

Star Gazer Promod Haque – Managing Partner at Norwest Venture Partners

Promod has more than 15 years of experience in the venture capital industry and currently serves as managing partner at Norwest Venture Partners. He joined Norwest Venture Partners in 1990. He has been ranked as a top dealmaker on the annual Forbes Midas List for the past five years, and in 2004, Forbes named him as the #1 venture capitalist based on performance over the last decade. Promod focuses on investments in semiconductor and components, systems, software and services.

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Michael Moe: Promod, obviously you've been a well-recognized, accomplished investor and venture capitalist for a long time, what specifically attracts you to the Indian opportunity?

Promod Haque: I think there are several different opportunities that are emerging there, they are in different phases. Some of them obviously are in the past, you've already seen the rise of the IT services firms and obviously they've done very well, and they're maturing. I think the opportunities that I see and that our firm sees in India today, first of all is in what we call the consumer internet space. I think that's fueled by two or three different drivers. First of all, the business models have been proven to do well in the US, in Europe, and to some extent in Korea and Japan, in the developed countries, so to speak.

For three years or so, those business models have also started brewing in different stages in China. So now you say, the consumer internet boom, and those models have been successfully transplanted into China, so now let's look at India, and that's when you start to look at some trends within the Indian economy itself. You've got a fairly significant middle class population that in recent years has acquired a significant amount of purchasing power, fueled as a result of the idea revolution that's taken place in India, you've got Broadband penetration that is really starting to take off, and is where China was five years ago. The same is true with wireless penetration, wireless and mobile penetration is increasing significantly to the tune of about 40 million subscribers a year, and currently at the same level as where China was about four years ago. You look at a lot of those drivers and vectors and come to the conclusion that the consumer internet market is really poised for tremendous growth in India, so that's an area where we're funding companies, in fact we just funded our very first online travel portal. We brought in two corporate partners in India, one of them being PV18 because of the coverage they have, the viewers that they have, it's an affiliate of NBC, and the other partner that we brought into the deal is Reliance Capital that has tremendous presence in terms of their web growth and kiosks and outlets in 5,000 cities, so we felt that even though internet penetration is increasing, wireless penetration is increasing, travel bookings need to be done in a multi-channel fashion. That's one of the interesting things about the Indian market today in that you can't be just an online business. You have to have an online business obviously, but you also need other channels to complement your online business, you need some physical presence, and obviously a start-up company can't do that, so partnering with some established players makes a lot of sense.

I think the whole consumer internet space, and I'm speaking of that pretty broadly, that alternate XXX will be called value-added services in the mobile space. We believe that's a tremendous market and it's proven pretty lively in Europe and to some extent, again in Japan and Korea that are way ahead of wireless adoption than even the US. We see the same trends taking place in India. We combine all of that into what I call consumer internet services.

MM: I believe you've been a proponent of joint ventures or collaboration between the US and India, hybrid business models. What do you see in this area?

PH: What I just talked about, the consumer internet, that's not a hybrid model. That's us going to the local market, and it's literally a business that's totally established in India and there's no other presence other than India that's looking at the local market.

I think the other segment that we see growing and where we have started to make investments is the whole availability of technical talent at a very reasonable cost. The trend that started with IT services is now into outsourced product development services. You've got lots of companies out there that are providing outsourced product development services to lots of companies, including really large ones like

IBM, Microsoft, Cisco, Oracle, and so on. So one of our portfolio companies that we just invested in is a company that does that, provides product development services. That's another interesting segment, we're pretty active in that.

The third segment, which is still in its infancy, I believe, is this whole space of what I call a product company. While India has been very successful in producing IT services companies, there really aren't many significant product companies that have come out of there. There are a few, iFlex that was bought by Oracle, and Hughes Software that was acquired by Flextronics. There are a few others, but what we see happening as a result of what's happened with a lot of this outsourcing that's happening in the product development space, not in the IT services space, but in the product development services space, we see a model developing that's very akin to what happened in Israel. There are tremendous parallels there between what happened in Israel 10-15 years ago and what's happening in India now. So if you look at the Israel story, a lot of NMCs went there, started to utilize a tremendous amount of Israeli technical talent, you saw Intel go there, you saw IBM go there, and lots of other firms.

