Fintech India – The Changing Landscape of SME Lending

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MAPE Advisory Group
ADVISORY FOR GROWTH

MXV CONSULTING

PREFACE

As the proverb goes, **"every oak must be an acorn"**.

Small and Medium Enterprises (SMEs) are the engine that drives the global economy, typically contributing more than a third of the GDP and about half of all employment. India has more than 50 Mn SMEs, accounting for 38% of GDP.

Funding has always been a constraint to the growth of SMEs. Smaller entities often do not have the credentials to avail funding from banks or other formal lenders. Even where credit is available, they often have to go through cumbersome processes and pay exorbitant fees – impacting their competitiveness and growth prospects. It is not unusual for a bank to take a few months to approve an SME loan. In the western world, the median difference between credit rates to large and small borrowers is almost 2%. In Spain, an SME may end up paying a bank 10% for a loan – at a time when the bank's own cost of funds is close to zero.

The situation has worsened post 2008. Despite the overall improvement in global liquidity, SMEs continue to struggle. In the US, small business credit from banks decreased 20% between 2008 and 2012. In India, barely 10% of small organisations have access to formal credit. Post-demonetisation, many SMEs have had their strength tested. Building a formal credit history takes time; many of these enterprises may not last that long.

All of this, of course, presents a large opportunity. Even 5% of the unmet SME lending requirements in India could be a $ 15 Bn opportunity by 2020. The system has the liquidity – but banks do not have the processes or risk management framework to enable lending to these firms. This is where alternate lenders come in.

PREFACE

Over the last decade, non-traditional (or alternate) lenders have entered the SME lending space in numbers. These are children of a digital world – using data and digital processes to transform the lending space. They work with new-economy partners, use non-traditional data sources (including daily POS collections and social network scores), develop new credit rating algorithms (with significantly higher approval ratings compared to banks), have built smoother straight-through digital processes (loan approvals in minutes) and have made innovations in the collections process that make them attractive to borrowers. Such lenders have also displayed the ability to scale up and improve their economics on a sustained basis. Several marquis investors have supported the segment.

Unlike some other sectors, the incumbents have not pretended to be inert. Banks have made several attempts to address their shortcomings. The Bank of China has created a credit factory to speed-up SME loans (though they still have four layers of approvals). Many traditional financial services organisations are partnering with Fintech start-ups in order to tap into the opportunity and also make sure they have an innovation ecosystem they can learn from. Bank of Baroda, for instance, has recently announced tie-ups with five Indian Fintech companies.

All of this makes alternate lending a fascinating space for investors. The opportunity is a blue-ocean and new business models are being built every day. For an innovator, this is a great place to be.

Jacob Mathew
Co-Founder, MAPE

Amit Garg
Founder, MXV Consulting

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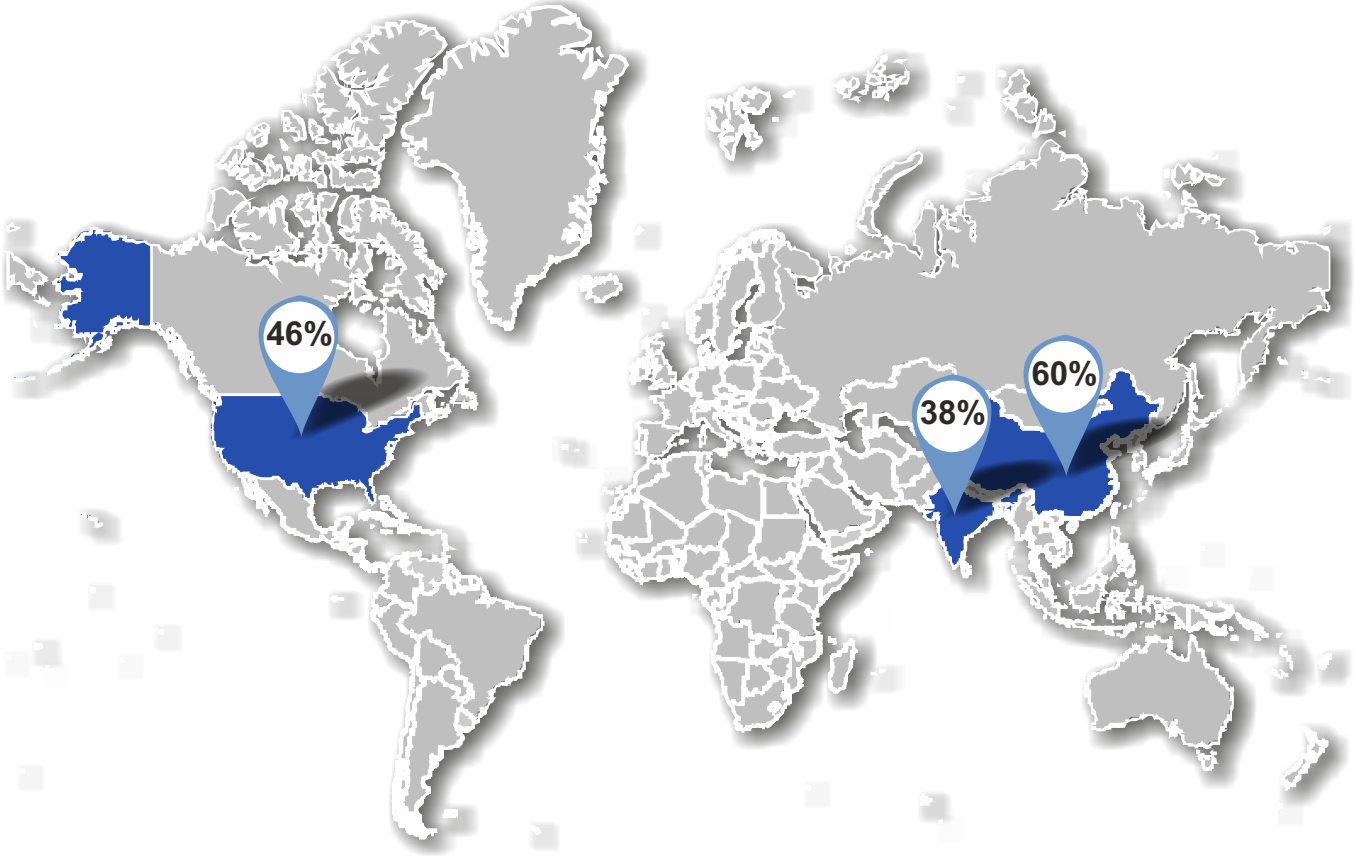
SMEs MAKE A SIGNIFICANT CONTRIBUTION TO THE WORLD'S GDP

Contribution of the SME sector to GDP



Note: Definition of SME differs between countries
Source: Literature review

FUNDING FOR SMES IS A GLOBAL OPPORTUNITY

$2.38 Tn
Global demand for SME credit

40%
Completely unserved MSMEs in developing countries

50%
SMEs who do not have a loan overdraft

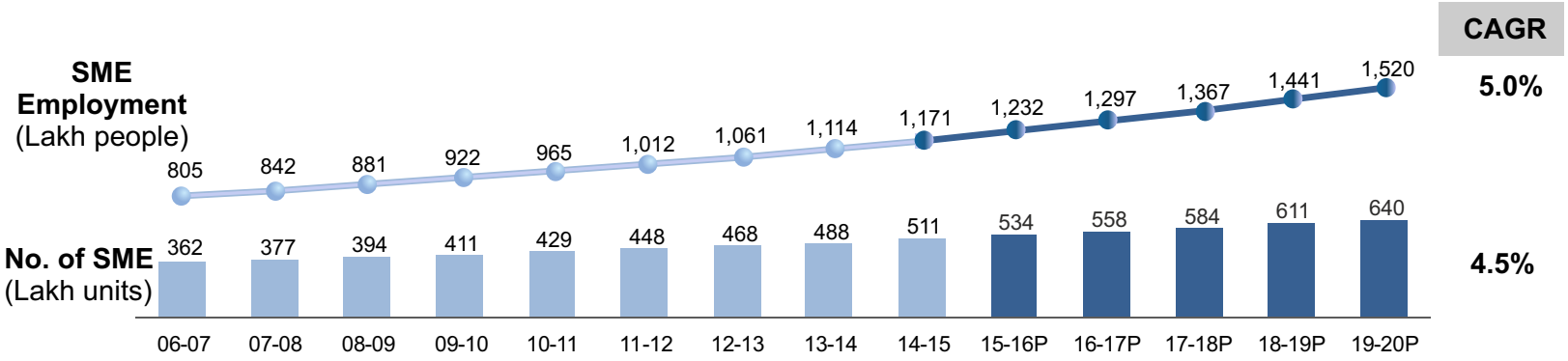
44%
In the US, percentage of SMEs who did not receive any of the bank credit they applied for

>75%
SMEs who are financially constrained

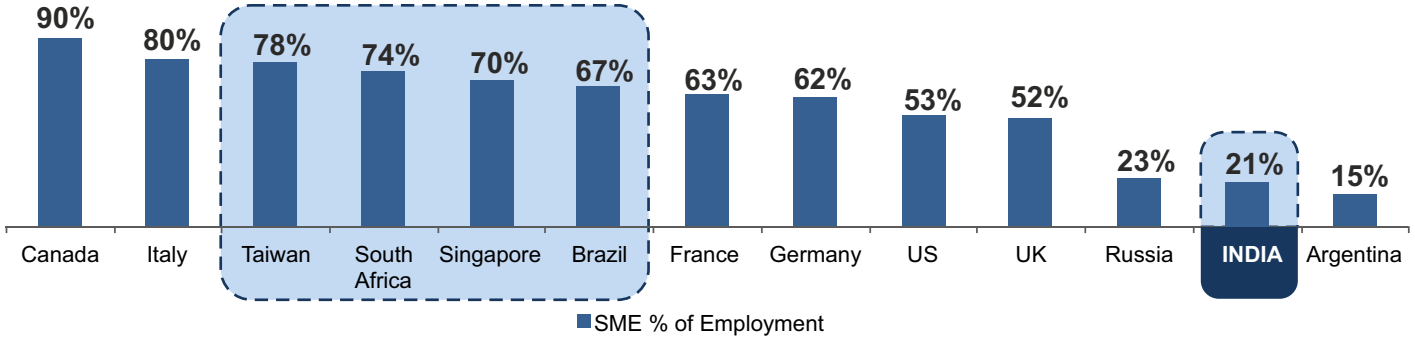
-20%
Change in small business loans in the US between 2008 and 2012

