Section 2
SME Development Policies and Programmes

Chapter SIX

Access to Finance

Chapter SIX | Access to **Finance**

"ENTREPRENEURSHIP DRIVING SMEs"

Malaysia's SME sector contributes 38.3% to GDP and provides employment for over seven million people. In view of the sector's crucial role in economic development, the Government has, over the years, set in place an ecosystem that facilitates access to a comprehensive range of funding options from public and private institutions to ensure the sustainability of SMEs, a more inclusive financial landscape as well as the creation of a sound credit culture. Measures which had been introduced for such purposes had brought about a SME financial ecosystem that offers a comprehensive array of financing and development facilities with financial institutions, avenues for information, advice and redress as well as management and outreach programmes and even debt resolution.

Financial institutions are the backbone of funding for SMEs, accounting for about 97.0% of total lending to the segment. Bank lending to SMEs is complemented by Bank Negara Malaysia (BNM), other Government agencies and development financial institutions in the form of schemes and programmes. The current financial and non-financial facilities cover a wide array of options to meet the needs of SMEs at various stages of their business cycle, including for start-ups, expansion and export.

> Financial institutions are the backbone of funding for SMEs, accounting for about 97.0% of total lending to the segment. Bank lending to SMEs is complemented by BNM, Government agencies and development financial institutions in the form of schemes and programmes.

Priorities in the existing financing policy including encouraging greater innovation by financial institutions, enhancing efficiency in the financing processes, provision of credit enhancement products and strengthening financial management capabilities of SMEs, continue to remain relevant and supportive of SME growth in 2018. A key focus was on enhancing and developing a holistic SME financing ecosystem which include addressing information asymmetry and market imperfections, improvement in credit information and guarantees, specialised funds, advisory services as well as redress and debt resolution mechanisms.

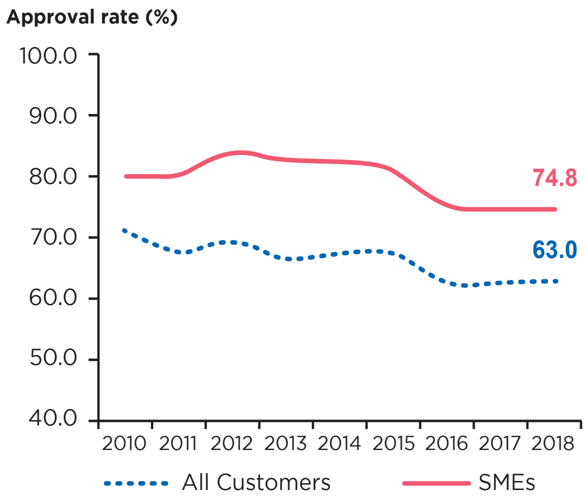
To better understand SME financing needs, BNM conducted the nationwide SME Finance Survey 2018 which commenced in the second quarter of the year, the highlights of which are presented in a box article in this chapter. Insights obtained from the Survey has enabled a more granular assessment on the needs, challenges and practices of SMEs in utilising financial services as well as policy considerations. The full Survey report is published in the 2018 Bank Negara Malaysia Financial Stability and Payment Systems Report.

FINANCIAL INSTITUTIONS ARE IMPORTANT SOURCES OF SME FINANCING

Reflecting the findings of the SME Financing Survey 2018 as well as other economic indicators, the overall demand by SMEs for financing increased at a more moderate pace during the year compared with 2017.

Financial institutions remain the dominant source of financing for SMEs, with RM307.3 billion disbursed and RM69.0 billion in new financing approved to over 123,600 SME accounts. SME financing constituted a 48.7% share of the total business financing outstanding (2010: 37.6%) while in terms of number of accounts, SMEs made up about 87.0% of total businesses. On average, three out of four SME applications were approved in 2018. Against a backdrop of moderate growth in the economy, new loans approved

Chart 6.1: Approval Rate Sustained at 75.0%



Source: Bank Negara Malaysia

and disbursed to SMEs in the first quarter of 2019 totalled RM15.7 billion (28,400 accounts) and RM75.4 billion respectively. Total financing outstanding stood at RM315.9 billion as at the end of March 2019 (RM317.7 billion at end of December 2018).

Development financial institutions (DFIs) continued to support financing to SMEs and accounted for 5.0% of the total SME financing channelled through financial institutions. Total financing outstanding of DFIs to SMEs grew by 11.7% in 2018 and stood at RM15.7 billion as at the end of March 2019.

SME FINANCING IN 2018

The Government continued to play its catalytic role in orchestrating initiatives to meet SMEs financing needs especially in the areas where gaps exist. In line with the Government's agenda for a more inclusive financial landscape, a bulk of Government's expenditure for SMEs has been dedicated to provide greater access to financing. Of the overall financial commitment for SME development in 2018, 95.1% or RM13.0 billion was spent for 44 programmes under the focus area of access to financing which benefitted 424,115 SMEs. The programmes in 2018 included:

- **Ikhtiar Financing Scheme** implemented by Amanah Ikhtiar Malaysia (AIM) has been instrumental at reducing the poverty rate in Malaysia by providing funding support to enable lower-income households to participate in viable economic activities in order to raise their economic status. The scheme includes i-Mesra, i-Srikandi and i-Wibawa. In 2018, AIM provided RM2.3 billion in financing for 359,474 beneficiaries under its schemes.

- ***Desa Lestari* Programme** under the Ministry of Rural Development has served as a community-based programme targeted at enhancing the capability of village communities to plan and implement projects that will spur wealth creation through economic activities via a co-operative platform. In 2018, an expenditure of RM10.0 million was recorded for the scheme which provided assistance to 10,000 beneficiaries.

- **TEKUN Financing Scheme** led by TEKUN Nasional under the Ministry of Entrepreneur Development has been designed to provide for SME expansions, project implementation as well as micro financing for working capital to assist small Bumiputera entrepreneurs in their existing business or new start-ups. A platform to provide information on entrepreneurship and business opportunities as well as advisory service and support has also been enabled through the programme. In 2018, RM354.0 million in expenditure was recorded for programmes under the scheme for 27,628 beneficiaries.

- **Business Accelerator Programme (BAP)** led by SME Corp. Malaysia has been assisting SMEs via an integrated approach to develop and nurture dynamic, competitive and resilient SMEs through SME Competitiveness Rating for Enhancement (SCORE), capacity building and advisory services complemented with financial support. In 2018, a total of RM69.2 million was provided to assist 838 SMEs.

- **Working Capital Guarantee Scheme – Extension** which is led by Syarikat Jaminan Pembiayaan Perniagaan Berhad (SJPP) in collaboration with the Ministry of Finance has set an aim to assist SMEs across all sectors to gain access to financing from participating financial institutions. In 2018, a total of RM2.7 billion was provided through the programme that benefitted 2,520 SMEs.