That led to tremendous proliferation of entrepreneurs spinning out of those product development schools, so to speak, or those labs, those entities, and then fueling the start-up scene there. As you know, today, next to the US, in number of companies listed on NASDAQ, Canada is number two and then number three is Israel. It's just amazing. So we see some parallels to what happened to Israel and what's happening in Israel.

So our approach so far has been to do what we call hybrid companies or cross-border companies. The whole premise is that if you're doing product development in areas that are disruptive or technologies that are disruptive, the early adopters of those technologies are still in the US and Europe, largely US, and so therefore it's very important if you're starting a product company to have your initial conceptual folks here doing market validation with early adopters of technology, customers, and then maybe even doing some architectural work here, and then doing the bulk of the product development for cost reasons and availability of talent reasons, in India. So we've got about 18-20 companies in our portfolio that have used that model and have been very successful. In a VC backed company that's very important because capital efficiency is driving that. More and more VC backed companies are doing that, not just in India, some are doing it in China, some are using development centers in Eastern Europe and so on, and what's driving it is capital efficiency.

What's particularly interesting about India is the tremendous number of people available, even though competition is eating up and it's hard to find these people, but there's still quite a large number of these folks, so what we see happening, again sort of based on the Israel model, is a lot of hybrid companies getting created, and what's happening is it's sort of centered around entrepreneurs that start a company here, maybe one of the founders is an Indian and he's going back for various reasons, and we say, hey this is perfect, let's start building around him in India. I think what we're going to see in the future is as Indian enterprises start to adopt technology, and they are, they're getting very aggressive because they need to differentiate themselves against new entrants as markets open up and to banks getting very aggressive and very prolific users of technology. So as early adopters of technology as customers start to surface there, hybrid models won't be necessary. In other words, you'll have product management people, and as more and more Indians are returning back, and some of them are marketeers and product management folks that have customer relationships and customer relations skills, as more and more of these folks return and as the Indian enterprises start to adopt technology earlier than they usually have been, you are going to start to see companies getting germinated there and getting validation of their concepts with local customers, the early adopters, and being able to build product companies that have global scope.

A little bit of what's happening in China, companies like WaWe and DE, that are pretty well-known companies today in the networking space, competing very effectively with Cisco and 3Com and so on, very similar model. They took off as a result of some of the Chinese service providers buying their gear, and now they're out there challenging American vendors.

For that reason, that third segment, which is global product companies, software, hardware, and so on, is also of interest to us. So those are the three distinct areas that we're seeing that we're investing in right now.

MM: How often do you get to India? How many times a year and how long do you spend when you get there?

PH: I usually go there every two months, and I usually try to spend anywhere between 7-10 days there. The reason for that is I'm on the boards of some companies and then sort of being abreast of what's going on, plus as I've said, some of our hybrid companies have presence there, so helping them recruit and keeping tabs on those folks sort of necessitates that I be there. At some point we're going to add some local folks there, we're going to hire so we can be more active in the investments that we're making.

MM: So as you look at what are some of the issues in investing in India, or some of the impediments to innovation, what are some of the biggest issues?

PH: Let me again speak about the three distinct entities that I talked about, but some of these comments in general apply to all of them. I think management teams are a challenge, there's a cultural issue there, and that is if you look at the role models of companies that have been successful there, there's a lot of family-owned businesses, and another way to say that, you know the VC scene and therefore the whole VC ecosystem is very rudimentary there, still in it's infancy, so it's sort of difficult therefore to find entrepreneurs that have been successful before, especially in VC backed companies that understand the value of VCs, that understand that gee, if you bring in a VC, or if you start a company with venture capitalists, you as the entrepreneur isn't going to sit there with 70% ownership in the company, that you are going to have to buy into the principle that says, I'd rather own a smaller piece of a company that can become very large, versus trying to control it and not having the capital available. I think that's a common challenge. Expectation and ownership, the ecosystem isn't trained, there aren't enough people that have gone through the process, there's a lot of education that's required. There's not a lot of lawyers out there for example that understand the venture capital process.

