UNVEILING THE ROLE OF ANGEL INVESTORS IN SME GROWTH - A LITERATURE REVIEW

[1]DR. RATINDER KAUR
[2]SARBJEET KAUR

[1]Assistant Professor, Punjabi University, Patiala
[2]Research Scholar, Punjabi University, Patiala

Abstract

Angel investment is a crucial component of informal equity investing in India, which has been there for a very long time; in fact, it is possible that it is the most important component. Over the course of the last ten years, it has attracted a growing amount of attention for a number of different reasons, one of which is the widespread penetration of angel networks. Informal equities investment in India is a study subject that is substantially undeveloped and has not been examined to a significant extent. The goal of this study is to get an understanding of the connection that exists between angel investment and the small and medium-sized enterprise (SME) sector in India. Data that is easily accessible to the general public is the only source of information that will be use here. According to the conclusions of this research, angel investment has an impact on the expansion of small and medium-sized enterprises (SMEs) that it funds. Based on the findings of the research, small and medium-sized enterprises (SMEs) that work together with angel investors see a higher rate of growth. The following is a description of the structure of the essay. A complete overview of angel investments and the small and medium- sized enterprise sector is presented in the first part. A detailed discussion of the pertinent research may be found in the next section. Specifically, the reference for the data source may be found in the third section. A presentation of the findings can be found in the fourth part, which also includes a discussion of possible directions for further investigation.

Keywords: Angel Investments, Angel investors, Performance, Early-stage funding, Small-Medium enterprises (SMEs).

1. Introduction

The mindset of Indian youth has undergone a significant transition in the last twenty years, which has contributed to India's robust economic growth. According to the most recent figures, 55,000 people in India have registered, which is 100% higher than startups in 2015 (Kamaluddin, 2021). Private equity firms, venture capitalists, and angel investors are the main investors. Angel investors make major contributions to early-stage firms as a result of the shift in focus among venture capitalists. After a startup company bootstraps with the aid of friends and family, angel investors are the main source of seed money (Timmons, 2008).

1.1 Concept of SMEs

Over the last 50 years, the Small, and Medium Enterprises (SME) sector has grown to be a very active and dynamic area of the Indian economy. After agriculture, it becomes the second largest contributor to the social and economic growth of the country by encouraging entrepreneurship and creating major employment opportunities at comparably low capital costs. The SME sector makes a substantial contribution to the country inclusive industrial growth by acting as an ancillary unit to large businesses. The SMES sector produced a wide range of goods and services to satisfy the needs of both domestic and international markets, expanding their sphere of influence across economic sectors.

The Small, and Medium Enterprises (SMEs) are categorized as follows in compliance with the provisions of the Micro, Small, and Medium Enterprises Development (MSMESD) Act, 2006: (i) a micro enterprise, where the investment in plant, machinery, or equipment does not exceed Rs. 1 crore and the turnover does not exceed Rs. 5 crores; (ii) where the investment in plant, machinery, or equipment does not exceed Rs. 10 crore and the turnover does not exceed Rs. 50 crores, is a small enterprise; and (iii) where the investment in plant, machinery, or equipment does not exceed Rs. 50 crore and turnover does not exceed Rs. 250 crores, a medium enterprise.

As of December 31, 2020, a total of 8,65,058 businesses were registered in the service sector, while 5,37,677 businesses were registered in the manufacturing category. • Food Products, Textiles, Apparel, Fabricated Metal Products, and Machinery & Equipment make up the top 5 industrial sectors for registrations.