THERE ARE MORE THAN 50 MILLION SMEs IN INDIA

In 2013-14, SMEs absorbed 44% of new entrants into the labour force in India

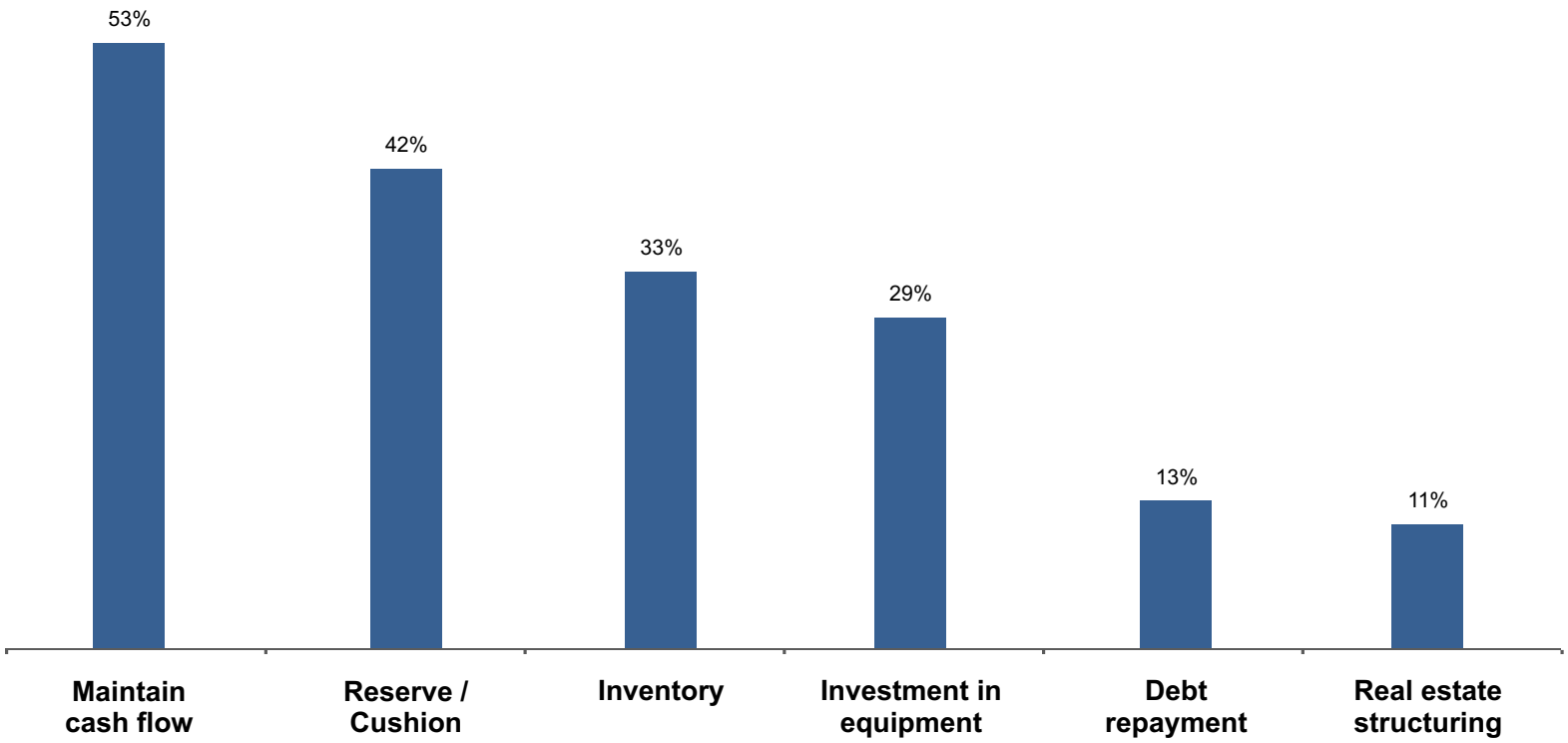


However the gap to other EMs highlights the potential to grow employee contribution to 50%



SMES NEED FUNDING FOR VARIED APPLICATIONS

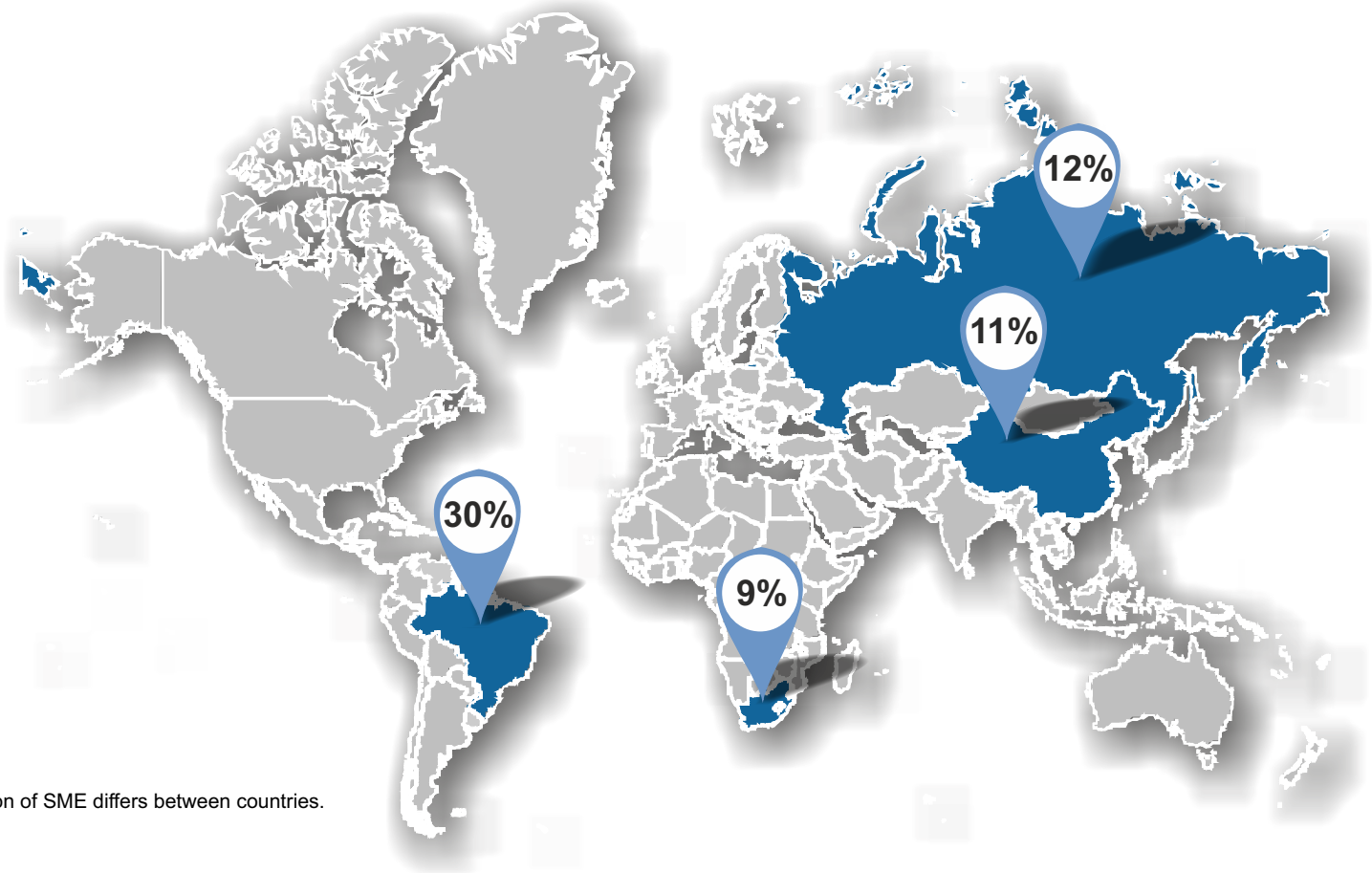
% of Surveyed SME Respondents on Application of Loan Capital



Source: HBS

GLOBALLY, SMES HAVE TROUBLE RAISING FUNDS

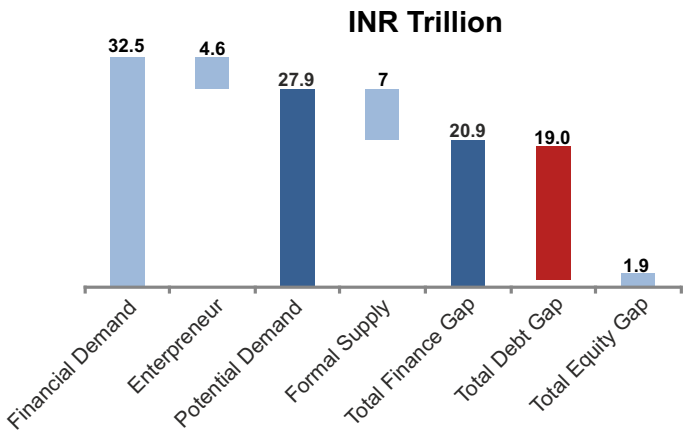
SMEs with access to credit



Note: Definition of SME differs between countries.
Source: IFC

FINANCING CONSTRAINTS A SIGNIFICANT HURDLE TO SCALE UP

Huge demand-supply gap in SME financing



That traditional institutions aren't able to bridge

Traditional banks are generally unwilling to make small ticket loans to these micro and small enterprises due to the perceived risk of such businesses especially without some form of collateral

