Finding funding

Although Asia is perceived to be a region awash with capital, the cost of bank financing is quite high. As a result, corporates and SMEs are exploring alternative sources of funding, from venture capitalists, private equity and angel investments through to trade finance and bond markets.

Khalid Quadir is a Bangladesh entrepreneur who was educated in the West and worked on Wall Street. He helped set up Grameenphone, Bangladesh’s largest mobile phone operator, which partnered with the well-known microfinance organisation, Grameen Bank. His latest venture is about providing Bangladesh companies with an alternative means of financing to help grow their businesses.

Quadir estimates that there are approximately 50 private commercial banks in Bangladesh. Large global banks like Citi and HSBC also have a presence, but he says the cost of bank financing is quite high – anywhere from 16% to 18%. “If you are a strong performing company growing between 15% and 20% a year, it is possible to operate at such a high financing cost, but in some ways you are working for the bank,” he says.

While most companies in Bangladesh rely on funds provided by friends and family, Quadir says there is only so far they can get using this form of financing. In a bid to provide Bangladesh companies with an alternative, Quadir in partnership with Patrik Brummer, the founder and chairman of Brummer & Partners (the largest hedge fund group in the Nordic region), set up Bangladesh’s first private equity fund – the $88m Frontier Fund. It will make long-term investments in privately-owned family firms in Bangladesh that are looking to expand. Its equity investments range between $5m and $15m and target company’s in the country’s export, retail, manufacturing, agriculture, health, education, IT and services sectors.

Family-owned companies in Bangladesh were initially reluctant to relinquish equity to an outsider, but Quadir says a new generation of Asian entrepreneurs are becoming more open to alternative forms of financing.

Awash with capital

The picture that Quadir paints of companies in Bangladesh suggests somewhat of a dichotomy when it comes to funding
growth in Asia. The commonly-held perception is that Asia is awash with capital from outside investors, banks and other financing vehicles – and there is certainly some truth in that. According to EuroFinance’s Treasury Verdict Asia 2013, more than 70% of Asian treasurers reported that longer-term funding was not a major issue and they did not foresee any problems accessing it in future.

“Companies have access to myriad sources of capital,” says an Account Officer with The CID Group, which is Taiwan’s largest venture capital (VC) firm. In addition to traditional bank loans, he says it is important to not overlook the ‘gray market’ and ‘black market’ loans. Although the cost of ‘gray’ loans can be as high as 10% a month, according to some reports, the Account Officer says these loans are trending up and serve a critical role for many local entrepreneurs. “Also, many entrepreneurs are funded by their family and friends,” he continues. “For factories and corporate suppliers, these tend to be the most utilised avenues of capital.”

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Steven Beck, Asian Development Bank (ADB)

VC and angel investment is also growing in Asia. For small and medium-sized enterprises (SMEs) with intellectual property (IP), the Account Officer says there is ample opportunity to raise venture investment. Tom Russell, co-founder of SeedAsia, one of the first Asian-based crowd-funding platforms to offer international investment opportunities in Chinese and South-East Asian technology start-ups, says is not too difficult for Chinese start-ups to obtain financing as there are a lot of VCs and private equity (PE) firms. Crowd-funding platforms like SeedAsia are relatively new to Asia though, and Russell says there are some cultural barriers to overcome. He says if they tried to introduce the platform five years ago, it probably wouldn’t have taken off. “Thanks to the global financial crisis, people now want to have more say in what they do with their money and don’t want to rely solely on banks,” he says.

The Asian dichotomy

But the funding picture starts to look a little less rosy for smaller companies that are not creditworthy, have no IP or other kinds of assets. Obtaining bank financing is hard for many entrepreneurs, says the Account Officer at The CID Group, as banks are used to lending against real estate assets. “For software or technology companies, it can be hard to get a loan. And if you are an Asian entrepreneur without connections, IP or real estate assets to securitise debt, they are often forced to grow organically.”