- **Syariah-Compliant SME Financing Scheme (SSFS)** has been designed to provide subsidised financing assistance to eligible Malaysian SMEs through thirteen participating Islamic financial institutions. Led by SME Corp. Malaysia, an expenditure of RM12.4 million was provided to assist 476 SMEs in 2018 whereby 2.0% of the profit rates charged by the banks were absorbed by the Government.

- **Services Sector Guarantee Scheme** implemented by SJPP in collaboration with the Ministry of Finance has been set-up to assist SMEs in the services sector to gain access to financing from participating financial institutions. In 2018, RM984.0 million was spent to assist 835 SMEs.

CREDIT GUARANTEE FOR MARGINAL BORROWERS

Credit Guarantee Corporation Malaysia Berhad (CGC) since the establishement in 1972, has evolved from a traditional guarantee provider into a financial institution that offers a wide range of financing products and services and has also entered into strategic alliances with various financial institutions to broaden its SME funding programmes. Besides guarantee services, CGC also provides direct financing products as part of its initiatives to reach out to a wider segment of under-served businesses, namely, Bumiputera Entrepreneur Project Fund-i (TPUB-i), BizMula-i, BizWanita-i and BizBina-i.

In February 2018, CGC launched Malaysia's first SME Loan/Financing referral platform known as imSME. The platform matches SMEs' financing needs with suitable products based on their business profile, credit score and financing needs. Currently there are 22 participating financial institutions offering 37 products. CGC has also set up the imSME Financial Advisory Team to assist SMEs that are unable to find matching financing products via imSME or whose applications through the platform had not been approved by financial institutions. The imSME Financial Advisory Team will conduct a diagnostic review of the cases and make recommendations for capacity building programmes or alternative financing mechanisms or platforms.

As at the end of December 2018, 405 SMEs obtained a total of RM46.9 million in financing from financial institutions and peer-to-peer (P2P) financing platforms. Another 2,515 SMEs received assistance from the Financial Advisory Team. As at the end of September 2019, 1,417 SMEs have obtained RM137.0 million in financing through imSME.

SKIM PEMBIAYAAN MIKRO FOR MICROENTERPRISES

Financing for microenterprises, which accounts for about 77.0% of total establishment borrowing, has risen consistently over the years. Its share of the total SME financing has grown from 22.0% in 2010 to 34.0% at the end of 2018. *Skim Pembiayaan Mikro* has been providing financing of up to a maximum of RM50,000 without collateral to microenterprises since 2005.

From its inception until the end of 2018, a total of RM4.1 billion financing was approved to 230,082 microenterprises via ten participating banks. The total financing outstanding under the scheme stood at RM910.7 million as at the end of 2018, with RM302.7 million approved to more than 13,000 accounts during the year. As of September 2019, 8,148 applications amounting to RM187.6 million were approved while RM174.6 million was disbursed. Total financing outstanding stood at RM847.3 billion.

CHEAPER FINANCING FROM BNM FUND FOR SMEs

As at the end of 2018, outstanding financing - mainly for working capital or business expansion - under the Bank Negara Malaysia Fund for SMEs stood at RM5.8 billion. More than 80,000 accounts amounting to RM31.1 billion have been approved since the establishment of the fund in 1993. At the end of the September 2019, outstanding financing of the fund stood at RM5.2 billion, with RM3.8 billion still available for new applications.

ALTERNATIVE FINANCING

Venture Capital and Private Equity

In tandem with the Government's agenda to create a new and innovative economic model, private equity and venture capital as alternative financing avenues are seen as the next engine of growth to push Malaysia into the ranks of high-income nations. The role of private equity and venture capital in financing is increasingly significant as the focus shifts to attracting investment in new growth areas, such as information and communication technology (ICT), multimedia, biotechnology and renewable energy which traditional lenders consider as high-risk undertakings and thus are reluctant to provide financing.

At the end of 31 December 2018, there were 117 registered corporations involved in venture capital and private equity. Of the total, 105 were venture capital management companies (VCMC) and venture capital corporations (VCC) while 12 were private equity management corporations (PEMC) and private equity corporations (PEC).

Table 6.1: Statistics of Industry Participants

	31 December 2018	31 December 2017
Number of registered corporations	117	110
Number of registered VCMCs and VCCs	105	101
Number of registered PEMCs and PECs	12	9
Number of investee companies	387	381
Number of VC and PE professionals*	235	182

** Professionals with more than four years of experience*

In 2018, there were 387 investee companies compared with 381 in 2017 while the number of professionals with at least four years of experience employed by the industry totalled 235. The total amount of funds committed by these corporations was RM6.1 billion at the end of 2018, a decrease compared with that of 2017 owing to the deregistration of a major VCC. Nevertheless, there was a 46.8% increase in investment activity amounting to RM613.3 million in 2018 compared with RM417.8 million in 2017. At the end of 2018, total cumulative investments stood at RM3.1 billion while there was a decrease in divestments, from RM375.2 million in 2017 to RM161.0 million.

Public funds remain the largest source of capital for the industry with Government agencies and investment companies making up 40.2% while sovereign wealth funds contributed 30.2%. Private sector contribution to the industry were led by asset managers (9.7%) followed by corporate investors (10.8%) and individual investors and family officers (5.1%).

Investee companies at the early and growth stages received the bulk of the funding in 2018. Of the total investments made in the year, 86.9% (RM53.0 million) was channelled into 96 investee companies. Investments into start-up stage firms accounted for 0.8% of total investments while five investee companies were recipients of investments. The life sciences sector was the biggest recipient, receiving 49.6% of total investments which were primarily channelled towards medical devices, pharmaceuticals and environmental biotechnology. The IT and communications sector saw an increase to 22.7% in its share of investments while the manufacturing sector's share declined to 5.9%. Other sectors, such as wholesale and retail trading, creative media, logistics, education and financial services obtained a 21.8% share of total investments.

Table 6.2: Sources of Funds (2018: RM6.08 billion)

Government agencies and investment companies	40.24%
Sovereign wealth funds	30.19%
Corporate investors	10.80%
Fund-of-funds and other asset managers	9.74%
Individual investors and family offices	5.09%
Pension and provident funds	2.99%
Financial institutions	0.54%
Insurance companies	0.41%

Table 6.3: Investments by Financing Stage (2018: RM613.28 million)

Early stage	46.48%
Growth	40.43%
Others	10.61%
Turnaround / restructuring	1.01%
Start-up	0.80%
Bridge / mezzanine / pre-IPO	0.67%

Notes:
Government agencies and investment companies includes ministerial investment companies (e.g. Minister of Finance (Incorporated), Government agencies, statutory bodies and Government-linked investment companies established for the purpose of managing investments of public funds (e.g. PNB, Ekuinas)

Equity Crowdfunding

Since its inception, equity crowdfunding (ECF) has raised RM48.8 million in capital through 51 successful campaigns by 50 issuers with a 93% campaign success rate. In 2018, RM15.0 million was raised by 14 issuers. Among the successful fundraising campaigns to date, 47% raised RM500,000 and below.