Microfinance institutions have been able to successfully provide small uncollateralized loans to individuals and community groups however, based on regulations in place, microfinance loans are capped at Rs 100,000 -

Informal lending through local money lenders is available, but the annualized interest rates charged can be as high as 80%-100%

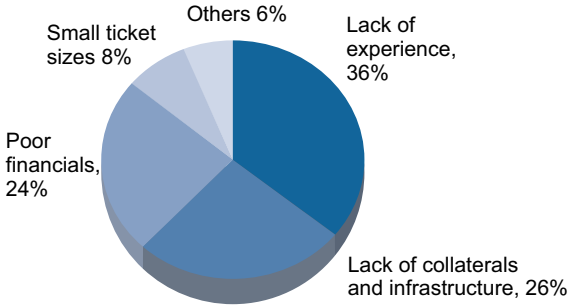
Further exacerbating the problems faced by SMEs

- Stretched receivables when dealing with larger customers
- High inventory carrying costs in the manufacturing sector
- High working capital requirements & limited expansion ability
- Stringent collateral requirements
- Limited access to equity capital

Resulting in a scarcity of adequate capital at a reasonable cost

Source: IIBF, IFC

Due to a combination of constraints



THE ASSESSMENT PROCESS IS TOUGHER ON SMES

Debt is the primary financing option for SMEs

- SMEs have had limited success with capital market floats, with only 143 IPOs through the BSE SME platform since 2011

SMEs are inadequately prepared to apply for credit

- Record-keeping at smaller entities is less rigorous, resulting in fragmented data
- Financial literacy is low among SMEs, and they are either not aware of options available for credit, or are unable to establish and state the case for loans

Cost of capital is higher because of difficulty in assessing risk accurately

- Standard bank tools fail to assess credit risk using the fragmented data from SMEs
- Rating Agencies like SMERA (SME Rating Agency) provide limited coverage of the segment – SMERA has rated about 43,000 entities, or less than 0.1% of all SMEs

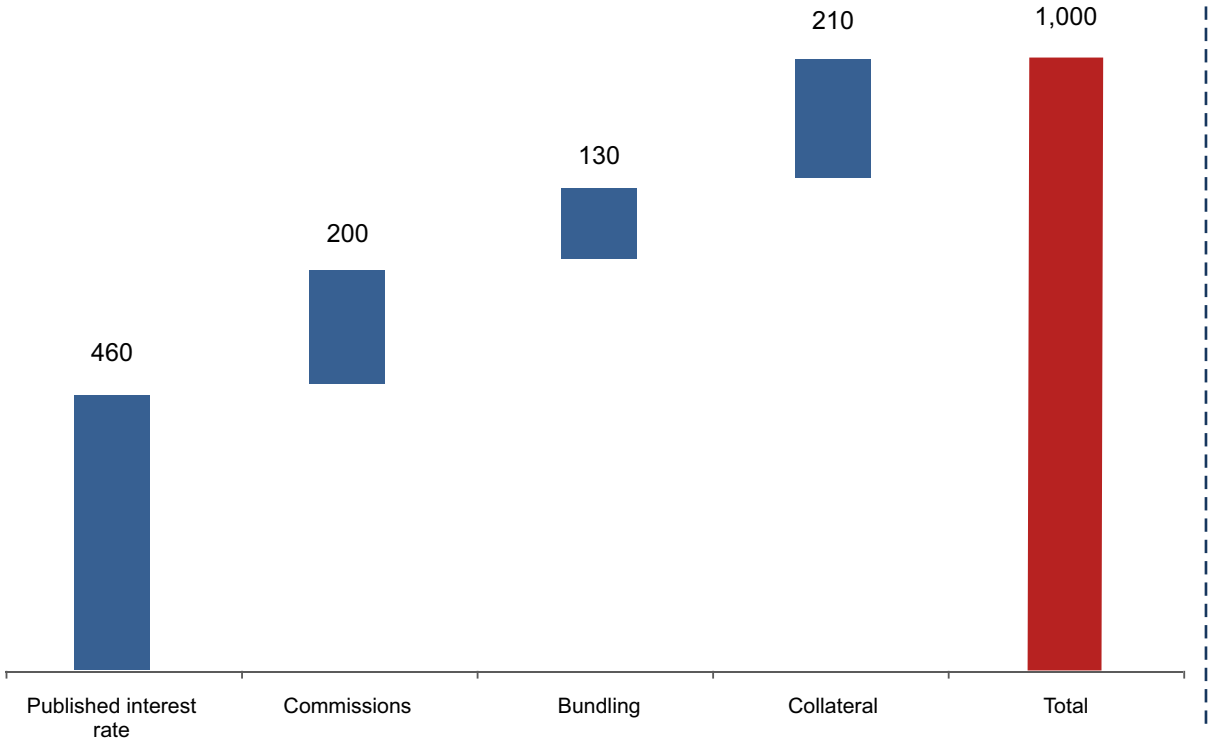
SMEs require flexibility in payment options

- Income volatility is higher for SMEs, and hence fixed monthly payments may not always work for them

Source: MXV Interviews, Literature Review

EVEN WHEN FUNDING IS AVAILABLE, COST TO SMES CAN BE HIGH EXAMPLE: SPAIN

Total cost paid by SMEs for their line of credit (basis points)



Borrowing rates for banks in Spain are close to 0%, but SMEs pay close to 10%for credit

Source:INBONIS

SEVERAL SME CLUSTERS COULD BE ATTRACTIVE

Agriculture / food processing

Food products and beverages account for 19% of MSME output; employing 6.3 Mn

Agricultural / commercial equipments leasing

Commercial leasing accounts for 25% of all leasing in India

Traders

Retail has 14 Mn enterprises and 25 Mn employees

Manufacturing

Textile and apparels alone employs almost 10 Mn people

Vehicle for transport /logistics

Small fleet owners account for over 70% of the market

Hospitality

There are 3.4 Mn people employed in 1.3 Mn hotels and restaurants

Education and allied institutions

The segment employs 2.7 Mn people

Travel and tourism

Expansion of e-visa scheme is expected to double tourist inflow

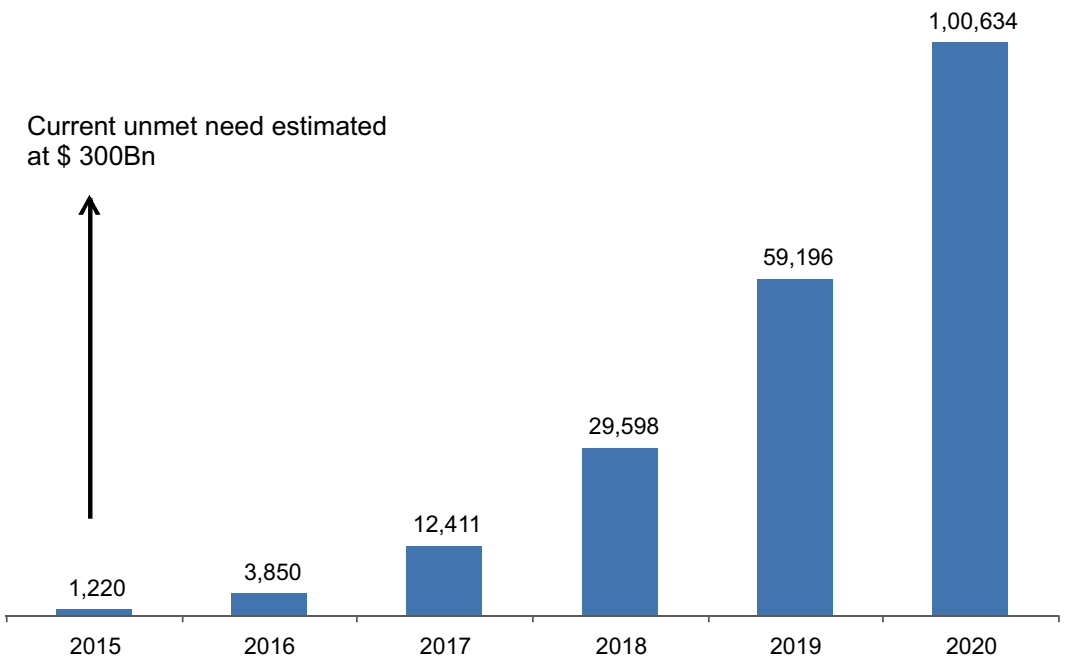
Start-ups

There is expected a 3x jump in Start-ups in India by 2020

Source: Ministry of MSME, NSDC, Assocham, Ministry of External Affairs, MXV Interviews

THIS COULD YIELD A $ 15BN OPPORTUNITY BY 2020

Projection of AUM under Fintech companies in India (Rs. Crores/year)



- This scenario envisages a 5% share for Fintech players in SME lending in 2020
- In 2015 in the US, Alternate Lenders originated about 4% of loans to small businesses, which is expected to increase to 20% by 2020

Source: MXV Analysis BI Intelligence, Interviews, Literature Review

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ALTERNATE LENDERS HAVE EVOLVED ALONG DIFFERENT PATHS IN THE US AND CHINA