1.2 Angel Investing in India

Angel investing has been practiced in India for a very long time, according to Shane (2009) definition. These were essentially investments made by wealthy members of industrial families who supported and provided financial help to members of their community or other friends or acquaintances who wanted to start up their own businesses. However, as we know it today the growth of angel investing only began with the emergence of a class of investors who were not from a traditional industrial family, who were first-generation business owners who had made a profit, and more recently wealthy corporate executives who used angel investing as a part of their own personal asset allocation strategy. The actions of angel investors in India must be seen in the larger context of supply and demand for early-stage finance in the country. The Planning Commission's (2012) optimistic prognosis may be used to analyze the demand for early-stage funding. In the ten years after the report, the Task Force predicts that around US $ 700 million in angel investments will be needed. In turn, this also appears to be related to their estimate that 10,000 startups have the potential to grow into 2500 firms, which would need a capital infusion of US $ 55 billion, split equally between debt and equity, which is anticipated to be necessary. The study provides a list of a wide variety of subsectors that are expected to offer investment opportunities. These will originate from the crucial industries of manufacturing and related services, technology, healthcare, and related services, education, luxury and personal care services, and infrastructure. The study is significant because it lays out the first design for nine national- level institutions that would be involved in the creation and supervision of the channeling of money to the entrepreneurial ecosystem. As per the numerous varieties of sources from which these funds come, there are many approaches to examining the supply of early-stage funds in India apart from traditional institutional sources like investment funds. Entrepreneurs who have made a profit can be an important source of early-stage equity financing. The family offices of affluent industrialists might become another source of funding. Thus, we look at the most likely superset of funding sources, since our focus is on the participants themselves, which is the group of high-net-worth individuals known as Angel Investors. According to CapGemini (2013a), the number of High-Net- Worth Individuals (HNIs) increased i.e., from 123000 in 2007 to 153,000 in 2012 but this growth was not monotonically. Their wealth increased, from US$ 437 billion to US$ 589 billion over the span of time, but again not monotonically. As per the estimation of Kotak and Crisil (2012) there are a number of 81000 Indian households with ultra-high net worth, defined as those with a wealth of Rs 25 crore or more, equivalent to Rs 65 trillion in wealth as of 2011–12. By 2016–17, they forecast an increase in these figures to 281000 households and Rs. 318 trillion, respectively. In 2016 (Sabrinathan, 2019), angel investors completed more than 855 deals successfully.

According to Karvy (2013), the estimation as per his study was that individual Indians held the entire value of financial assets estimated to be Rs 109,86,166 crores, of which 24% was invested in direct stocks and Rs 32,000 crores in alternatives, which amounted to Rs 4117 crores in private equity funds. So, because the marketing of private equity funds is constrained by legislation to high-net-worth individuals, it is logical to assume that the whole allocation to private equity originated from HNIs. According to research, HNIs displayed risk aversion in their asset allocation approach between 2011 and 2013, placing a greater emphasis on wealth preservation than the quest for exceptional returns. These reports of the HNI universe focus on a different aspect and use a different methodology and set of assumptions for their analyses when viewed collectively, a picture of (i) a high level of wealth that can support more risk-tolerant investment choices (ii) a low-level of allocation to asset classes like private equity or early-stage equity as at present and (iii) once they increase their allocations to unlisted equity, the volumes that are required as unlisted equity becomes more popular emerges. Through the conclusion of 706 agreements in the year 2021, an Indian firm succeeded in securing a sizeable sum of money totaling $1.1 billion (Inc42, 2021).

2. Review of Literature

2.1 Angel Investment

Once the money from founders, family, and friends commonly referred to as the &quot three Fsquot has run out, standard entrepreneurship textbooks like Timmons and Spinelli (2008) and Sahlman et al (1999) recognize angel investors as the initial source of external financing.

According to Shane (2009), an angel is &quota person who provides finance, in the form of debt or equity, from his own funds to a private business owned and run by someone else who is neither a friend nor a family member". Unlike an angel, a second definition of an informal investor is someone who invests in organizations that are owned by others, including friends and relatives. According to Macht and Robinson (2009), "private wealthy individuals are the ones who invest their money and experience in small, unlisted, entrepreneurial ventures " and are considered angels. Others, like Laszlo et al. (2007), have made an effort to categorize angels based on family relations and bonds, or the lack of such things. Research on angel investors reveals that they are typically high-net-worth individuals who engage in entrepreneurial companies as part of a broader portfolio, as described by Freear et al. (2002), despite the fact that the profile of angel investors varies greatly between nations. While generally speaking, angels have been thought to maintain their anonymity, as noted in Benjamin and Margulis (2000). According to Shane (2009), there are several reasons why people choose to become angel investors: To (i) earn money (ii) join private companies (iii) study new things (iv) pursue a pastime (v) land a job (vi) and to (vii) make money.