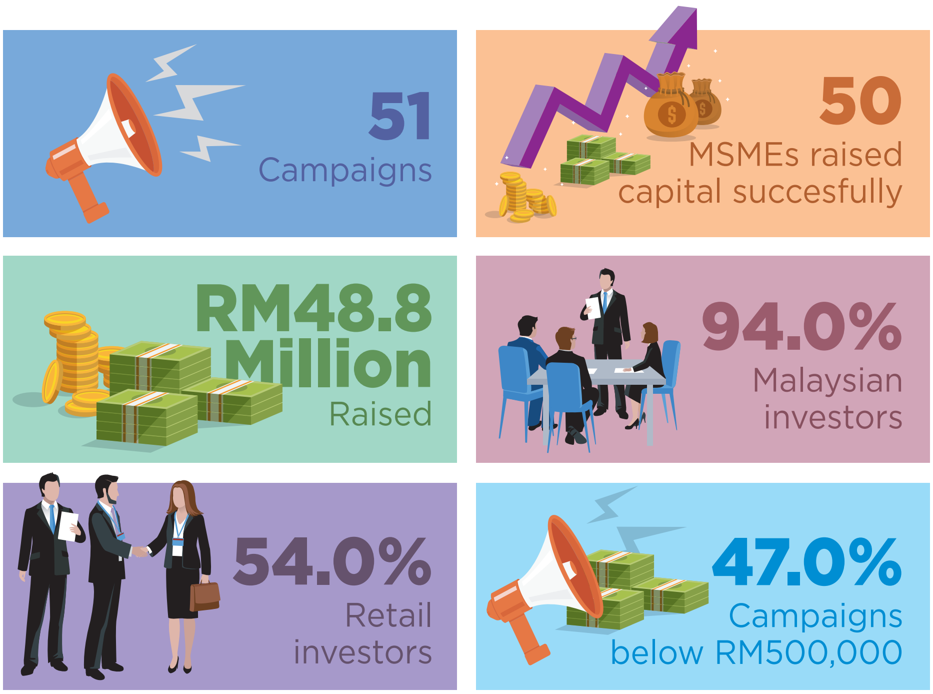
Table 6.4: Number of Successful Campaigns and Issuers by Year

	2017	2018
Number of campaigns	24	14
Number of issuers	24	14

Table 6.5: Distribution by Fundraising Amount

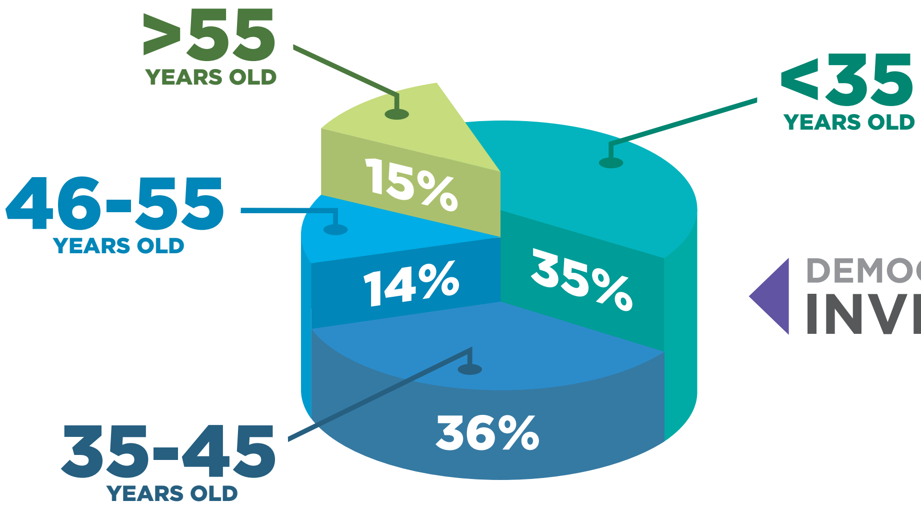
RM500,000 and below	47.0%
More than RM500,000 and up to RM1.5 million	29.0%
More than RM1.5 million and up to RM3.0 million	24.0%

Chart 6.2: Equity Crowfunding in Malaysia at a Glance (2016-2018)

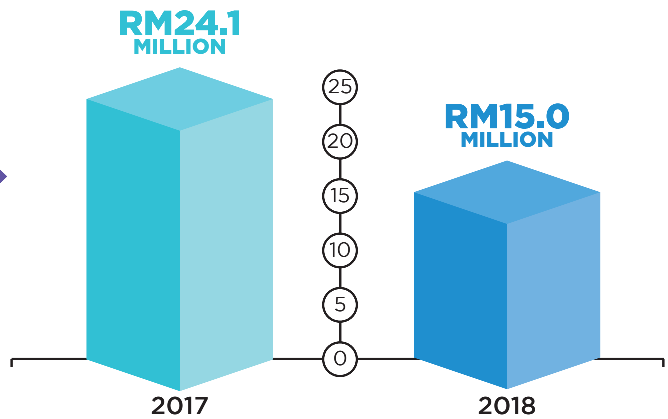


"ENTREPRENEURSHIP DRIVING SMEs"

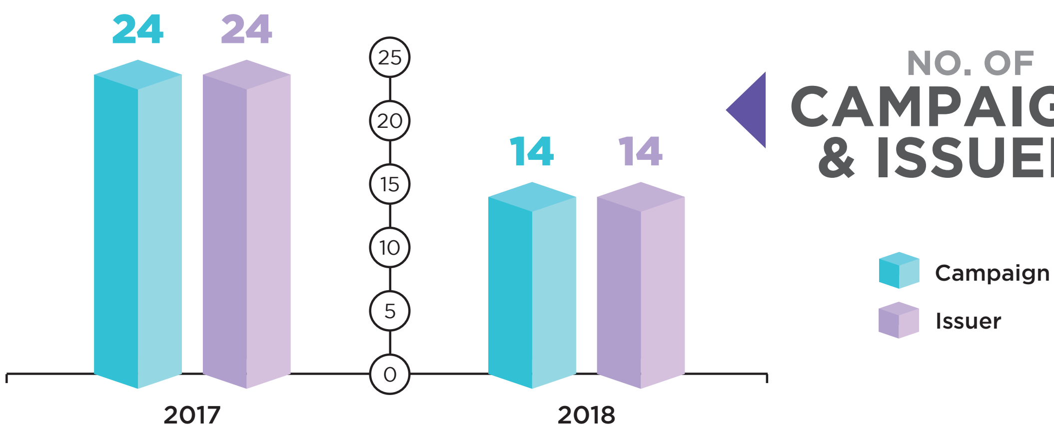
DEMOGRAPHIC OF INVESTORS



TOTAL CAPITAL RAISED



NO. OF CAMPAIGNS & ISSUERS



Peer-to-Peer Financing

Since 2017, RM212.6 million have been raised through 2,505 successful peer-to-peer (P2P) financing campaigns by 643 issuers. Issuers raising funds on P2P financing platforms have maintained a campaign success rate of 99.0%.