Outside of Singapore, Hong Kong and possibly Japan, unsecured lending is relatively scarce (most loans tend to be secured) and smaller companies tend to be rather constrained in their ability to borrow from banks, says John Chen, Treasury Director Asia Pacific at Honeywell. “These companies typically do not have access to the debt markets either.” The most common form of funding, says Chen, is through compression of collection and extension of payment terms. But as Asian businessmen are not necessarily open to disclosing their sources of funding, gaining an accurate assessment of their sources can be difficult.

Plugging the trade finance gap

“There are two faces of Asia,” says Steven Beck, Head of Trade Finance, Private Sector Operations Department, Asian Development Bank (ADB). “There is all the exuberance of high growth rates, but who in Asia is benefiting from that? Then there is the other face of Asia that has yet to reap the benefits – countries such as Bangladesh and Cambodia, which are very different from coastal cities in China and parts of India.”

Beck says there is a clear link between the provision of trade finance, economic growth and jobs. But ADB’s trade finance survey of 147 banks and more than 500 companies in 4Q12 found that banks rejected a substantial percentage of requests to finance imports and exports. This meant that $1.6 trillion of demand for global trade finance was unmet, according to the ADB, with $425 billion not realised in developing Asia.

The ADB’s Trade Finance Programme (TFP) supports trade by assuming risk in 18 developing markets in Asia. Last year alone, Beck says it provided $4 billion in financing and more than 75% of its portfolio supported transactions involving SMEs. “If we didn’t support a lot of these transactions they probably wouldn’t end up getting done,” says Beck, “and as a result, there would be a lost opportunity to create more economic growth and jobs. This is the bread and butter of the global economy but it is often overlooked.”

Beck says the banks have finite amounts of capital, which means they tend to focus more on core markets and clients, and typically that is not developing countries outside of the BRICs (Brazil, Russia, India and China).

Another factor aggravating trade finance support is more stringent capital requirements under Basel III. Banks surveyed by the ADB indicated that they would reduce support to trade finance by approximately 13% if Basel III was fully implemented. Since the survey was concluded, the Basel Committee announced more lenient liquidity requirements, but it is still expected to have a negative impact.

Standard Chartered Global Research estimates that Basel III and European bank deleveraging will have a profound impact on the Asia ex-Japan (AXJ) corporate financing landscape. It predicts a $66 billion equity shortfall for the AXJ banking system over the next five years, with India’s banking sector being the most capital-constrained. Over the next five years, it says there will be a cumulative financing gap for Asian corporates of around $340 billion.

The rise of Asia’s bond markets

As bank lending decreases, the hope is that local bond markets will help plug the corporate financing gap. In light of Basel III and European bank deleveraging, Standard Chartered estimates that there will be a tripling in size of the AXJ corporate bond market to more than $10 trillion by 2017 from just $3.3 trillion today – a compounded annual growth rate (CAGR) of 21%. “Basel III has meant generally that lending has come down from the banks, so a lot of borrowers have turned to the bond market,” says Henrik Raber, Global Head of Debt Capital Markets at Standard Chartered. “Companies want to diversify their funding base, and the opportunities are quite attractive in terms of locking in longer-dated fixed funding.”

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According to the ADB’s Asian Bond Monitor for 1Q13, emerging East Asian bond issuance expanded 12.1% year-on-year to $6.7 trillion at the end of March 2013, driven by double-digit growth in corporate bonds (19.5% year-on-year). Indonesia had the fastest growing corporate bond market in the region during the first quarter, expanding 27% year-on-year to $20 billion, followed by the People’s Republic of China (PRC), which had the region’s largest corporate bond market at $1.1 trillion, up 25% year-on-year. “Asian economies are growing fast and investors are interested in having exposure to currencies in the region – it is not seen as risky anymore,” says Thiam Hee Ng, Senior Economist with the ADB’s Office of Regional Economic Integration.

As a result of quantitative easing, the rise in US dollar liquidity is also spurring higher levels of US-dollar bond issuance by Asian companies. “Chinese companies are issuing US dollar bonds, even though their revenues are not in dollars, and then swapping the proceeds back into renminbi (RMB),” says Ng. By 2030, Standard Chartered forecasts the Asian bond markets could be larger than the US.