2.2 Performance Measurement of SMEs

We provide a summary of pertinent research on the operation of micro-to-medium-sized businesses in this section. According to Neely et al. (2005), performance measurement is the process of calculating an action efficacy and efficiency. According to Lönnq vist (2004), performance measurement is a method used to ascertain the state of one or more attributes of the measurement objects. According to Radnor and Barnes (2007), quantifying the input, output, or degree of activity of an event or process also qualifies as performance measurement. The literature has characterized the performance of micro small and medium-sized businesses (SMEs) in a variety of ways, and in any business, linked parties always want to see high performance in their organization (Harash et al. 2014; Harash et al. 2013). Performance is defined as a measure of how effectively a corporation can utilize its resources from its principal mode of operation and generate income (Selvarajan et al.2007; Thrikawala, 2011; Watson, 2007). On the other hand, according to contemporary literature, a company level of success in the SMES sector is determined by its financial performance over a chosen time frame (Harash et al. 2014). According to Davis & Cobb (2010), Sabanczer (2012), Sacristán-Navarro et al. (2011), and Thrikawala (2011), performance can also be described as the achievement of specific business objectives judged against known criteria, completeness, and cost.

S. No	Author and Year	Research objective	Sample	Research Methodology	Resultsofthestudy
1.	Zhou etal.,2021	Toassesshowangel investments affect the expansion of SMEs	404 angel-backed firms from2002-2013	Ordinary LinearSquare Regression	After initial public offerings, the risk of a stock price collapse is lower for companies backed by angel investors, showing the early influence of angel investment on their market performance.
2.	Du&Cai,2020	To evaluate the effect of venture capital on the expansion of SMEs	40 SME's	Multivariate regression analysis	SMEs that usedventure capital investors experienced greater technological advancements and greater profitability than non-venturecapitalinvestors.VCalso hasapositiveeffectontheexpansion ofSME firms.
3.	Katoetal.,2020	To determine how venture capital financingaffectsthe performance of SMEs.	90 SMEs	Multiple regression analysis and correlation coefficient	Comparedto firms not supported by venture capital, venture capital-backed companies manifest rapid increases in revenue,profitability,andreturn on assets.
4.	Duet al.,2020	To investigate how venture capital influences the expansion of agricultural SME	40agricultural SEMs	Multivariate regression	Venture capital substantially enhances the profitability, technological innovation, and expansion potential of small and medium-sized enterprises (SMEs). The promotion of SME solvencyby venturecapitalisnot readilyapparent.

5.	Eldridgeetal., 2019	To analyze the effects of equity crowdfunding on growth prospects and innovation within small and medium-sized businesses.	230 companies	Ordinaryleast square regression	The lack of substantial impact that crowdfunding has on innovation within small firms refutestheclaimthattheadoption of crowdfundingresults in raised levels of innovation. However, crowdfunding does indeed influencethepotentialfor expansionofasmall company.
6.	Levratto et al. 2018	To evaluate the influence of angel investors on the performanceof companies	432 companies	Ordinaryleast square regression	Angel-backed companies experience greater rates of employment growthcomparedto non-angel-backed companies.
7.	Schmidt et al. 2018	To determine the process by which angel investors influence the value of the companies in which they place their investments.		Harman's single-factor test	An angel investor should preferably use a means-oriented approach while supporting an investeefirmduringthefirstpost-investmentperiod.Thisfacilitates the initialization procedure.
8.	Dalicetal.,2017	To ascertain the functionofventure capital funds in the growth of newly formed companies	106 companies from mid-January 2016 to mid-April 2016	Survey Based	Businessesthatgetfundingfrom venture capitalists (VCs)also receive various forms of help, meaning that VCs provide entrepreneurs with technical support inaddition tofunding. In this manner, businesses may expand quickly, hire people, and supporttheexpansion o ftheworldeconomy.

9.	Dutta&Folta, 2016	Toascertainhowa venture'sgrowthis affected by the value-added advantages of privateinvestors.	350 ventures (137 angel ventures and 213 venture capitals)	Ordinaryleast square regression	Angel investors do not provide the same advantages as venture capitalistsdoforthedevelopment of ventures.
10.	Collewaert & Manigart, 2016	Tofindtheworthof companies backed by angel investors	123 angel investment rounds from 46 angel investors	Ordinaryleast square regression	Higher values are often negotiated by angel investors with more expertise, education, andhumancapitalthanbythose withlowervaluations.
11.	Huaetal.,2016	Tolookathow venture capital(VC) affects small- and medium-sized businesses' (SME) performance and innovationinChina.	2699 VC-backed and non-VC-backed firms		Venture capital (VC) investment is a useful tool for advancing the growth of SMEs. Value creation for businesses sponsored by venturecapitalistsissupportedby them.Thereis,however,noproof that internationally VC-backed companies outperform domestically VC-backed companies.
12.	Memba et al., 2012	Toascertainhow venture capital affectssmall-and medium-sized businesses(SMEs') progress	200 SMEs	Descriptive statistics	Venture capital influences the expansion of the SMEs it finances. Venture capitalistsboost the profitability of SMEs.
13.	Shane,2012	To measure the phenomenon of angel investment in entrepreneurial finance	143 businesses between 1994-2014	Regression Analysis	Angelinvestmentstotaling $10000were made on average between 2001 and 2003, with 25% of those investments going intoretailbusinessesand12.5% intopersonalservicebusinesses.