- **Emergence of digital intermediaries and cloud enabled enterprise solutions**
  These new platforms often have greater visibility into business performance than banks
- **Availability and Monetisation of Digital Footprints**
  Explosion in mobile penetration and advent of big data leading to emergence of "non-traditional" data points
- **Shift in preferences**
  New customers no longer feel the need to physically interact with the service provider at a branch

This has created an opportunity for start-ups to attack and win share from banks in the SME lending space

OnDeck
fundera
Funding Circle
Kabbage
LendingClub
Biz2Credit

- In the US, a variety of models have emerged, notably, peer to peer models where individuals fund businesses requiring loans
- Alternate lenders initially targeted a narrow segment of SMEs and focused on a smaller set of services

蚂蚁金服 ANT FINANCIAL
WeBank 微众银行

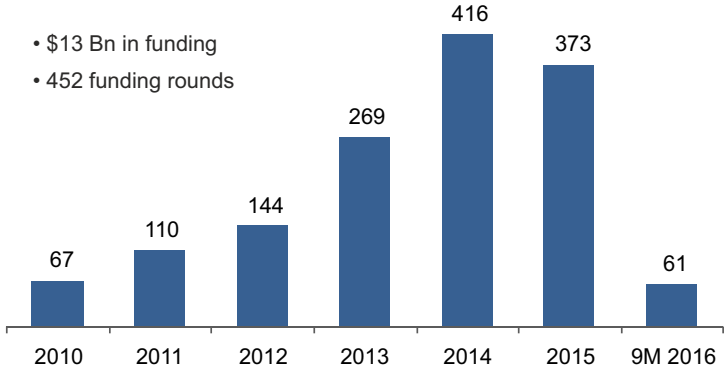
- Chinese SME fintech solutions emerged from digital intermediaries
- SME lending often formed a part of a broader solution provided by the parent organization, e.g; digital bank WeBank from Tencent and lending service Ant Credit from the Alibaba group

Source: MXV Research, Literature Review

MORE THAN 300 ALTERNATE LENDING COMPANIES FOUNDED EVERY YEAR

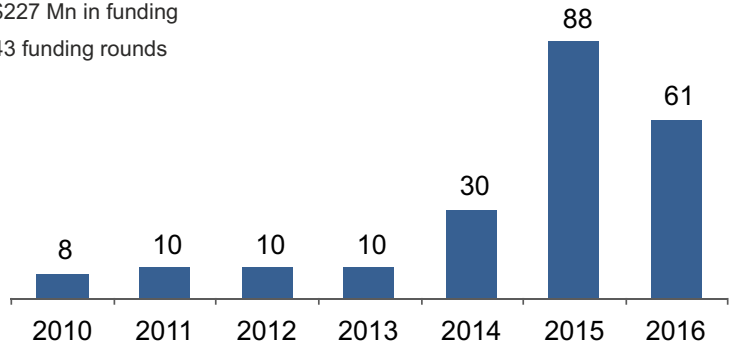
Number of Alternate Lending Companies Founded (Global)

- $13 Bn in funding
- 452 funding rounds

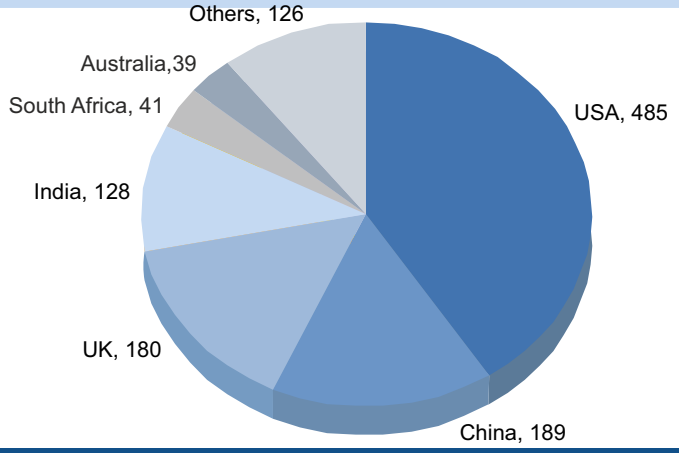


Number of Alternate Lending Companies Founded (India)

- $227 Mn in funding
- 43 funding rounds



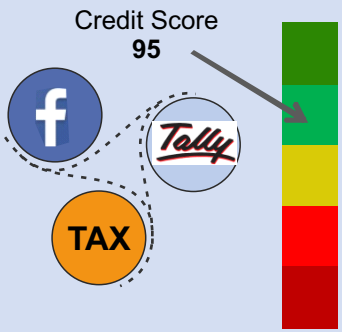
India has the 4th highest number of start-ups



Source: Tracxn

SME LENDING IS BEING TRANSFORMED

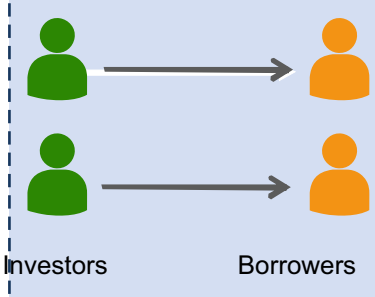
Use Of Alternate Data Sources & Automated Risk Assessment



- Several data points are drawn into the lending platform's automated underwriting mechanism where an algorithm assesses credit risk

Kabbage

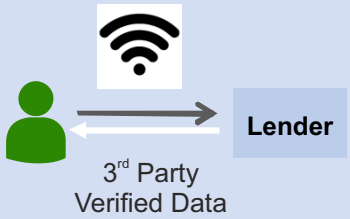
Increased Accessibility & Transparency



- In marketplaces, lenders and borrowers choose each other
- Investors benefit from diversifying risk across borrowers
- Borrowers are able to access unsecured loans, quicker

Funding Circle

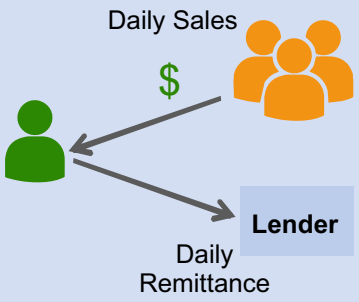
Improved Experience



- For the borrower, the process of applying is simplified, while disbursement and payment experiences are improved
- For the lender, the data is 3rd party verified
- For the lender, the data is 3rd party verified

Kabbage

Innovation In Collections



- SMEs can repay a portion of the loan advance as a % of transactions made that day

CAN CAPITAL

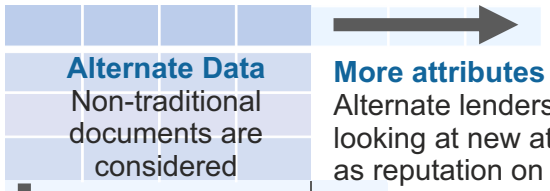
Source: Interviews, MXV Research

USE OF SMARTER DATA LEADS TO LEANER DOCUMENTATION REQUIREMENTS

Traditional Lenders Data

- Rating agencies like SMERA have limited data on SMEs
- Traditional documents such as balance sheet may not be available

Alternate Lenders Data



Alternate Data
Non-traditional documents are considered

More attributes
Alternate lenders are also looking at new attributes such as reputation on social networks

More Data
Through tie-ups with intermediaries, alternate lenders now have more data points

Traditional Lenders Documentation / Alternate Lenders Documentation

	Traditional Lenders Documentation	Alternate Lenders Documentation
Personal	• IT returns for 2 years • Assets & Liabilities Statements	• Personal bank statement for previous 12 months
Business	• IT returns for 2 years (business) • Balance sheet – 2 years • VAT/Sales tax return for 2 year	• Company bank statement for previous 12 months • Supporting documents such as invoice copy, receipts against payments, references • Cancelled cheque (for account details)
Collateral	• Original title deed & prior deeds for collateral • Land & building tax receipts • Possession certificate	• PDC (personal & business)

Source: Interviews, MXV Research, Literature Review

ADVANCED ANALYTICS HAS HELPED BRIDGE A RATING GAP

MODEL	RISK ASSESSMENT
TRADITIONAL	
Traditionally risk modeling used to be the preserve of large financial institutions Entrenched requirements and constraints leading to static models	Only a small set of SMEs has been rated by credit rating agencies Many have been excluded on a prima-facie basis
ENABLERS	
Cloud based infrastructures, more data and wide dissemination of modeling techniques have allowed alternate lenders to differentiate on the quality of risk assessment	Ability to isolate specific risks leads from having access to more granular and real-time data which give traditional “thin-file” applicants a better chance at availing affordable credit
ALTERNATE	
Newer risk models are dynamic and adopt machine learning to become smarter which is a significant advantage over traditional models which often required a change in processes and regulations which was more time consuming and left many out of reach of credit	Analytics and newer risk models being developed also give lenders the ability to better securitize their loans with low-risk bundling

Source: Interviews, MXV Research, Literature Review

THE DIGITAL ECOSYSTEM IS RIPE

E-commerce

Flipkart, amazon.in, Paytm

B2B market places

ofbusiness (order for. order from.), tradohub.com

Transport/logistics

OLA, SMART SHIFT (by Mahindra), UBER

Hospitality and tourism

via.com, OYO

Payment processors

mswipe, Pine Labs, PayU

Enterprise solution providers

intuit, taxspanner.com

- These partners provide alternate lenders with a captive market and better data for risk assessment
- The lending platforms help these companies expand their market by funding partner SMEs

Source: Interviews, MXV Research, Literature Review

DIGITAL INTERMEDIARIES PROVIDE 'DEEPER DATA' FOR RISK ASSESSMENT

Want more sellers / taxi drivers on their platform, and the sellers to offer more stock for sale

