Venture capital for MSMEs in India

Small Industries Development Bank of India (SIDBI)
https://smallb.sidbi.in

Venture Capital is emerging as an important source of finance for small and medium-sized firms, especially for starting the business and business expansion. An entrepreneur usually starts the business with his own funds, and those borrowed from banks. It is during expansion that they find it difficult to raise funds. SMEs have traditionally been dependent on Bank finance for expansion and working capital requirements. However, in the recent past, bankers have curtailed lending to SMEs due to the greater risk of non-performing assets (NPAs) in a downturn. Thus, even though many SMEs have profitable projects and expansion plans, they find it difficult to get finance for their projects, as bankers may not be willing to fund high risk projects.

In order to provide financial support to such entrepreneurial talent and business skills, the concept of venture capital emerged. Venture capital is a means of equity financing for rapidly-growing private companies. Finance may be required for the start-up, expansion or purchase of a company. Venture capitalists comprise of professionals in various fields. They provide funds (known as Venture Capital Fund) to these firms after carefully scrutinizing the projects. Their main aim is to earn higher returns on their investments, but their methods are different from the traditional moneylenders. They take active part in the management of the company as well as provide the expertise and qualities of a good bankers, technologists, planners and managers.

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Traditionally, Venture Capitalists in India have shied from the MSME sector. The non-corporate structure and small size of majority of MSMEs in India makes the Venture Capitalists and Private Equity Players reluctant to investing in them due to higher transaction costs and difficulties in exits out of such investments. However, the VC scenario in India is rapidly changing. Alternative funding like VC is picking up in the India, including in the MSME sector. Moreover, the VCs are expanding their reach into areas besides the traditional VC sectors like Information Technology (IT); nowadays interest in sectors like clean energy, healthcare, pharmaceuticals, retail, media, etc. is also growing.

The Small Industries Development Bank of India (SIDBI) is the main public financial institution involved in VC funding operations. SIDBI operates through wholly owned subsidiary, SIDBI Venture Capital Limited (SVCL). It co-finances state-level funds, and sometimes co-invests with private sector VCs on a case-by-case basis.

Benefits of VC over other funding methods

Venture capital has a number of advantages over other forms of finance:

- It injects long term equity finance which provides a solid capital base for future growth.
- The venture capitalist is a business partner, sharing both the risks and rewards. Venture capitalists are rewarded by business success and the capital gain.
- The venture capitalist is able to provide practical advice and assistance to the company based on past experience with other companies which were in similar situations.
- The venture capitalist also has a network of contacts in many areas that can add value to the company, such as in recruiting key personnel, providing contacts in international markets, introductions to strategic partners, and if needed co-investments with other venture capital firms when additional rounds of financing are required.

Venture capital funds in India

In India, venture capital funds (VCFs) can be categorized into the following groups:

- Promoted by the Central Government controlled development finance institutions, for example:
  - SIDBI Venture Capital Limited (SVCL)
  - IFCI Venture Capital Funds Limited (IVCF)
- Promoted by State Government controlled development finance institutions, for example:
  - Gujarat Venture Finance Limited (GVFL)
  - Kerala Venture Capital Fund Pvt Ltd.
  - Punjab Infotech Venture Fund
  - Hyderabad Information Technology Venture Enterprises Limited (HITVEL)
- Promoted by public banks, for example:
  - Canbank Venture Capital Fund
  - SBI Capital Markets Limited
- Promoted by private sector companies, for example:
  - IL&FS Trust Company Limited
  - Infinity Venture India Fund
- Overseas venture capital fund, for example:
  - Walden International Investment Group
  - SEAF India Investment & Growth Fund
  - BTS India Private Equity Fund Limited

Private sector funding for SMEs in Malaysia

SME Corporation Malaysia

http://www.smeinfo.com.my

Banking institutions

SMEs can approach Commercial Banks and Islamic Banks for funding, depending on their needs.

Conventional as well as Islamic financing products are available for a wide range of needs. These would cover items like term loans, leasing and industrial hire-purchase for asset acquisitions or business expansions; overdrafts, revolving credit facilities and factoring for working capital; letters of credit (LC), trust receipts, banker's acceptance (BA) and Export Credit Refinancing (ECR) for trade financing; and bank guarantee as well as shipping guarantee facilities.

Development financial institutions

Aside from commercial banks and Islamic banks, there are also Government-backed Development Financial Institutions (DFIs) which can provide SME financing.

Development Financial Institutions (DFIs):

(governed by the Development Financial Institutions Act 2002)

- Bank Perusahaan Kecil & Sederhana Malaysia Berhad (SME Bank)
- Bank Pembangunan Malaysia Berhad
- Export-Import Bank of Malaysia Berhad
- Bank Kerjasama Rakyat Malaysia Berhad
- Bank Pertanian Malaysia
- Bank Simpanan Nasional

Other DFIs:

- Malaysian Industrial Development Finance Berhad
- Credit Guarantee Corporation Malaysia Berhad (CGC)

Leasing and factoring companies

Leasing

SMEs in need of expensive machinery need not only rely on hire-purchase arrangements as a means to financing their business.

They can also choose to lease equipment, which would give them use of equipment owned by a leasing company, in return for regular lease payments over a specific period of time.

This allows SMEs use of vital equipment without ever having to buy it.

Any moveable asset can be leased. This includes office equipment, vehicles, industrial and manufacturing equipment, as well as construction and heavy equipment.

Features

- A facility which allows SMEs to lease equipment from financial institutions without having to purchase the equipment.
- There are 2 types of leasing facilities available:
    1. *Operating Lease.*
       Ownership is held by the financial institutions.
    2. *Finance Lease.*
       Ownership is held by the financial institutions. However, the lessee has the option to purchase the asset at the end of the tenure.

Benefits

- Facilitate management of funds, as leasing instalments amount is predetermined.
- For an operating lease, maintenance cost is borne by the lessor (financial institution).
- Instalments paid for leasing are eligible for full tax relief.

Factoring

SMEs can also choose to pledge their future income in order to obtain working capital. Factoring companies specialise in buying debt owed to a business, or account receivables, at a discounted price. If this happens, the factoring company will take over collection of the debt, while the company selling the debt receives money for a debt earlier, and up front.

- Malaysian Industrial Development Finance Berhad
- ORIX Leasing Malaysia Berhad

Venture capital companies

SMEs in need of capital injections might also look to venture capital companies. Venture capitalists willing to take a stake in a business will provide capital, usually in exchange for a minority stake in the company concerned.

Businesses with expansion and the potential for and eventual listing on the stock exchange are favoured targets of venture capitalists. The money is often provided for long-term expansion projects undertaken by the company concerned.