14.	Pierreetal.,2011	To ascertain the extent to which venture capitalists (VCs) havecontributedto smallandmedium-sized enterprises (SMEs).	600 small and medium-sized manufacturing firms.	Chi-square test	There were notable disparities between VC-financed and non-VC-financed SMEs' strategic ability, with the former group clearly outperforming the latter.
15.	Dagogoet al., 2009	Toinvestigatethe value-added advantages that SMEs get from venturecapitalists	120SMEs(60 VC-backed and60non-VC-backed)	T-test,F-test and Regression	SMEs with venture capital funding did much better than those without. The social impact ofVC-backedSMEsishigher thanthat ofnon-VC companies.
16.	Macht & Robinson,2009	To look at how angel financing affects the businesses they back.	9directorsof angel-backed businesses	Qualitative Techniques	Business angels help investee businesses overcome funding difficulties and make them more attractivetopotentialequity investors.
17.	Smolarskietal., 2009	Toinvestigatethe effectsofequity-based venture financingtechniques onthe performance and internationalization ofSMEs	36 firms	Descriptive statisticsand PROBIT regressions	The chance of the company exporting and achieving performance,bothriseswith venture capital.
18.	Sorheim,2005	To recognize the additionalvaluethat business angels provide	20 business anglesthrough a structured interview	Qualitative techniques	Angel investments set up a company's financial future. The assistance of angel investors lowersthe"liabilityofnewness."

19.	Madill et al., 2004	To investigate the existence of angel investorsforfurther SME financing	766 listed firms	Logistic regression	Institutional venture capital funding is pursued by angel-backed companies significantly more often than comparable companies thathavenotobtained angel financing.
20.	Maula & Murray,2002	Toassessthe effectiveness of businessesprovided with corporate venture capital.	325 venture capital-backed companies	Ordinaryleast square regression	Companies supported by corporate venture capital are valued at higher valuations compared to those backed by independent venture capitalists andindustry-leadingcorporate investors.

3. Methodology

This paper focuses on the role of angel investment in affecting SMES firm performance. Secondary sources are used to gather the study's data. The study reviewed the research paper taken from Google Scholar. The main goal of this study is to review research articles about the role of angel investing in India. This examination of the literature will help in understanding how angel investors affect the success of SMES businesses. Data for this conceptual study was gathered through publications, articles, journals, reports, and papers and websites.

4. Analysis and Findings

Business angels are crucial in this situation, particularly for the growth of start-ups and SMEs. A business angel is a private individual who directly invests a portion of his or her finances in start-ups and developing unlisted enterprises. They are typically high-net-worth individuals with prior business experience, skills, and a powerful network. A business angel may choose to invest alone or with several angels in a syndicate, where one angel often assumes the leadership position. According to Hellmann et al. (2020); Block et al. (2019); Cipollone and Giordani (2019); and Clercq et al. (2012), business angels provide other things besides finance such as entrepreneur contacts, business management expertise, and skills in addition to financing. The role of business angels in risk capital provision, economic expansion, and technical advancement is becoming more and more important. In addition, business angels have a bigger role in the supply of start-up and early-stage equity financing. During the years 2008 to 2015, angel deals grew on average by 124% annually. In the years 2008 to 2015, the estimated amount invested through angel transactions increased at an average annual growth rate of 205 percent, and the number of angel investors increased at an average annual growth rate of 107 percent at the same time. The growth rate of investors who are reinvesting has been 105 percent, compared to a 98 percent growth in the number of new angel investors. The amount of angel investment in Indian start-ups reached a five-year high in FY16, standing at Rs. 113.6 crores across 69 agreements, according to InnoVen Capital, a venture debt business. This represents an increase of roughly 62% in deal value and 47% in deal volume from FY15, which saw Rs 70 crore in investments across 47 deals. In total, Indian entrepreneurs raised $1.42 billionacross 307 agreements in Q1 2016, with e-commerce capturing the most deals and the highest deal value, compared to 147 deals for $1.7 billion in Q1 2015. Venture capital funds have struggled to handle a lot of small acquisitions due to a lack of funding over the past few years. They took a back step and reduced their investments in hazardous SMEs and switched to later, larger-scale investments that offered better returns. Bank lending, a traditional source of start-up and early-stage finance, is constrained and has significantly decreased since the 2008 financial crisis because of risk and processing costs (Demirguc-Kunt, Martinez Peria and Tressel, 2020; Chen, Hanson, and Stein, 2017; Casey and O'Toole, 2014). The SMES industry has seen consistent development throughout the last few years (Pawar and Sangvikar,2019). Business angels increase the likelihood of their survival and expansion by offering start-up businesses both financial support and managerial expertise. As a result, encouraging business angel investment in start-ups has the potential to significantly impact the growth of economies and governments. The industry, SMES financing, digital entrepreneurship, and regional development may get benefit from greater awareness of business angel activities or the policies and programs that are offered in various nations or regions (Zhou, Zhang, and Sha, 2021; Harrison, Bock, and Gregson, 2020). Business angels play a significant role in encouraging the substantial expansion of small enterprises, so serving as a crucial element in the whole process of economic development (Olaorea and Adetoye, 2014).