To some extent, I think what's also happened is that the venture capital scene there, venture capital is relatively new to India in the form that we use venture capital here. It sort of really took off in 1999-2000, and then just fell flat when we went through the XXXX session, so a lot of the dot coms crashed, and some of those VCs went out of business, or they had to exit the business, or changed their business models and went into buyouts, and so on, so there's a scarcity of early stage money readily available in the country. That created a perspective that entrepreneurs have about VCs and so that whole impression that I think was half-baked and incorrect, that needs to change, so that's one impediment today. It's hard to find good, solid management teams because they're all developing, they're all in their infancy. That's across the board in all three sectors that I talked about.

I think with respect to the last sector, the product company, products with a global market, I think one of the challenges is that you don't have enough people with product management expertise and the reason for that is the markets are all in the US, at least the disruptive technologies, so you end up in a situation where you don't have enough product management people, there's not enough people that understand customers and that have intimacy with customers because they're all over here. Lack of product management skills today make it difficult to fund product companies there, which is why we're using the hybrid model, because we keep the CEO here, we keep the VP of marketing here, we keep the VP of sales here, because this is where the markets are, so we keep the product management people here as well, and then do all the development back there. I think that's going to change as the Indian enterprises start to become more avid users of technology, and early users of technology and early adopters. So that's a third impediment.

MM: In terms of regions of investment opportunity or where you see particularly interesting things going on, obviously Bangalore is the most famous, but is it all over India, or is it more concentrated like a Silicon Valley? Better question, is Bangalore the equivalent of Silicon Valley, or do you see innovation opportunity throughout?

PH: I think you would look at Bangalore today and say it's probably the closest proxy to Silicon Valley within India. There's other centers as well, but in terms of concentration that's probably the largest concentration of engineering talent, NMCs with Indian headquarters there, lots of engineers available there. You've got pretty interesting innovation going on, but like I said, it's still in its infancy because the challenge they have is they're not close to the customers.

MM: If you were to give some advice to what I call the stars of tomorrow today in India, what do you think the key thing to be looking for is? You talked about the three areas that you're focused on, but if you could sum it up into one thing to focus in terms of where these stars of tomorrow will be, or how to identify and invest in them, what is the key thing, if there is such a thing? If there's a takeaway for identifying and

investing in what I call the Stars of Tomorrow, Today in India, what's the one takeaway that an investor should be focused on?

PH: Again, I'm talking about private investing, so I can't speak about the public markets and so on, they're pretty vibrant and at an all-time high. But when it comes to investing in earlier stage or even mid-stage companies that are private, I think there are lots of challenges. There's lots of companies there. I think it takes a certain amount of discernment to understand the psyche of the entrepreneur, not to get trapped in an entrepreneur that can't think big, or that has a family-run business, his mother's in the business, his brother's in the business, and all of a sudden, you're sitting across the table from a family. Sometimes it's not very apparent that you're going to be dealing with a family. I think the thing really is discernment, understanding is this the kind of entrepreneur that can think big, and that is going to let go and surround himself with other managers that he's going to bring in that have more experience and really let go. There's a tendency for entrepreneurs there to be hold things very close to their vests, so it's a big discernment issue to try and understand the psyche of the entrepreneur, in fact I would even go so far as saying that I'd be reluctant. My first lesson would be to back an entrepreneur in India that has lived in the US and understands the ecosystem of how business is done here. It's a lot easier with those entrepreneurs that have already broken into the VC ecosystem in the US versus trying to deal with someone there that doesn't know the protocols, doesn't know the way the VC system works and you get to fund that company and all of a sudden you've got a nightmare on your hands. [end box]