In 2018, RM180.0 million was raised, a 452.0% growth compared with 2017. Among the successful campaigns, 91.0% raised RM200,000 and below while 22.0% of the successful issuers raised funds more than once.

> Since 2017, RM212.6 million have been raised through 2,505 successful peer-to-peer (P2P) financing campaigns by 643 issuers.

Table 6.6: Number of Successful Campaigns and Issuers by Year

	2017	2018
Number of campaigns	604	1,901
Number of issuers	79	602

Table 6.7: Distribution by Fundraising Amount

RM200,000 and below	91.0%
Above RM200,000	9.0%

As at September 2019, the ECF and P2P financing platforms have collectively raised RM580.0 million, benefitting over 1,600 SMEs. These financing campaigns attracted more than 12,000 investors, 90% of whom are local and retail investors. Year 2019 also saw the Securities Commission (SC) registering three new ECF and five new P2P financing platforms as well as the first two exits of the ECF market:

i. **Skolafund**, a social enterprise crowdfunding scholarships for university students, fundraised on the Ata Plus platform in 2017 and by one of Asia's biggest donation crowdfunding platforms; and

ii. **MyCash Online** which caters to the needs of unbanked migrants, acquired after initial fundraising on PitchIn.

SMALL DEBT RESOLUTION SCHEME TO ASSIST VIABLE BUT FINANCIALLY DISTRESSED SMEs

Viable but financially distressed SMEs which could not find debt resolution with their lending banks can seek assistance under the BNM Small Debt Resolution Scheme (SDRS), a mechanism for financial institutions to assist distressed SME borrowers through restructuring and rescheduling of existing debts.

SDRS, which was established in 2003, serves as a platform to assist SMEs that are constrained by impaired financing or facing financial difficulties from multiple financial institutions. In 2018, a total of 66 distressed firms received assistance through the scheme.

The Small Debt Resolution Committee (SDRC), an independent committee established by BNM, undertakes an assessment of the SME application and its business viability. If eligible, the SDRC would propose to the participating financial institution to assist the SME via the restructuring or rescheduling of its financing facilities.

In 2018, 85.0% of the applications received, totalling RM118.0 million in impaired loans were approved by SDRS for restructuring or rescheduling. At the end of 2018, about 54.0% of SMEs assisted under the scheme were able to improve their cash flow and turned around their businesses to remain viable while 74.0% have fully settled their debt. Since its establishment and up to the end of September 2019, the SDRS has helped to restructure a total of RM1.6 billion in impaired loans.

OUTREACH TO SMEs

As part of its outreach to SMEs, BNM continues to promote awareness of the existence of programmes for financing, capacity building, provision of assistance by relevant agencies as well as the availability of redress mechanisms of financial institutions in partnership with Government agencies.

Regular outreach initiatives have been conducted nationwide to educate SMEs on financial management and to create awareness on the various financing options, programmes and initiatives available for businesses. In 2018, more than 8,000 SMEs benefitted from 50 outreach programmes while about 1,100 SMEs had benefitted from seven financing seminars and clinics conducted nationwide.

The seminar module covered areas, such as financial management, requirements by financial institutions and processes involved in applying for financing, Islamic financing, avenues to seek advisory information and redress assistance, capacity building initiatives including business risks management and business digitalisation through adoption of e-payment as well as alternative financing avenues, such as P2P lending and ECF.

In the drive towards greater financial inclusion, BNM also focused its education programmes in 2018 on reaching out to smaller towns, such as Jerantut, Taiping, Labuan and Pagoh via the Karnival Kewangan programme. The outreach was particularly effective in educating the unserved-bankable and under-served-banked population. As at October 2019, BNM has conducted several Karnival Kewangan programmes at the regional level with sessions in Miri, Terengganu, Melaka, Sabah and Perlis.

> A total of 33 programmes under access to financing category have been planned for 2019 with a financial commitment of RM13.1 billion for 434,502 beneficiaries.

SME FINANCING IN 2019

The need to broaden the range of financing instruments for SMEs and entrepreneurs remains one of the key agenda for the Government to address diverse financing needs in varying circumstances. To further stimulate their contribution to economic growth, a total of 33 programmes under access to financing category have been planned for 2019 with a financial commitment of RM13.1 billion for 434,502 beneficiaries. The programmes include:

- **Working Capital Guarantee Scheme** by SJPP in partnership with the Ministry of Finance, offers assistance to SMEs in all sectors of the economy to obtain financing from participating financial institutions. For 2019, RM3.0 billion has been allocated to assist 2,500 beneficiaries.

- SJPP is also undertaking the **Automation Process Guarantee Scheme** to assist SMEs in all sectors to automate production processes and reduce employment of foreign workers. The programme, which is implemented through financial assistance offered by participating financial institutions, targets to assist 300 beneficiaries in 2019 with a total allocation of RM950.0 million.

- **TEKUN Financing Programme** offers funding for business expansion and micro financing for working capital to assist small Bumiputera entrepreneurs in their existing or new business start-ups as well as project implementation. The programme, which is led by TEKUN Nasional, also provides participants with business opportunities, advisory and support services as well as inculcates a culture of competence, innovation and progressive entrepreneurship among the TEKUN entrepreneurs community. TEKUN Nasional has allocated RM100.0 million for the programme for 2019 and set a target to assist 17,500 beneficiaries.

- CGC is undertaking six **Guarantee Schemes** to facilitate financing for SMEs. The schemes comprised Portfolio Guarantee (PG)/Wholesale Guarantee (WG), BizJamin (previously known as Credit Enhancer), BizJamin Bumi (previously Enhancer Bumi), BizMaju (previously Enhancer Excel), BizSME and Flexi Guarantee Scheme. Under the PG/WG scheme, CGC collaborates on a pre-agreed criteria and fast-track basis with individual financial institutions to help SMEs obtain financing while the other schemes provide assistance to SMEs to secure credit facilities. CGC has secured a financial commitment of RM3.9 billion to assist a target of 8,500 SME beneficiaries in 2019.

- **Business Accelerator Programme (BAP)** is an integrated programme which is led by SME Corp. Malaysia to develop and nurture dynamic, competitive and resilient SMEs through the SME Competitiveness Rating for Enhancement (SCORE), capacity building, advisory and technical service as well as financial support. For 2019, RM58.9 million has been allocated to implement the programme for 450 beneficiaries.

