Role of non deposit taking lenders in SME Finance and SCF

Lee Kheng Leong
HPDLendscape
khengleong.lee@hpdlendscape.com
Survey by ADB on financing SME

- 20 countries surveyed – Central Asia, East Asia, South Asia, South East Asia and the Pacific
- SME accounted for 90% of enterprises
- Employed 62% of labor force
- Formed 42% of GDP (2015)
- SME has difficulties in accessing to Finance as the financing in many countries are dominated by banks
SME needs support from NBFI in SCF

- Post Pandemic – SME needs to get financing beyond government support
- Problems in getting financing as most financing requires security
- According to IFC – There is a APAC SMEs Financing Gap of US 2.4 trillion
- According to ICC survey 50% of the world trade will be under open account
- Receivable offers the best security as it forms more than 50% of SME assets
- SCF which covers, factoring, receivable financing and reverse factoring offers the best form of financing against receivable

More than 50% of trade will be in OA under V shape
APAC MSME financing Gap US2.4 trillion

Figure 12:
BCG Trade Finance Model, estimated share of documentary trade vs. open account trade, 2011-2028
NBFI will therefore play an important role in APAC economies
Bank

◆ A bank is a financial institution that accepts deposits from the public and create demand deposit while simultaneously making loans

◆ Due to the importance of banks in the financial stability of a country, most jurisdictions exercise a high degree of regulations over banks.

◆ Also regulated by international banking regulatory agency

◆ Bank has a fiduciary duty

Non bank financial institution

◆ NBFI is a financial institution that does not have a full banking license or is not supervise by national or international banking regulatory agency

◆ More flexible in financing than bank

Wikipedia
Types of NBFI

- Factoring company
- SCF company
- Leasing company
- Pawn shop
- Finance company
- Micro finance company
- Fintech company
NBFI is a growing industry in Asia

- CFEC- China Factoring Expert Committee
- Many regional factoring association in China
- Indonesia Financial Services Association
- Asian Financial Services Association
- Indian Factoring Association
- Malaysian Factors Association
- Malaysian Finance Association
- Hire purchase, Finance and Leasing association of Singapore
- Debtor and Invoice Finance Association of Australia and New Zealand
Receivable finance company can be very large

- Scottish Pacific – Australia
- Hong Leong Finance – Singapore
- Orix Group – Japan
- Hitachi Capital – Japan
- Bibby Financial Services
- IFS Capital
Factoring credit policies are different from bank

- Based on the quality of the receivable
  - Are the receivable factorable?
  - Are the debtors acceptable?
# Factor can give higher financing than bank for receivable financing

<table>
<thead>
<tr>
<th><strong>Borrower credit standing</strong></th>
<th><strong>Bank</strong></th>
<th><strong>Factor</strong></th>
</tr>
</thead>
<tbody>
<tr>
<td>$500,000</td>
<td><strong>Loan amount:</strong> $500,000</td>
<td><strong>Upto $1.6 million or 80% of receivable outstanding</strong></td>
</tr>
<tr>
<td><strong>Receivable outstanding</strong></td>
<td><strong>Amount static until the next review</strong></td>
<td><strong>Amount of financing grows with sales</strong></td>
</tr>
<tr>
<td>$2 million</td>
<td></td>
<td><strong>The more the SME sells the more financing it can get</strong></td>
</tr>
<tr>
<td></td>
<td></td>
<td><strong>Factoring limit is dynamic</strong></td>
</tr>
</tbody>
</table>
Bank’s credit policy vs factoring company’s credit policy

- Bank - company must be viable at least for one year
- Factoring company – company may not last for more than 6 months
- Why?
- Because the company may not last for more than 6 months, the factoring company will have to ensure that the debts are collectable as such factoring company will
  - Ensure that the debts are factorable
  - Buyers are good
  - Strict on compliance to documentation
  - Risk analytics to detect fraud and negative trend
Banks also play an important role in supporting NBFI

- Funding the NBFI
- Re factoring
- Ping Ann Factoring cloud
Funding Factoring company via factoring cloud

Commercial factors use Ping An Bank factoring cloud

Ping An Bank provides financing to the commercial factors

Advantages to bank
- To reach out to SME via factoring company
- Less manpower
- Less risk

Advantages to Factoring company
- Access to state of art factoring software at low cost
- Access to funds from bank

Advantages to SME
- Access to financing
Direct bank factoring vs through factoring company

- Direct factoring
  - 500 clients
  - 10 relationship managers
  - 50 operation staff

- Via factoring company
  - 1,000 clients
  - 2 relationship managers
  - 5 operation staff
  - 10 factors
    - 100 clients
Barriers to entries for NPFI to go into factoring and SCF

- Barriers
  - Lack of factoring/SCF platform
  - High cost in factoring/SCF platform
  - Lack of experience

- No more barriers to entry
  - State of art technology is available
  - No heavy investment cost
  - Low cost at monthly rental based on the number of concurrent users
  - Plug and play system
  - Risk analytics
  - Leapfrog into the new technology
  - Training provided by
    - International Factors Association
    - FCI
NBFI is an essential part of the financial ecosystem

- NBFI play an important role in financing SME as many SME are unable to comply with the credit policies of the banks.
- When the SMEs are small, they will use NBFI.
- As they become bigger and their financial standing become acceptable to the bank, they will move to the bank.