our country into Smart Cities in a decade.
2. It is an initiative to identify new digital technology innovations for solving the many problems faced by our country.
3. It is a programme aimed at making all the financial transactions in our country completely digital in a decade.

Select the correct answer using the code given below:

- (a) 1 and 3 only
- (b) 2 only
- (c) 3 only
- (d) 2 and 3 only

Ans: (b)

Mains

Q1: The nature of economic growth in India in recent times is often described as a jobless growth. Do you agree with this view? Give arguments in favour of your answer. **(2015)**

PDF Reference URL: <https://www.drishtiias.com/printpdf/funding-winter-impact-on-start-ups>