Require funds for working capital in case of e-commerce seller, or for the purchase of car in case of taxi operators

Digital intermediary

Flipkart | OLA | amazon.in

SME

E-commerce sellers | **Drivers on taxi aggregators**

Re-payments could be directly from the intermediary through deduction

Lending Start-up

CAPITAL FLOAT

LENDINGKART

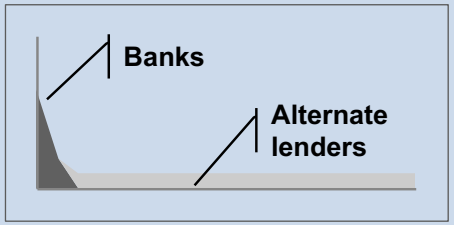
The digital intermediaries provide data on past performance and expected performance of SME partners

Alternate lenders use the data for risk assessment and provide funding to the SMEs

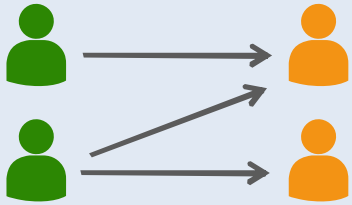
Want more 'quality' applicants for loans, and better data for risk assessment

Source: Interviews, MXV Research, Literature Review

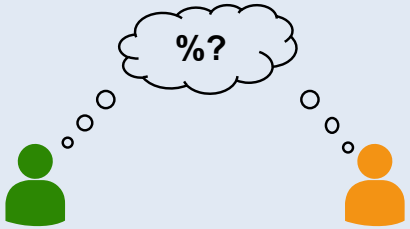
INCREASED TRANSPARENCY MAKE THESE MODELS ATTRACTIVE TO LENDERS AND BORROWERS



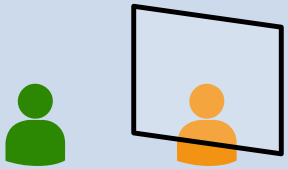
Increased access through long tail targeting
Alternate lenders have provided access to SMEs beyond those targeted by Banks



Increased availability of funds
Marketplaces tap individuals for funds, letting them partly fund a borrower, or fund multiple borrowers, spreading the risk



Rates and charges
Borrowers get clarity on the rates and on pre-payment; while the lenders get to set their desired risk group and lending rate

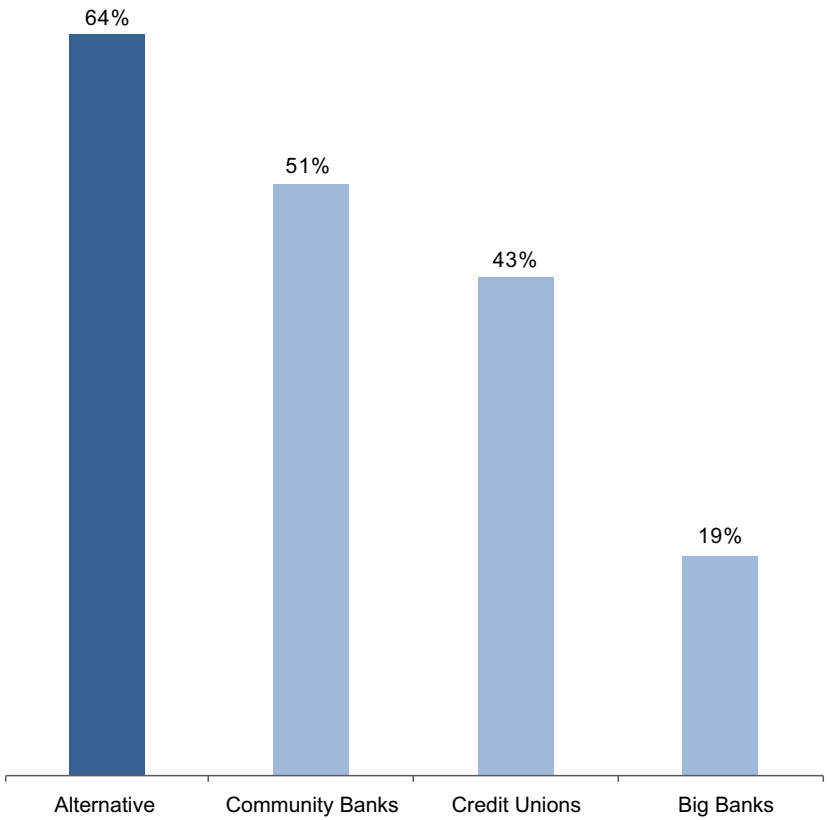


Visibility on the process and flexibility
Borrowers get better view of the state of the process, allowing them to shop elsewhere if the loan is being declined

Source: Interviews, MXV Research

WITH SUPPLEMENTAL DATA, ALTERNATIVE LENDERS SEEM ABLE TO TAKE MORE RISK

Approval Rate by Lender Type (US, 2014)



Source: HBS

THE LENDING EXPERIENCE HAS IMPROVED

Handholding & support
Informal and unregistered SMEs get support through a structured process that helps them establish their case

Verified data
Lenders get assurance of better data, and of more accurate risk assessment

Online process and e-signing
Online process, accepting scanned documents, and allowing e-signing / e-KYC reduces cycletime

Application → **Internal evaluation** → **Signing and closure**

Faster turnaround
Better risk assessment, and a simplified process with fewer physical touch points helps complete the cycle faster

Tracking
Real-time tracking and updates allow lenders to monitor borrowers' performance and to proactively manage risk

Lesser frustration
Lesser frustration from late-stage rejection

Source: Interviews, MXV Research, Literature Review

REDUCING PHYSICAL TOUCH POINTS AND SIMPLIFYING DOCUMENTATION HAS LED TO FASTER TURNAROUND TIMES

BANKS

SME Loan Process	6-27 days	Interaction
Application for loan	(1-2)	1x
Collecting documents from borrower	(1-12)	0-3x
Assessment	(3-12)	
Queries related to credit risk assessment*	(1-4)	0-4x
Discussion to understand business	(1-2)	1x
Reference check of supplier or customer*	(1-2)	0-3x
Final call on credit appraisal	(0-4)	
Disbursement	(1)	

Alternate lenders

SME Loan Process		2-7 days	Interaction
Online registration	(0+)		1x
Login creation			1x
Filling in the application form			
Document upload			1x
Discussion with credit officer *		(1-2)	0-4x
Basic terms sent to borrower		(0-3)	0-3x
Personal reference check		(1)	1x
Document pick-up		(0-1)	1x
Disbursement of loan			

Alternative lenders shorten the process time by at least 30%

Source: Interviews, MXV Research

* Optional

SEVERAL PLAYERS ARE INNOVATING IN COLLECTIONS

NeoGrowth
NeoGrowth Credit Pvt. Ltd.

- Provides loans to sellers on e-commerce platforms and to retailers with EDC/POS machines
- In both cases, the borrowers do not pay a fixed EMI, but instead pay a percentage of their daily revenues

State Bank of India

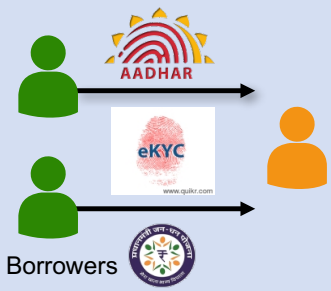
OLA | Chola Enter a better life

- SBI and Cholamandalam Finance have partnered with Ola to offer competitive loans to Ola drivers with the option of daily-repayment
- 20% of the driver's daily earnings is deducted towards the loan

Source: Interviews, MXV Research, Literature Review

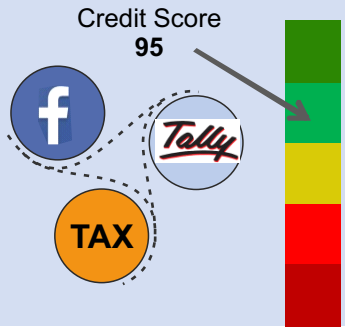
THE COST OF OPERATIONS IS SET TO REDUCE

ON-BOARDING SIMPLER AND COST EFFICIENT



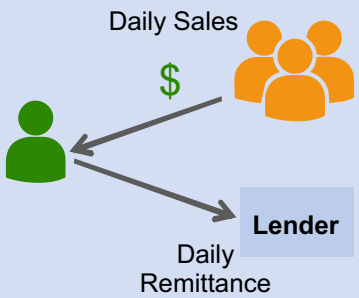
Availability of digital records through initiatives like Aadhar and
e-KYC have reduced the need for feet-on-the-street thus simplifying on-boarding and reducing the cost of acquiring a customer

COST OF UNDERWRITING MUCH LOWER



Digitization of data and use of non-traditional sources in risk models have led to shorter turn-around times and lower cost of underwriting through effective use of technology

INNOVATION IN COLLECTIONS



Efficiency in collections will lead to lower default rates, allowing lenders to reduce costs.