- **Syariah-Compliant SME Financing Scheme (SSFS)** is another programme implemented by SME Corp. Malaysia through thirteen participating Islamic financial institutions (FIs) to provide financing for eligible Malaysian SMEs whereby 2.0% of the profit rate charged by FIs absorbed by the Government. The programme targets to benefit 450 beneficiaries through an allocation of RM14.5 million in 2019.

- ***Tabung Projek Usahawan Bumiputera-i* (TPUB-i)** provides financing to Bumiputera SME entrepreneurs who have been awarded projects or job contracts but are unable to obtain financing from financial institutions. An allocation of RM480.0 million has been committed by CGC for 2019 to assist 370 beneficiaries.

- Perbadanan Nasional Berhad is leading the **PNS Financing Scheme** with an aim of developing and promoting middle-level Bumiputera entrepreneurs in the franchise business through financial assistance for business expansion and new start-ups. An allocation of RM25.0 million has been earmarked to assist 180 beneficiaries in 2019.

- The Ministry of Rural Development is leading the implementation of **Rural Business Challenge Programme** which has been designed to uplift the socio-economic status of the rural population by encouraging youths to choose entrepreneurship as career of choice as well as to create jobs and increase the income of the rural population. The programme also aims to reverse rural-urban migration by creating an attractive lifestyle in rural areas. The programme which takes the form of business proposal competition where winners are offered grants to kick-start their entrepreneurial dreams, has been allocated RM15.0 million to assist 20 beneficiaries in 2019.

FINANCIAL ADVISORY SERVICES

BNM's *Laman Informasi Nasihat dan Khidmat* (BNMLINK) offers advisory services on matters related to financing as well as providing avenues for redress for SMEs. While providing education to consumers on financial matters, BNMLINK also serves as a public information platform on BNM's latest policies and initiatives, such as access to financing for SMEs, awareness of financial scams and implementation of e-CCRIS.

In 2018, BNMLINK held more than 1,000 engagement sessions on SME-related matters, covering mainly enquiries and complaints and appeal cases on access to financing, products and services and disputes. In 2019, efforts to resolve SME financing issues continue to be stepped up to provide end-to-end facilitation to SMEs through enhanced collaboration among BNM, SME Corp. Malaysia, Association of Banks Malaysia, ministries and agencies as well as CGC.

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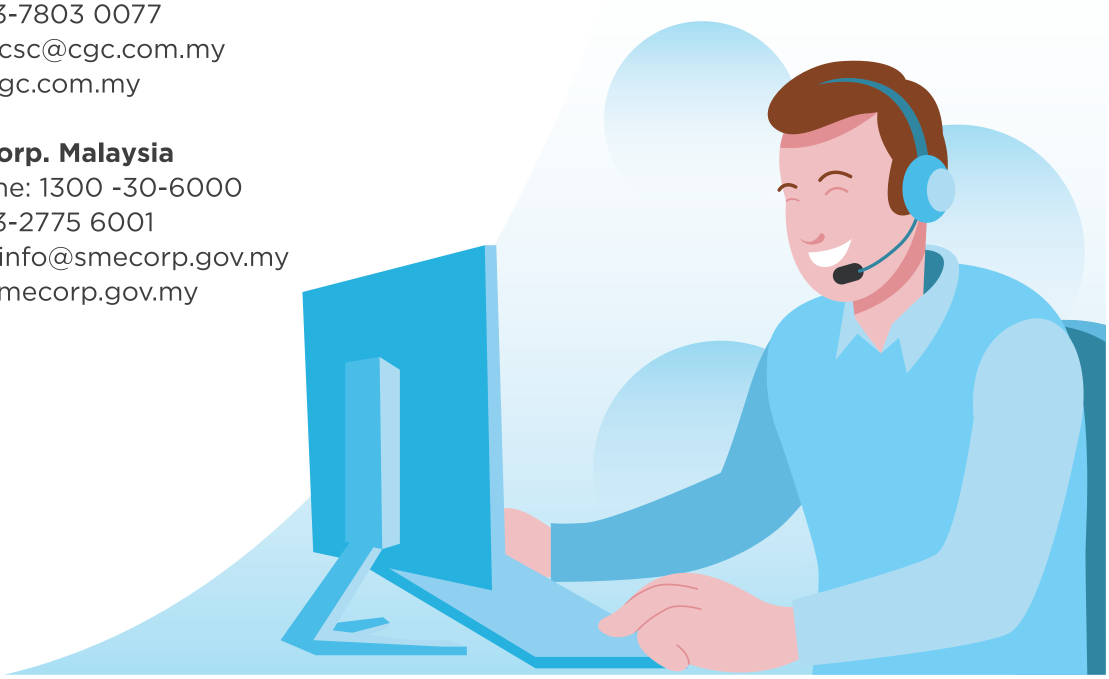


BOX ARTICLE

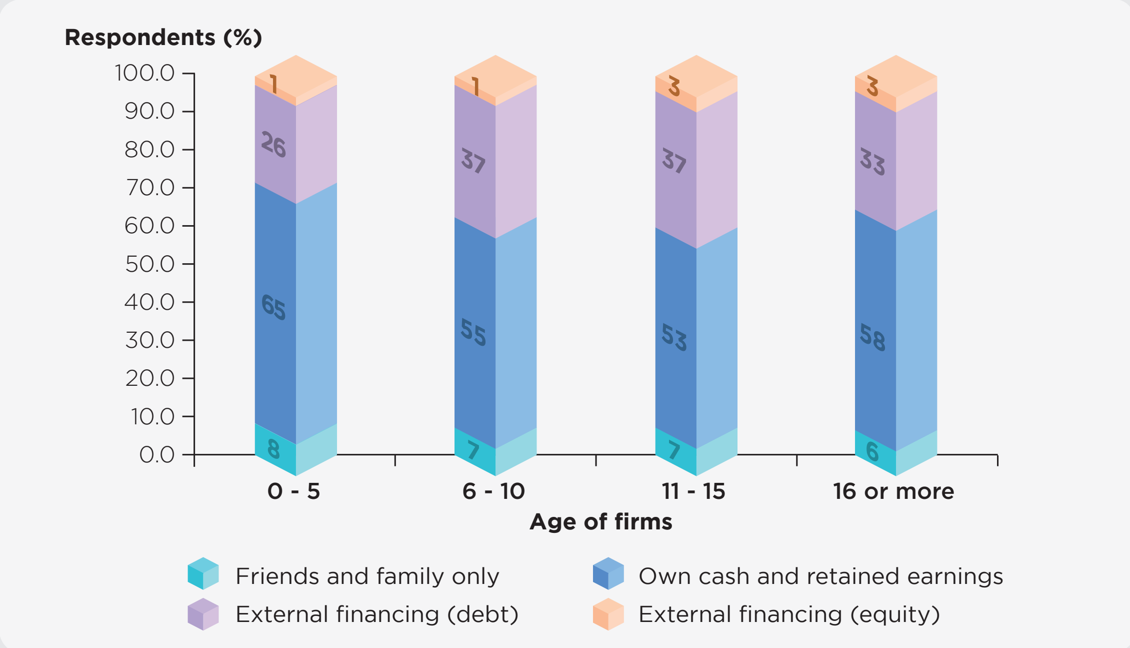
SME Finance Survey 2018: Understanding Financing from the SME Perspective

As an ongoing effort to promote greater access to financing for SMEs, Bank Negara Malaysia commissioned an independent SME Finance Survey with a field of 1,529 formal SMEs and 223 informal businesses in the second quarter of 2018. The field of Survey was intended to be representative of the national SME population while its focus was largely on obtaining an insight into the respondents' perspective on access to finance coupled with a look into other complementary areas of activities, such as business performance, challenges encountered and utilisation of other financial services.

