1. **Elaborate on the working of Venture Capitalist funds and crowd-funding. What are the major advantages involved with them for borrower and risks involved for lenders; also suggest how such risks can be minimized? (250 words)**

Answer:

- There are various financing options available to modern entrepreneurs, when starting a new company, such as venture capital and crowd funding. Venture capital is money that is given by risk investors to help build new start-up firms that often are considered to have both high-growth and high-risk potential.
- In exchange for their funding, venture capitalists expect a high return on their investment as well as shares of the company.
- In contrast Crowd-funding is a way of raising finance by asking a large number of people each for a small amount of money. Until recently, financing a business, project or venture involved asking a few people for large sums of money. Crowd-funding switches this idea around, using the internet to talk to thousands - if not millions - of potential funders.
- People invest simply because they believe in the cause. Rewards can be offered or Investors receive their money back with interest. This is also called peer-to-peer (p2p) lending, it allows for the lending of money while bypassing traditional banks.

Benefits of alternate sources of finance

- Entrepreneurs often turn to venture capitalists for money because their company is so new, unproven and risky that more traditional forms of financing, such as through banks and debentures, aren't readily available.
- Unlike other forms of financing where entrepreneurs are only required to pay back the loan amount plus interest, venture capital investments most commonly come in exchange for ownership shares in the company to ensure they have a say in its future direction.
- The relationship between the VC fund and beneficiary company is lengthy and engaging. Instead of working to get the loan + interest immediately, the venture capitalists work with the company for five to 10 years before any money is repaid.
- Aside from the financial backing, obtaining venture capital financing can provide a start-up or young business with a valuable source of guidance and consultation. This can help with a variety of business decisions, including financial management and human resource management.
- In a number of critical areas, including legal, tax and personnel matters, a VC firm can provide active support, all the more important at a key stage in the growth of a young company. Faster growth and greater success are two potential key benefits.

Risks with VC funds

- Investing in start-ups is a risky business. The high failure rate of venture capital companies parallels the high failure rate for new businesses themselves.

- The failure rate of venture capital companies is between 20% and 90%. However, the risks associated with venture capital firms are often off-set by the successful few investments that drive profits.
- Risk of fraud e.g. funds may be used for different purpose than what was initially disclosed.

Risks with Crowd-funding

- A lot of donors are just average people. They are not subject matter experts and might be ignorant on the processes that go into various projects.
- Since the companies are small and private, or probably not even registered, then audited company accounts as well as business plans may not be available to allow them to find out more about the company.
- Crowd funders give small dollar amounts and thus are not particularly bothered by the returns, they write it off as soon as they give the money
- There is a free-rider problem where everyone thinks that others have carried out due diligence whilst in essence no one has.

Minimization of Risks

- Risks can be reduced by extending regulations to these areas and settling the accountability norms to prevent frauds.
- SEBI has already created database of registered VC funds, which get technical support from SEBI.
- SEBI (Venture Capital Funds) Regulations ("VCF Regulations") were framed in 1996 to encourage funding by entrepreneurs' early-stage companies in India. This also provided an official and regulatory framework for this largely unorganized market.
- SEBI is currently in the process of establishing regulations on crowdfunding. Once this picks up, it will be a boon to the SME/early-stage startups to raise funds from small-time investors. Similarly, it would also provide an accountability mechanism for the borrowers, particularly in case of equity crowdfunding.
- Risk of fraud is primary reason as why SEBI wants to regulate crowdfunding as there is possibility of genuine websites being used by fraudsters claiming to be promoters of projects or of false websites being established, simply to defraud the investors or to entice individuals to provide credit card details etc. Thus, there is a risk of misuse as well as cyber-security and/or identity theft.

PRACTICE QUESTIONS

Answer the following Questions

1. What do you understand by social audit? Discuss the impediments to institutionalizing social audits in India. Also, highlight the recent steps being taken by the legislative and the judiciary in this direction. (250 words)
2. Briefly explain the role of deep learning neural networks in AI technology. Discuss features of Google Duplex which makes it a revolutionary technology. (250 words)