CASE STUDY: CAPITAL FLOAT

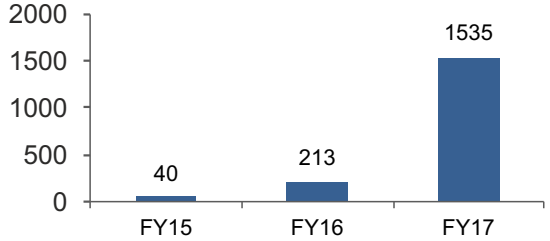
A Tech Company with Innovative Lending Models

- Founded in 2013 by Gaurav Hinduja & Sashank Rishyasringa
- Disbursed loans worth more than Rs 1,500 crores in FY 16 -17
- Widest product portfolio of finance options for SMEs in India: Pay Later, Taxi Finance, Online Seller Finance, Merchant Cash Advance, Supply Chain Finance, Unsecured Business Loan,
- Harnesses data and analytics to provide better lending solutions to both merchants as well as lenders
- Disbursed the quickest SME loan in India in under 90 seconds
- Hybrid Marketplace Model: Partnered with banks & NBFCs, co - lending aligns interests and maintains product discipline.
- Focus on Tier II & Tier III cities, besides Metros, to drive future business
- Raised $42 million in equity funding and $75 million in debt funding till date

Technology Just One of their Key Differentiators

Tailored Products	Broad and growing product portfolio, targets multiple under-served SME pockets, including micro-entreprenuers like taxi drivers and kirana store owners
Ecosystem Plays	Partnering on both the lending side as well as with platform partners has allowed rapid scaling and penetration
Hybrid Marketplace Lending Mode	Hybrid marketplace model enables co-lenders to achieve priority sector lending targets and provides Capital Float access to co-lender's funds.
Data Analytics	Data Analytics has played a big role in improving the acquisition and underwriting processes in particular

Total Disbursals



Note: Figures in INR Crores

Strength in Partner Ecosystem

Lending Partners

Platform Partners

Securitization Partners

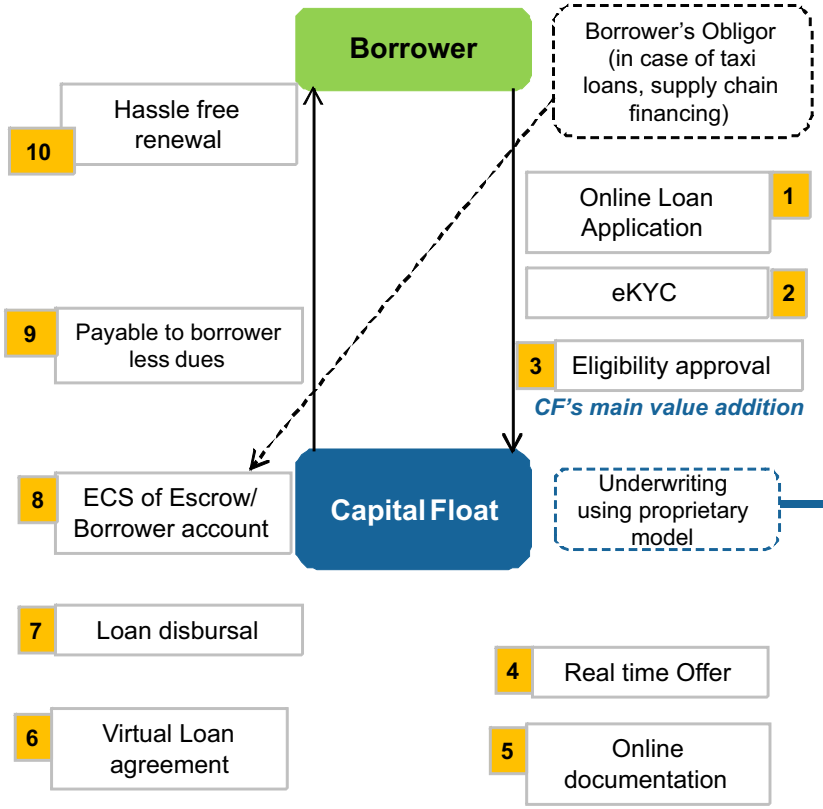
Repeat Investments in Follow-on Rounds

Date	Round	Amount ($ mn)	Lead Investors
May '14	Seed	4	Aspada, SAIF Partners
Feb '15	Series A	13	SAIF, Aspada, Sequoia
May '16	Series B	25	SAIF, Aspada, Sequoia, Creation Investments LLC

Source: Capital Float, VCCEdge

CASE STUDY: CAPITAL FLOAT

Technology and Tie-ups Underpin Core Processes of Underwriting, Disbursals and Collections



Loans on CF's hybridmarketplace, are co-lent with FIs ensuring skin in the game; while some loans are entirely on Capital Float's balance sheet

Source: Capital Float

Applicants Evaluated on Intent & Ability to Repay

Source	*Underwriting Enabler*
Partner tie-ups eg: Amazon, Uber	Financial stability, Professional behavior
Digital footprint	Social quotient
Machine Learning	Dynamic model
Financial Sources	CIBIL, Bank Statements, Ministry of Corporate Affairs

Selective Human Intervention Augments Machine Learning

Cost of underwriting at 30-40% of traditional lenders

Complexity	Type of loan – complexity of product/ fit to existing products
Human Intervention	
Value	High value loans are given human oversight

Majority of the loans are sanctioned through automation

NPAs <1%

CASE STUDY: FLEXI LOANS

Building Sustainable Scale with Smart Use of Machine Learning & Technology to Address Gaps in SME Lending

- Digital lending platform with a RBI registered NBFC that aims to solve working capital gaps of underserved SMEs through quick disbursal times and flexible repayment options
- Started in Apr '16 and has rapidly grown its user base with loans being disbursed in over 100 cities through 50+ partners like Amazon, Flipkart, Firstdata, Pinelabs etc
- Processes more than 3000 applications a month with average loan size of less than 5 lac (highly underserved segment in India)
- Have on-boarded reputed investors with long-standing industry experience - Sanjay Nayar (CEO, KKR India), Vikram Sud (ex-COO, Citi Asia Pac.), Anil Jaggia (ex-CIO, HDFC Bank), Narayan Seshadri (ex-head, KPMG India)
    - Raised USD 15 mn in October 2016
- **Well Diversified Products Mix:**
    - Term Loans
    - Line of Credit
    - Invoice Financing – Payable & Receivable
    - POS Financing
- **Strategy:**
    - 100% digital acquisition and processing
    - Uses technology and robotic process automation (RPA) to enable faster turn-around times and dramatically reduces the need for feet-on-street
- **Road Ahead:** Supply Financing for SMEs (acquired CreditPeriod, a supply chain financing platform), Co-lending arrangements with banks and NBFCs, Leadership in key segments

Hurdle		FlexiLoans Approach
Cumbersome Online Forms	→	'Tap, Snap & Swipe' approach to mobile app interface; data parsing through uploaded photo
Complicated lenders and policies	→	Chatbots for online connect; vernacular language support for app and call center
Patchy and incomparable bureau scores	→	Develop multiple scoring models - Trust Score, Cash Flow Score, Social Score, Digital Score, Psychometric score
Backtesting of Underwriting Model	→	Back testing done on historical user database from Bureau, banks etc

Bolstered by Differentiators Unique to FlexiLoans

Founders bring diverse experience	Founders bring 45+ years of unique experiences across financial services (Axis Capital, Aditya Birla Money), start-ups (Housing.com), and Data Science (Fractal Analytics)
Industry Stalwarts as Investors	Marquee investors bring invaluable experience and can potentially facilitate access; Suggests confidence in the business model and the team's capabilities
Applied and contextual Data Science	Backtesting on historical data and Machine Learning improves the learning curves of credit models and brings down the time-to-market of new products

Source: FlexiLoans Management

SEVERAL INDIAN PLAYERS HAVE EMERGED ALREADY

Aggregator

- rubique
- Biz2Credit
- CoinTribe
- indifi
- NAMASTE CREDIT – Jumpstart Your Dreams
- kredX

P2P

- FAIRCENT – EVERY % COUNTS
- LOANZEN
- RXchange – An Alternative Lending Platform – www.rupaiyaexchange.com

Balance Sheet

- NeoGrowth – NeoGrowth Credit Pvt. Ltd.
- LENDINGKART
- FLEXI LOANS
- CAPITAL FLOAT
- ZipLoan™
- NAB

- Marketplace models have seen significant interest from start-ups
- While most incumbents began as market-place lending platforms, many of them have turned to lending off their own balance sheet or a hybrid lending which straddles both models
- This interchangeability is likely to remain a feature of the online lending space as it evolves, giving its incumbents avenues of flexibility and risk mitigation

Source: MXV Research, Literature Review

THREE BROAD BUSINESS MODELS PREVALENT

	Aggregator	P2P	Balance-sheet
Model	Borrowers can approach several lenders via a single platform	Connects borrowers and lenders, who can be individuals or corporates	Uses balance sheet capital to fund the loans after algorithmic assessment of risk
Loan size	Rs 1 Lakh – 5 Crore	Rs 1-50 Lakh	Rs 1 Lakh – 1 Crore
Source of funds	Financial institutions	Investors (corporate or individual)	Debt or equity raised by platform
Interest rates	16-22%	Set by lender or reverse auction	18-24%
Terms	Upto 3 years	Upto 3 years	1-12 months
Processing fee	Free / 1-2%	Free (with charges for additional services)	2%

Source: Interviews, MXV Research, Literature Review

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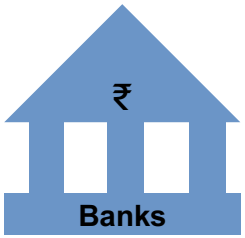
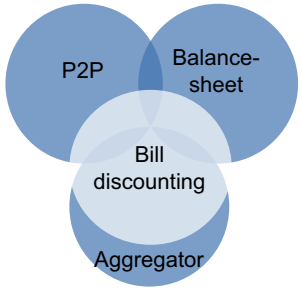
COMPETITION BETWEEN ALTERNATE LENDERS AND BANKS WILL CHANGE THE OPERATIONS OF BOTH

BANKS



- Increasing their focus on SMEs
- Will increase investment in technology
- The overall customer experience will improve
- Will adopt techniques from alternate lenders to become more relevant in this space

ALTERNATE LENDERS



- While volumes are exploding, customer acquisition costs remain high
- Larger customer base will help alternate lenders improve their risk assessment capabilities
- As SME organizational hygiene improves, less time and effort will be spent on handholding services

COLLABORATION

- Banks will directly or indirectly co-opt alternate lenders
- Banks and other NBFCs will use alternate lenders as an additional channel, reducing customer acquisition cost for both
- Data could be shared with alternative lenders that provide risk assessment
- Mixed model service providers will arise that provide broad financial services with low physical footprint

Source: MXV Research, Literature Review

BEWARE OF THE INCUMBENTS: BANKS CAN FIGHT BACK

Globally, Citibank has started 'Citi Fintech', a small team of former technology and banking employees, to create a smartphone centric business model.

