

POOR CAPITAL ALLOCATION?

IT Cos' Startup Investment Not Sound Strategy, say Analysts



IT's a Startup Connection

Cognizant

No venture fund but has a systematic programme to engage with startups

Infosys

\$500 m venture fund. Half is to be invested in Indian startups; has made 2 investments

Wipro

\$100 m fund; has made two investments so far

HCL Technologies

No venture fund

TechM

\$50 million

joint fund with SBI Holdings, Japan (investment is **\$25 million**); no known investment yet

Persistent

\$10 million

fund; targets investing in up to 40 startups globally through the fund and has already invested in five

TCS & Cognizant

No venture fund, but have a systematic programme to engage with startups

Experts feel returns are uncertain for tech majors' venture capital arms

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Mumbai: Indian IT companies' move to set up corporate venture capital arms to join the current gold rush in startups hasn't gone down too well with equity analysts who argue that the strategy is unsound and returns uncertain.

Infosys, Wipro, Tech Mahindra and Persistent Systems have set up venture capital arms — with funds ranging from \$10 million to as high as \$500 million — to enter the world of startups in hope of finding innovative ideas and technologies that they may not be able to create in-house.

However, analysts are not pulling any punches in criticising this strategy. "We find no merit in the strategic reasons given to support such investments," said Sagar Rastogi, analyst with Ambit Capital. "Moreover, given significant disadvantages as compared to independent venture, we consider corporate venture funds to be poor capital allocation," he said in a note. "Infosys with investments in early stage startups far removed from its core business is the

worst offender," Rastogi said. Infosys has created a \$500 million (approximately ₹3,150 crore) 'innovation fund' to back startups and innovations.

It has made two minority investments so far — in a spinoff of Dreamworks Animation Studio, which has digital technologies, and Airwiz, a maker of indoor pollution sensors. Analysts say both firms are far removed from Infosys's core business with large enterprise customers.

Tata Consultancy Services and Cognizant, too, work with startups although they don't invest in them.

Viju George, analyst with JPMorgan, said the financial services firm is not a backer of the idea of corporate venture capital funds (CVFs) as they can stifle innovation.

"In trying to detect some use of the startup business model for the parent, the CVF runs the risk of undermining the funded company in the first place. It is conceivable that in the name of adding value to the parent and exploring/driving technology synergies, the startup ends up getting somewhat straightjacketed," he said.

George also pointed out the problem of minority stake giving insufficient bargaining power, as happened with Wipro in the case of its investment in Axeda. Wipro had to exit when Axeda was sold to an outright buyer.

Even some startup entrepreneurs find it hard to accept funding from large Indian IT players. "If I take an investment from one, then it would be hard to work with the other players in the market and I would narrow the number of potential partners. Working with them on joint-go-to-markets makes more sense," Rohil Sharma, CEO of disaster recovery optimisation company Perpetuuti Technosoft, told ET in an interview in October.

Viju George of JPMorgan said such corporate venture capital funds can stifle innovation