Key Findings of the Survey

- **Financing Sources Vary at Different Stages of Business Lifecycle**
  At the initial stage of business, SMEs tend to rely on their own funds and informal sources, such as family and friends but would increasingly turned to external financing, in particular debt financing, as the business matures (refer to Chart 1). At the time of the Survey, 35.0% of respondents reported obtaining financing from external sources.

Chart 1: Sources of Financing by Age of Firms (%)



Source: SME Finance Survey 2018, Bank Negara Malaysia

- **High Approval Rate of Financing for SMEs in the Last Six Months before Survey**
  About 22.0% of the respondents had applied for financing in the six months prior to the Survey. There was a 91.0% approval rate for applications made to financial institutions and a 99.0% approval rate for applications to other sources (mainly Amanah Ikhtiar Malaysia, AIM and TEKUN), making for an overall approval rate of 94.0%.

  Women-owned firms reported higher-than-average demand for financing, comprising 33.0% of applications received compared to the average of 22.0% for all respondents. Women-owned firms also experienced a lower approval rate of 83.0%, owing mainly to a lack of track record and insufficient documentation. Women-owned firms obtained their financing largely from microfinance institutions.

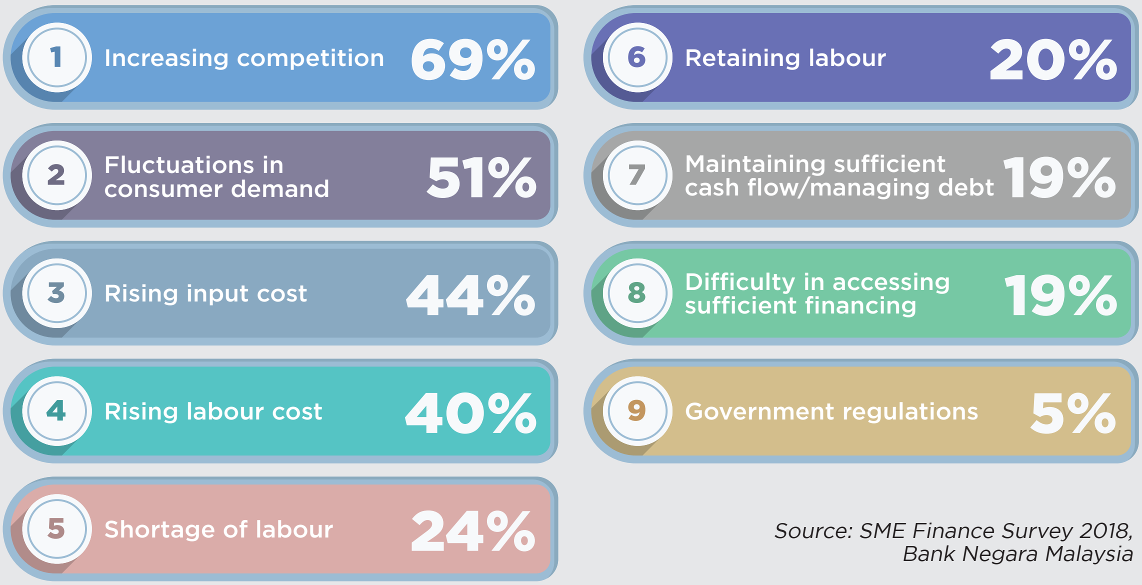
  The main purposes of financing as cited by all respondents were for asset purchases, such as building, property, machinery and equipment (23.0%), working capital (22.0%) and starting a new business (19.0%).

- **Usage of Other Financial Services**
  More than half (54.0%) of the respondents reported using insurance or Takaful products, with usage progressively increasing as firms grew in size. Though the current take-up rate is low, there is a significant potential demand from SMEs for insurance and Takaful for all products across the board, with emerging interest particularly in protection against risks associated with cyber security, professional indemnity and payment default products.

SMEs mainly used electronic payment modes where their creditors are concerned while preferring to receive payment in cash from customers. Cheques continued to be the most popular payment mode for SMEs in Business-to-Business (B2B) transactions.

- **Access to Financing not a Major Constraint to SME Growth**
  The majority of respondents (71.0%) do not consider access to financing as a major impediment to growth. Access to financing as a constraint was ranked very low, second from last of the major constraints. Increasing competition was ranked by 69.0% of the respondents as the top challenge faced by SMEs, followed by fluctuating demand (51.0%), rising input cost (44.0%) and labour-related issues.