Indian banks have had time to prepare

The earlier advances across the globe have demonstrated how quickly banking services can be unbundled and provided at lower cost by start-ups

Case study: State Bank of India (SBI)

State Bank of India

OLA

SBI, along with Cholamandalam Finance, have tied up with Ola to provide loans to drivers

snapdeal.com

SBI has tied-up with Snapdeal to provide working capital to the sellers on the Snapdeal platform under SBI e-Smart SME program

SBI InCube
Nurturing Ideas. Empowering Growth.

SBI has created a specialized branch to meet the specific requirements of startups

SBI has specialized products for segments such as Doctors (DoctorPlus), Schools (SchoolPlus), Women Entrepreneur (StreeShakti), etc.

Source: Company reports, Techcrunch, Literature Review

CASE STUDY:
BANK OF CHINA'S "CREDIT FACTORY" FOR SME LENDING

- "Credit factory model", pioneered by Singapore's Temasek Holdings, applies standard factory procedures to SME lending
- Reduced number of management layers involved in approval of a loan from 10 to 4
- Reduced time taken to process loan applications from months to 4 business days
- More than 200,000 SMEs served
- Default levels comparable to larger corporate loans

However, even this improvement needs to be seen in the context of Kabbage in the UK, which claims a 1-day-to-fund process, with decision shared with the applicants within a few minutes

Source: WEF ADB, Santander

START-UPS ARE SPENDING TO DEVELOP DATA ASSETS, INNOVATE AND EXPAND THE MARKET

Technology First

LENDINGKART

LendingKart planned to use the $32 Mn Series B round in June 2016 to strengthen data science capabilities, enhance technology platform, and infrastructure for improved mobile capabilities.

Data Assets

NeoGrowth
NeoGrowth Credit Pvt. Ltd.

NeoGrowth uses records of card transactions on from PoS/EDC machines to understand the repayment ability of retailers looking for a loan.

Agile Systems and Processes

LENDINGKART

LendingKart can make disbursals immediately after the photographs of the signed documents are sent for processing by the field executive.

Handholding and Market activation

kredX

KredX provides handholding support to potential borrowers at the early stages of the loan process in order to bring traditionally difficult to service customers into the fold

Source: MXV Research, Literature Review

GLOBALLY THE OLD AND THE NEW ARE COLLABORATING

JPMorgan Chase & Co. ondeck

In 2015, JP Morgan Chase tied up with Ondeck to provide small ticket business loans off the bank's balance sheet using Ondeck's underwriting model to process these loans

BancAlliance FUNDATION

In US, BancAlliance, a network of 200 community banks, has tied up with Fundation to use Fundation platform to offer co-branded loan solutions for SMEs.

Kabbage KIKKA CAPITAL

Kikka Capital launched a small business lending solution using the Kabbage platform, where Kabbage provides the technology for onboarding, underwriting and monitoring.

网商银行 MYbank

MYbank , an Ant Financial business, services suppliers on Alibaba (to which it is affiliated) by using financial projections shared by Alibaba.

State Bank of India

SBI has launched the e-Smart SME e-commerce Loan, which uses proprietary data and public information to asses credit worthiness

Source: MXV Research, Literature Review

THE INDUSTRY IS MOVING TOWARDS CO-LENDING

- Banks and traditional NBFCs are increasingly tying up with Lending Platforms to access new segments and to benefit from the innovations in analytics and credit scoring
- We see greater trend of banks and Lending Platforms co-lending to the borrower. Increasingly, banks insist on co-lending by the Platform to keep their skin in the game and align interests.
- We think this is beneficial for the Lending Platforms as well - it stimulates the participation of banks on their platforms and allows them to build size and scale with limited capital resources.

For Banks/NBFCs	For Lending Platforms
✓ Opens up new customer segments which were hitherto unserviceable as per their risk framework	✓ Platforms get an opportunity to build-up their AUM without deploying significant capital
✓ Innovative Credit Scoring: Banks benefit from innovative credit scoring solutions which the platforms make available	✓ Allows the platform to monetize upfront cost in product/tech development through fee income
✓ Risk-Alignment: Aggregators typically are co-lenders (and some have first-loss guarantee provisions) - ensures that interests of the bank and the aggregator are aligned	✓ Banks have a lower cost of funds – platforms are able to pass on the benefit to customers for higher market-share
✓ Benefit from the overall reduction in operating costs vis-à-vis their traditional business	

We see the industry gravitating towards a hybrid between Aggregators and Balance Sheet based models

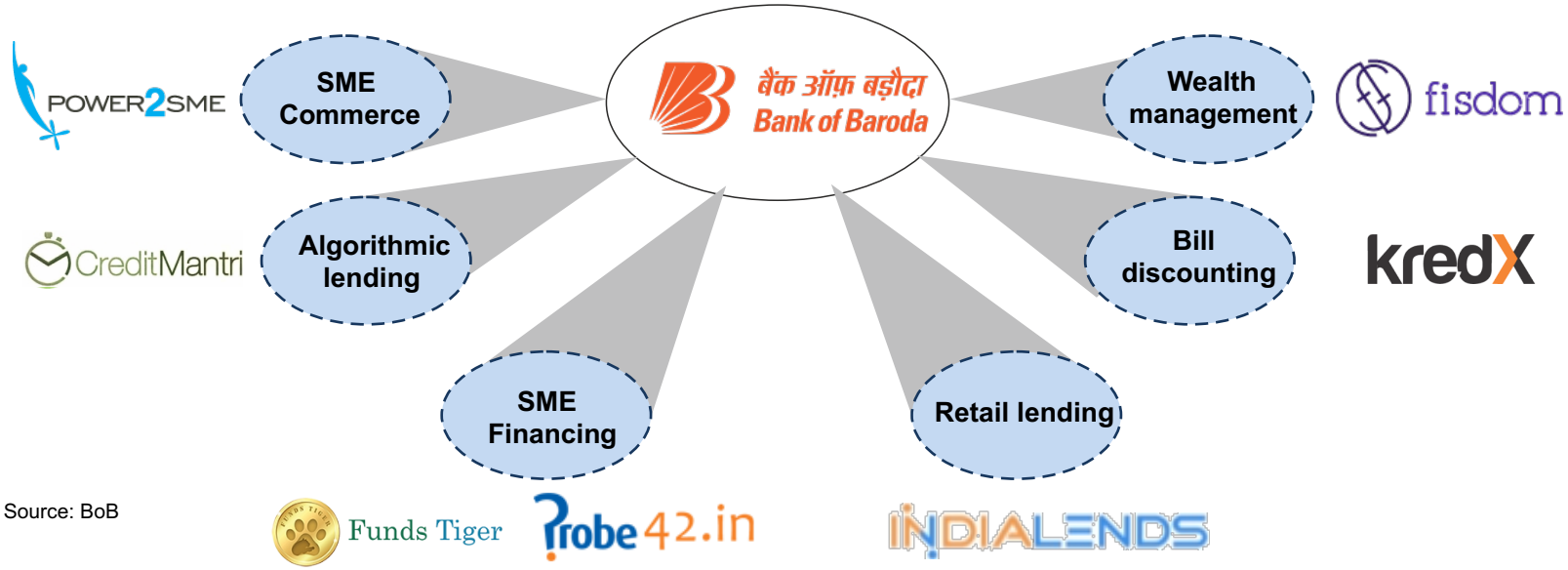
CASE STUDY:
BANK OF BARODA TIES UP WITH MULTIPLE FINTECH COMPANIES

"Our industry is going through a transformational phase... These tie-ups would help in expanding our business faster and reach out and support the customers in a better way."

P.S. Jayakumar
MD and CEO, BoB

"These partnerships will open windows for value additions in terms of better due diligence, better marketing opportunities and speedier service delivery."

B.B. Joshi
ED, BoB



Source: BoB

LOOKING AHEAD

RAPID PROLIFERATION	Strong demand and strengthening digital ecosystem, investor interest and bank willingness to participate in Fintech are lowering entry barriers – Expect to see a rush of new companies in SME lending
AN INDIAN TWIST .. OR TWO	Demonetisation is a game changer and massive accelerator for Fintech companies in India. With SMEs struggling for funding, this is the opportunity of a lifetime for alternate lenders. Keep an eye out for regulations.
SLOW INTERNATIONAL EXPANSION	Regulatory and partnership requirements are country specific – limiting the speed of internationalisation. Having said that, Amazon and Uber have had the same barriers to entry – and they haven't done too badly in India.
A MUDDIED FIELD	The presence of startups, banks, NBFCs and government – all make for a complicated ecosystem. Partnerships and specialisations with emerge rapidly – making it harder to read the field as time goes by.
THE CUSTOMER FINALLY RISES	SMEs may finally get the financing support that they have craved. Most importantly, the processes with get easier and more transparent – and the cost of credit will decline.
WINNERS AND LOSERS	With low entry barriers, differentiation will soon become critical. Besides the obvious – access to funds and customer acquisition costs – winners will have a straight-through digital process, that integrates with their deep analytics capabilities to develop segment specific strategies and risk assessment capabilities.