In order to promote the role and meaning of angel investors in India, the following measures are needed:

- **Increased understanding of angel investors advantages**

Given that angel investors are not well-known in my country, it is necessary to hold seminars, workshops, consulting sessions, etc., to introduce them into the curricula of faculties, and to publish academic and professional papers in which all the benefits and drawbacks of this form of financing are explicitly discussed.

- **Development of stock exchange**

If the stock market is not sufficiently developed, angel investors will not be interested in investing in new enterprises since their shares will be difficult to sell and they will not be able to earn back their investment.

Additionally, SMES ought to provide a unique service that would gather share purchase and sale prices from various dealers and reveal them to prospective investors. Later, without being connected to brokers, investors would complete their transactions through computers. For instance, these concepts underpin how NASDAQ,

Reuters, Telerate, and Bloomberg operate.

- Encouragement of wealthy individuals to become angel investors

There is a wealthy population in India. It is important to encourage those people to put some of their money into start-up small firms. A tax incentive or tax cut during the initial years of investing worked well to encourage rich people to participate in angel investing in practically all nations where angel investors are active.

- **Affirmation of angel investors from other sources of funding**

Because they are so helpful in starting new businesses, commercial banks, formal venture capital, and other diverse funds should recognize angel investors as distinct and particularly significant sources of capital. Once these businesses are "up," they will need money from these sources for later stages of expansion, earning them money from interest, provisioning, etc.

5. Conclusion

Angel investors are individual investors who have accumulated wealth and experience through their active working lives. They are willing to invest in small and medium-sized businesses to support emerging entrepreneurs and, typically, to make money. They are particularly crucial during the seed and start-up phases of the growth of small and medium-sized businesses.

The effect of angel investment resources on the expansion of SMEs was theoretically examined in this paper. Even while they individually contribute relatively small amounts of capital in the early phases of enterprise growth compared to other sources of financing, the study's findings indicate that angel investors are playing an increasingly significant role in financing many new businesses. It may be said that business angels play

a significant role in the rapid expansion of small enterprises. Over the past few years, the performance of the SMES sector has increased steadily. We conclude that angel investments have a positive impact on the SMES sector. The literature reveals that SMEs who utilized angel investment experienced significant growth than those who did not. The literature also revealed that angel-backed companies enjoy higher valuations than those without angel investments. They not only provide financial support to the firms but their experience, and education also enhance the profitability of the company. Some studies also indicate that angel investors create a roadmap for future funding. Angel investors reduce the liability of newness and attract other private investors for investments. However, Johnson and Sohl (2012) contradict these findings when they conclude that Private equity firms with BA support do not exhibit superior performance compared to those without BA support. Some researchers also claim that in the context of venture development, angel investors do not offer the same sort of benefits that venture capitalists do.

The research also has some limitations. Firstly, we reviewed a limited literature for the concerned study that too from the Google Scholar database only. So future research can be done using more literature and from different databases. Secondly, this is a review paper that only provides an overview of the topic, future research can be done in a different way and empirically.

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