Chart 2: Constraints Impeding SME Business Growth



Source: SME Finance Survey 2018, Bank Negara Malaysia

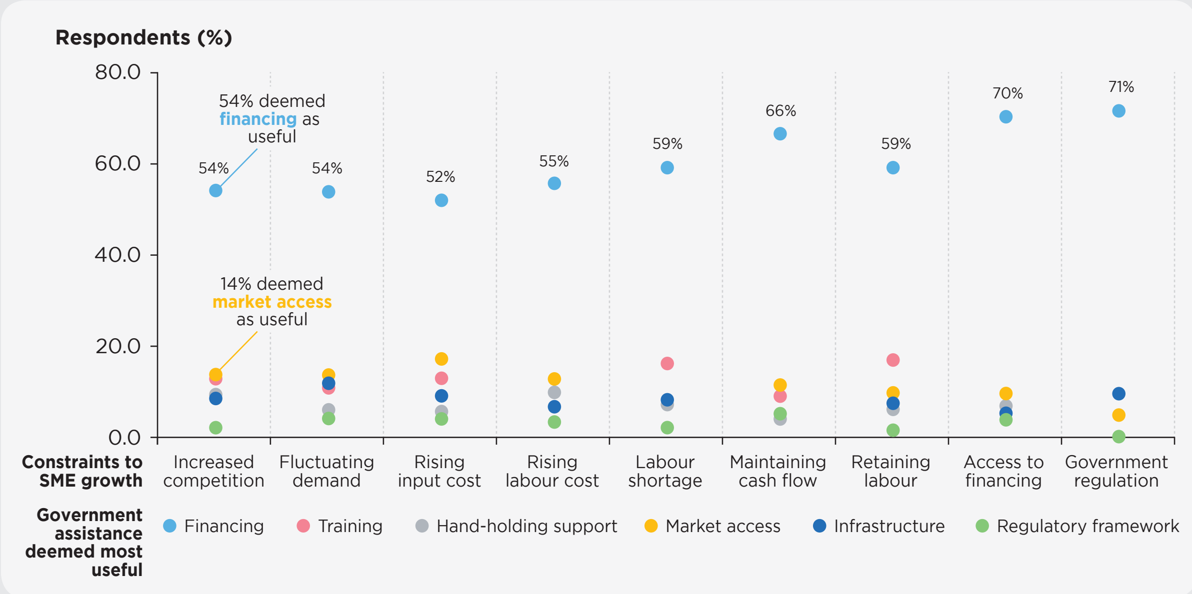
Underlying Challenges

The Survey reveals that financing barriers mainly relate to documentation, costs and business viability. Financing applications were rejected mainly owing to:

- Insufficient documentation;
- Insufficient cash flow; and
- Business plans which were deemed not viable.

Firms which automate have higher demand for financing from financing institutions (29.0%) but experienced higher rejection rates due to insufficient collateral or to projects that were deemed risky. The higher risk associated with these firms probably stem from the low salvage value of moveable and intangible assets in the event of commercial failure as well as high uncertainty on returns from new and untested processes.

Chart 3: Government Assistance Deemed Most Useful by SMEs (%)



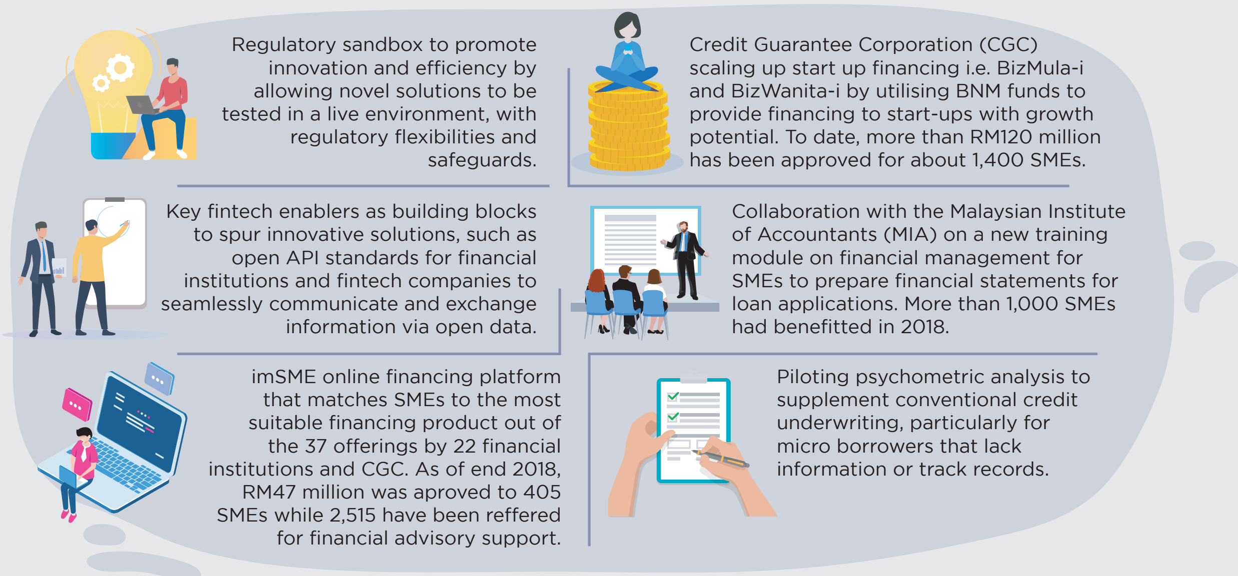
> While the performance of informal businesses was on par with formal businesses, only 6.0% of the former has intention to formalise their business.

The Survey also identified a significant majority of SMEs who viewed financial assistance (e.g. grants, soft loans, guarantees) from the Government as its most useful resource regardless of the challenges they faced. This could suggest a lack of awareness of other non-financial assistance, such as in capacity building, hand-holding support and access to new markets, which would be more relevant in helping them to face their challenges.

While the performance of informal businesses was on par with formal businesses, only 6.0% of the former has intention to formalise their business. Informal businesses which are not registered with the Companies Commission of Malaysia cited uncertain demand, difficulty to maintain cash flow and increased competition as the main factors that discourage them from formalising their business.

The findings of the Survey also affirmed that ongoing initiatives - encouraging greater innovation by financing institutions, improving the efficiency of financing processes, providing more credit enhancement products for SMEs and strengthening the financial management capabilities of SMEs - remain relevant to enhance their access to finance. Details of the initiatives are as in the following diagram.

Chart 4: Recent Initiatives to Enhance SME Financing



Moving forward, there are opportunities to pursue other policy priorities like a secured transaction network, promotion of alternative financing and formalisation of informal business.

- **Establishing a Secured Transaction Network**
  Efforts are ongoing to establish a modern and unified movable property security interest legislation, as well as a centralised collateral registry for movable assets in Malaysia as these could improve access to financing for SMEs. A new secured transaction framework would broaden the range of assets that SMEs can use beyond conventional collateral (building or property), for example, machinery and equipment, intellectual property, inventories and agricultural products.

- **Promoting Alternative Financing**
  Alternative financing which would include venture capital, equity crowdfunding, angel investments, leasing, factoring and peer-to-peer (P2P) financing, could play a bigger role in complementing bank financing to bridge the financing gap in catering to firms, such as technology-based start-ups and innovative firms - deemed not viable for financing by deposit-funded banks. It is estimated that alternative financing makes up less than 3.0% of total SME financing in Malaysia.

- **Formalising Informal Businesses**
  Incentives should be provided for informal businesses to formalise in order to enhance their accessibility to more financing options and other Government programmes. Access to benefits, such as social protection schemes, commercial finance and business development services as well as facilitative tax administration could encourage greater formalisation of businesses. However, such incentives should be balanced with better enforcement, including stiffer penalties for non-compliance with business regulations.

BOX ARTICLE

SME Investment Partner (SIP) to Enhance Access for Early Stage Financing

As Malaysia seeks to promote new areas of growth and move towards an innovation-led economy, there was a need to strengthen new avenues of financing to support start-ups and innovative firms. Banks are typically not structured to take on these types of financing. This gap in financing led to the establishment of the SME Investment Partner (SIP) Programme. Introduced as one of the high impact programmes in the SME Masterplan (2012 - 2020), SIP has the objective to enhance access to financing for SMEs, particularly those at early stage through the provision of risk capital financing. SIP finances SMEs particularly those at early-stage, covering all sectors including mainstreet firms that have strong high growth potential, innovative and in newly emerging areas. SIP entails a co-funding initiative between the public and private sector, whereby an investment entity established will channel the fund to viable SMEs in the form of equity, debt or a hybrid of debt and equity.

