



# Innovation in public policy

A public policy push is required to enhance investment in start-ups and thus fuel a national drive towards innovation, says **Govind Sankaranarayanan**

Not so long ago, *The New York Times* wrote an article which suggested that there was considerable concern in India over the absence of path-breaking innovators such as Google or Apple in the country. The authors seemed to believe that though India has performed fairly well in its outsourcing story, it still lacks the structural supports essential for robust innovation, in particular, more sophisticated forms of financing.

This argument has been further fuelled by leaders of some start-ups, such as the award-winning Shloka Telecom, who have been candid about their frustrations at the risk-aversion propensity among those who fund start-ups.

There is some merit in examining why venture capital (VC) funding in India is so anaemic. The answers lie in many different aspects of our economic structure.

The well-known academic Amar Bhide, in his book *The Venturesome Economy*, has opined that while in popular imagination the United States appeared to be losing ground in the manufacturing sector, it has continued to lead the translation of innovation into commercial use.

Mr Bhide refers to the success rate of a large number of products that were launched in the US, a nation where consumers are basically inclined towards trying out new things. What this implies is that many products, even those that prima facie do not appear promising to an investor, actually succeed in the marketplace because there are enough persons willing to try them out.

Mr Bhide contrasts this to the situation in many other countries where there is a natural aversion to change. What reinforces this psychographic preparedness to experiment is the fact that the US is also a very large market unlike, say, smaller countries

in Europe. As a result, it is possible for a new company to launch a product within just the domestic market in the US and meet with some commercial success.

## Ready to experiment

Perhaps as a natural extension of this thesis, we find that the US is also the country with the maximum levels of investment in innovation. For different stages of a company's life, there are seed, angel and first round investors who have, in one form or another, existed in the US for the better part of 75 years. The reason for their continued prevalence is the fact that investors at various stages have had a fairly good strike rate of conversion to success. In addition to the list of investors who have become billionaires, there are simply hundreds of others whose profits have been in the humble tens of millions. Indeed, nothing succeeds like success, and the success of the early generation of angel investors has led to the perpetuation of a culture of willingness to invest.

The situation in India, although superficially similar to the US in that it has a large domestic market, is also different in several ways. The Indian market is fairly heterogeneous; mass marketing can sometimes be a challenge because of our multilingual nature; and many years of scarcity have led to a strong inclination to save.

This is a sharp contrast to the US, which is more homogenous in many ways, and demonstrates a preparedness to consume at the expense of savings. These differences can lead to a self-fulfilling prophecy where many new products and services fail in the marketplace.

## Risking new ventures

High net worth individuals in India factor this difference into their thinking, and consequently, with

the exception of a few open-minded groups and individuals, there has not been a readiness to loosen purse-strings. Indeed, the total investment in venture capital in India through the domestic route was a scanty few hundred million dollars last year, a fraction of what would be required in a country of this size.

It is inevitable that in a country with a per capita GDP of \$1,000 per year, there should be a lower appetite for experimental consumption. Yet it is important to find some mechanism for investment, despite the higher level of risk (created by the lower propensity to consume) prevalent in an economy that is less rich.

Recognising that individual or private investors will invest rather more reluctantly, there may need to be a public policy initiative that channels a part of the country's savings into venture capital.

Large amounts of savings are currently stashed away in provident funds, pension funds, insurance as well as in the banking system. In today's context, there is very little incentive for even a fraction of the savings to be invested in high-risk asset classes. In some cases regulation actually prohibits such investment and in others there are, perhaps correctly, caps on such investment. Even where, as in the case of insurance companies, regulation does appear to permit investment, there does not exist the appetite to make these investments.

### A push from above

In the face of such a degree of risk aversion, there needs to be an intervention through public policy. The redirection of savings is a tenet of public policy, but the government has not been inclined to do so in the public interest. Channelisation of savings has only taken place through subsidies, support for oil companies, support for infrastructure and the like. Yet it is relatively easy to argue that innovations that create large numbers of jobs, raise the standard of life in backward areas, protect the environment, or increase levels of literacy and other social indicators, have enormous value to large developing countries such as ours.

Let's consider the form such policy initiatives can take. In the UK, there is a department of business innovation skills that has sought to push an agenda for public and private support of innovation, including setting up a fund. The appointment of Aneesh Chopra as President Barack Obama's chief technology officer has led to the expectation of much greater adoption of technology and consequently, technology-related innovation within the US government.

Some of the front-runners in examples of new



innovation may come from within the government itself, as was the case in the US many years ago. In addition, the Obama administration, spurred by the financial downturn, came out with a series of measures which supported industries in the healthcare, education and clean energy sectors; in many cases, the funding was explicitly supportive of companies which were involved in the creation of new technologies.

There is no reason similar initiatives cannot be introduced in India. If even half a per cent of the savings locked within the financial institutions were to be mandated for support of VC style investing, it would make a material difference to the quality of innovation across this country.

Were this to be done on a coordinated and systematic basis, perhaps through a series of well-managed funds with independent oversight, one could minimise the downside risks to any one investor group. Nobel laureate Linus Pauling once said that the best way to get great ideas was to have many of them. Only substantial support for many ideas will enable us to identify the next great idea. ●

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