Asian bond markets are far from homogenous however, and different regulatory environments in each market mean issuance is far from straightforward. “While Singapore, Hong Kong and the dim sum bond markets are akin to eurobond markets, if you move into Thai baht, foreign issuers need to get permission to apply,” Raber explains. Issuing bonds that can be marketed to investors regionally is also difficult, says Ng, as there is no unified regional bond market.

Financing the supply chain

For SMEs that need a steady stream of financing in order to grow, issuing bonds may be too costly and time-consuming. Another option that is gaining ground in Asia is financing linked to trade flows between buyers and suppliers.

Since 2010, Sheung Li Fung Ltd., a Chinese garment manufacturer, has supplied Perry Ellis, a US international clothing company, using GT Nexus’s electronic trading platform. The platform automates the exchange of trade documents and information between suppliers in Asia and large buyers in the West. It also supports a range of financing options for suppliers. One option, which Sheung Li Fung uses, is the Coface Early Payment Programme, which provides payment protection services that reduce the risk of non-payment.

With the recent introduction of the International Finance Corporation’s (IFC) Global Trade Supplier Finance (GTSF) programme, which is integrated with the GT Nexus platform, Sheung Li Fung used the online financing service for two recent transactions with Perry Ellis. “The online financing service is much faster and easier when compared to factoring services with local banks,” says Kelly Lee, Accounting Manager, Sheung Li Fung. She is now able to get capital within one week after approval from the buyer and no paperwork is needed for the application. “Our ambition at GT Nexus is to democratise access to capital by connecting everyone in a cloud-based network,” explains Kurt Cavano, Chief Strategy Officer. “By bringing the buyer and supplier together, we can leverage the buyer’s good credit so the supplier can get immediate access to capital.”

Cavano says the financing GT Nexus provides is much cheaper than what companies could obtain normally. “More than 10,000 SMEs worldwide use our platform, 70% of which are in Asia,” he says, “and a third of them are taking financial services.” RTS Financial, a commercial financing company in Kansas City Indianapolis, uses the GT Nexus platform to provide factoring for companies in countries such as Vietnam, Bangladesh and China. “We have many clients in Asia that have traditional banking relationships because, even if they have bank financing, there is a limit to how much they can obtain,” says Justin Goheen, Director of Business Development at RTS Financial. “In some cases, we replace traditional forms of bank financing. As long as the invoice and the receivables are good, we can provide financing.”

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Account Officer, The CID Group

In those countries where there is more competition and options for non-bank financing, Eugene Buckley, Vice President and General Manager Asia Pacific at PrimeRevenue, a web-based supply chain financing (SCF) platform, says companies are having to look at the best possible financing structures to keep pace with the competition. “There needs to be a greater understanding of the importance of supply chains,” he says. “Often companies in these markets are scraping together expensive sources of capital, but by participating in SCF programmes companies can obtain financing at rates they could only dream of if they were to go to their banks.”

SCF, however, is still a relatively new concept in Asia. “Most SCF programmes in the past were initiated by companies in the US or Europe that buy from companies in Asia,” explains Chetan Talwar, Head of Corporate Trade Advisory and Solution Delivery, Asia Pacific, J.P. Morgan Treasury Services. Atlas Copco, an industrial group, recently rolled out a SCF programme to strategic suppliers in three Asian markets: China, India and Japan. “We have many production companies in China (more than 15), as well as India and some in Japan,” says Audrey Deng, Head of Group Treasury, Asia Pacific at Atlas Copco. “They are very important to us and some of our suppliers can benefit from our scale and credit strength. Even if there are some existing funding channels from banks, SCF gives them more immediate access to funds.”

Atlas Copco uses its credit strength to help long-standing suppliers gain access to more affordable financing. “We don’t want money stuck in working capital,” says Deng. “More and more treasurers are becoming interested in this.”

J.P. Morgan’s Talwar says a SCF programme is linked to sales and is a much cheaper source of liquidity, but it can take time to get off the ground. He says a typical programme can be up and running in 12 months, and in certain jurisdictions suppliers may not sign up immediately. “It is not something that is applicable to all industries,” he says. “You need to have strong buyer/supplier relationships.”

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