Under the Programme, the Government would invest long-term capital in privately-owned and managed investment companies that are licensed, hence complementing the existing venture capital landscape. Essentially, the SIP is a 'fund of funds' – meaning that portfolio management and investment decisions are left to qualified private fund managers, termed as the SME Partner. The investment companies would raise capital from private investors with a pledge of certain amount debt capital availability from the Government. The debt capital will be subjected to a maximum cap for each investment company. This pooled fund will be channelled to viable SMEs in the form of loan, equity or a hybrid of loan and equity.

SIP is available for SMEs in all sectors including main street firms that have strong high growth potential, innovativeness and in newly emerging areas. This is more well-spread compared to current venture capital financing which are mainly for technology-based companies. This mechanism sketched the four unique offerings of SIP as below:

- Cater for early-stage SMEs;
- Cover SMEs in all sectors including traditional sectors;
- Co-funding between public & private sectors; and
- Flexibility to offer both equity & debt funding.

Chart 1: SME Investment Partner (SIP) Programme at a Glance

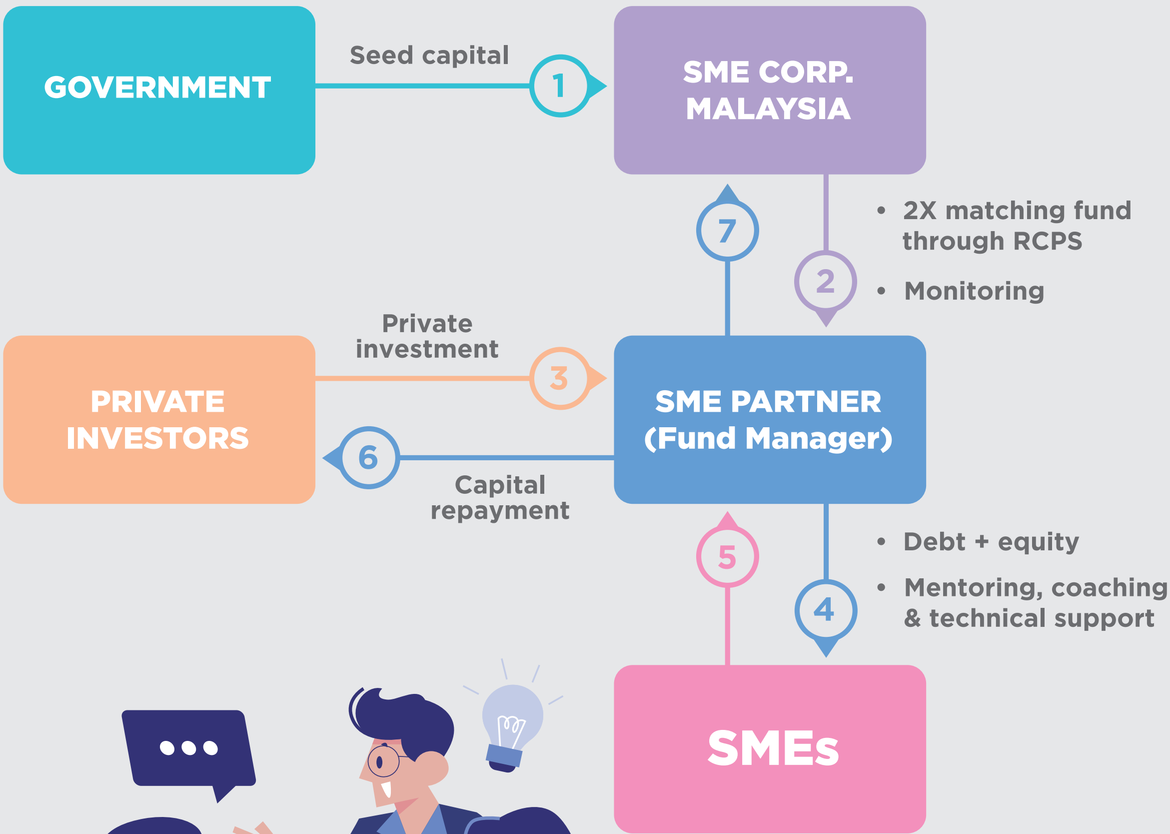


Chart 2: Role of SME Partner under the SIP Programme

- Raise funds from private investors
- Identify viable SMEs to be financed
- Perform financial analysis and due-diligence
- Provide detailed analysis or performance
- Provide financing to SMEs
- Provide hands-on mentoring and technical guidance
- Identify specific needs of SMEs
- Monitor investments made to SMEs
- Ensure timely repayment / service of investments
- Provide regular financial and operational reporting

There were many challenges in implementation of the SIP. Traditionally, early stage SMEs are deemed as being inherently more risky. Of such, investors prefer to concentrate on growth and expansion stage companies with good cash flow management. Most of the potential private investors take the wait and see attitude and prefer to study the first investor details and the market sentiment before putting their own investments. The SIP Fund is considered as micro fund compared to other private equity and venture capital funds available in the market. Hence many investors are not interested as it is deemed as not cost effective for the fund to be commercially viable. There is also a lack of support from local institutional investors on SMEs due to maximisation of investment based on size and preferred sectors.

"The SIP Fund is considered as micro fund compared to other private equity and venture capital funds available in the market."

In addressing these challenges, SME Corp. Malaysia appointed multiple SME Partners based on matching funds readiness from private investor. Conditional appointment was also introduced to eliminate the long fund raising process and to intensify the competition among the SME Partners. SME Partners are required to deliver the matching fund within their own committed time frame on a first come first serve basis.

Programme Scope

The SIP provides:

- Financing to early stage SMEs of one to three years in operation across all sectors;
- Working capital injection in the form of a debt or a hybrid of debt and equity in the range RM500,000 to a maximum of RM5 - RM7 million (based on the terms of the fund providers);
- Technical assistance, hands-on mentoring for SMEs to grow and expand their business; and
- Capacity building programmes to enhance business performance and to increase revenue in collaboration with SME Corp. Malaysia.

Potential investee must fulfill basic criteria as below:

- Has fulfilled the definition of SME;
- Registered with Companies Commission of Malaysia;
- Has at least 51% Malaysian equity;
- In operation between one to three years only; and
- Has exhibited evidence of market traction, especially revenue generation.

Application Process

Moving forward, the Government may need to introduce a policy to mandate contribution from Government institutional investors (vs retail investors) to support Malaysian SMEs. On the part of SME Corp. Malaysia, establishment of SIP Subsidiary to promote investments into main street (non-tech) SMEs with co-funding element will accelerate the fund approval and disbursement processes.