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INDIAN FUNDING SCENARIO

Company	Date	Investors	Primary Amount (INRCr)	Post-Money Price/Book Multiple
CapitalFloat	May-16	Creation,Sequoia,Aspada,SAIF	170	3.2x
	Feb-15	Saif, Aspada,Sequoia	78	2.2x
	Jul-14	Saif, Aspada	18	2.6x
LendingKart	Jun-16	Bertelsmann,Darrin,Mayfield, Saama,IndiaQuotient	132	2.7x
	Jun-15	Mayfield,Saama,IndiaQuotient,AshvinChadha,ShaileshMehta	38	2.5x
	Feb-15	Saama,IndiaQuotient, Ashvin Chadha,Ashish Goenka	4	2.0x
NeoGrowth	Jun-16	IIFLSeed, Omidyar Networks,KhoslaImpact, Aspada, Accion	107	3.3x
	Jul-15	Omidyar Networks,KhoslaImpact, Aspada, Accion	45	2.6x
	Jun-14	Aspada	18	1.2x
	May-13	Omidyar Networks	17	2.0x
Indifi	Nov-16	Accel, Elevar, Omidyar Networks	68	2.3x
	Aug-15	Tracxn, Elevar, Accel	33	3.1x
Rubique	Oct-16	Kalaari	18	4.2x
	Sep-15	Yournest,Globevestor,DextorCapital,KalaariCapital	20	3.1x
KredX	Oct-16	PrimeVenture,Sequoia	42	NM
	Sep-15	PrimeVenture	3	4.6x

Capital Float, LendingKart and Neogrowth stand out as the most well funded companies in size as well as number of funding rounds

Company Filings, MAPE Analysis

PROFILE: LENDINGKART

Company Overview

- Founded in 2014 by Harshvardhan Lunia and Mukul Sachan, LendingKart provides SMEs with short term working capital loans

  Set up its own NBFC arm to disburse loans with a focus on the e-commerce segment targeting sellers in need of supplier loans that help them avail cash discounts
- Disbursed over Rs 400 crore through 5600+ loans in 397 towns

  Ticket sizes range from Rs 50k-10 lakh with tenures from 1-12months depending on the turnover of the borrower

  Customers can repay either bi-weekly or monthly and collections are handled through automatic debit or NACH
- Minimal offline presence with no regional branches; operate out of 3 nodes in Ahmedabad, Mumbai and Bangalore

  Acquired KountMoney, an online lending marketplace, in Oct '16 to find synergies in technology, data analytics and service capabilities

  Raised over $40mn in funding over 4 rounds from VCs through debt and equity

Funding

Date	Round	Amount ($ mn)	Lead Investors
Feb '15	Angel	1	India Quotient Fund, Saama Capital
Jul '15	Series A	10	Saama Capital, Mayfield
Jun '16	Series B	32	Bertelsmann, Darrin Capital
Apr '17	Debt	5	Anicut Capital

Key Metrics after First Year of Operation (FY16)

Portfolio Size	INR 493 Mn.
Interest Income	INR 60 Mn.
Processing Fee	INR 10 Mn.

Source: Company Reports, Literature Review

Partnerships/ Tie-ups

flipkart.com | amazon.in | paytm

PayU | voonik.com | SMART SHIFT by Mahindra BUSINESS KO LIFT KARO

PROFILE: NEOGROWTH

Company Overview

- Started in 2010 by Dhruv and Piyush Khaitan (Venture Infotek), NeoGrowth provides short-term business loans to SMEs
- Focuses on e-commerce sellers and small businesses with EDC/ POS card swipe machines
- Type of loans range from Micro, which are typically of Rs 2-10 lakhs ticket size and 6-8 month tenure to Elite/ Signature loans which go up to Rs 1 crore in ticket sizes and 12-24 month tenure
- Flexible repayment terms based on credit/ debit card sales of the merchant
- NeoGrowth loan funds typically support retailers' expansion, renovation, one-time equipment purchases, or large seasonal inventory purchases
- Company claims on an average 3 in 4 customers return for a new loan
- Claims to have disbursed Rs 600 crore of loans as of July '16 through over 4000 loans
- Provisioning maintained stably below 2% of book size
- Raised close to $30mn in capital through equity and close to $50mn through private debt placements

Funding

Date	Round	Amount ($ mn)	Lead Investors
May '13	Series A	3	Omidyar
Mar '14	Series A	2	Aspada
Mar '15	Series B	7	Omidyar, Aspada, Others
Jul '16	Series C	16	IIFL Seed, Accion, Omidyar, Aspada

Key Operating Metrics (INR Mn.)

	FY14	FY15	FY16
Portfolio Size	42	470	2402
Interest Income	7	56	411
Processing Fee	2	12	73

Source: Company Reports, Literature Review

Partnerships/ Tie-ups

OPIC, RBL BANK, IFMR Capital, Flipkart, amazon.in

OTHER INTERESTING LENDERS

kredX

- Founded in 2015, KredX helps SMEs avail working capital finance by discounting unpaid invoices
- Raised $7mn from Prime Venture Partners and Sequoia in 2016
- Acquired US based Hummingbill for technology that allows automated tracking of invoices and cash-flow management

KNAB FINANCE

- NBFC founded in 2015 that focuses on short term loan products for SMEs that can be between 7 days – 1 year with a average ticket size of 8 lakhs
- Founded by seasoned professionals with experience from Barclays Bank, Mindtree and HSBSoft

indifi

- Founded in Oct 2015, Indifi is a marketplace for MSME loans
- Focuses on travel, hotels, e-commerce and retail segments for now
- Founders bring a good mix of entrepreneurship, risk and technology.
- Raised USD 10 mn from ON, Accel and Omidyar in Nov 2016

CoinTribe

- Online lending marketplace that connects SMEs with banks and NBFCs
- Targets SMEs with Rs 1-15 crore in turnover
- Raised $3mn in seed funding from Puneet Dalmia (MD, Dalmia Cements)
- Tied up with SMERA Ratings to provide technology driven services of CoinTribe to SMERA-rated SMEs

INCRED finance.com

- Founded in Aug '16 and backed by Anshu Jain (former Deutsche Bank CEO)
- Raised $75mn from Alpha Capital, IDFC PE, Anshu Jain, Gaurav Dalmia & others
- Acqui-hired Instapaisa using the funds raised
- Disbursed Rs 100cr of loans to about 1000 customers in less than 100 days
- InCred offers loans for four categories including home, consumer, education and SMEs

ZipLoan™

- NBFC and tech enabled platform that provides SMEs loans between Rs 1-3 lakh over a period of 6-24 months
- Also partnered with other NBFCs for co-lending using its tech platform
- Raised an undisclosed amount in seed funding from GrowX Ventures, Sarbvir Singh (MD, Network 18 Media) and Arun Venkatachalam (Murugappa Group)

GLOBAL FUNDING SCENARIO

Company	Country	Date	Recent Round	Amount ($mn)	Lead Investors	Total Funding ($mn)
Biz2Credit	USA	Dec '14	Series A	250	Direct Lending Investments	250
Ondeck	USA	Dec '14	IPO	200	Public	390
Kabbage	USA	Oct '15	Series E	135	Reverence Capital	239
Dashu Finance	China	Dec '15	Series B	77	PAG	93
ezBob	UK	Mar '16	Series C	20	Oaktree Capital	38
Licaifan	China	Apr' 16	Series C	51	Yingda Investment	85
SpotCap	Germany	Jun '16	Series C	14	Rocket Internet	66
Behalf	USA	Aug '16	Series C	27	Viola Growth, Sequoia, Spark	156
FundingCircle	UK	Jan '17	Series F	100	Accel	374

Source: MXV Research

ABOUT

- **MXV Consulting** (www.mxv.in) is a strategy and management consulting firm based out of Bangalore in India. Our focus is on building sustainable competitive advantage for our clients and helping them become industry leaders

- We have the experience of working across multiple industries and functional areas - enabling us to bring in fresh ideas and a strategic perspective to every engagement. Our insights are backed up by a rigorous process of analysis and solution development. This ensures that our recommendations are well researched, practical and tailored to an organisation's requirements. In many instances, we also take on the role of implementation managers

- Our clientele includes leaders across various industries. We believe in long term relationships with our clients, and have worked on multiple engagements with most of them

- MXV has worked on more than a 175 assignments till date. Our clients are global in nature – including India, the US, Middle East, Europe and Asia Pacific

- In 2014, MXV Consulting was listed among the most promising business consultants in India

- **MAPE** was founded in 2001 by ex DSP Merrill Lynch senior bankers as an investment bank focused on M&A advisory and Private Equity fund raising

- MAPE has an excellent deal track record having successfully closed over 180 transactions, across sectors, totaling to a deal size of over US$ 5 Bn (approx.)

- MAPE is present across 3 cities:
  - Mumbai
  - Bangalore
  - Chennai

- MAPE has been consistently ranked amongst the top 10 investment banks in the country (per Bloomberg league tables) for the last 13 years (CY2002 – CY2014) and was awarded the Boutique Investment Bank Of The Year Award at the India M&A Atlas Awards 2012

- Leading clients who have closed signficant M&A / PE transactions include Tata Sons, Dr. Reddy's Labs, Goldman Sachs, Godrej Consumer, Blackstone Group, Mahindra, Wipro, Café Coffee Day, CRISIL, Star Health Insurance, Glenmark Pharmaceuticals and Jyothy Labs amongst others

Authors of this report		For further discussion, please contact	
MXV Consulting	**MAPE Group**	**Amit Garg** Bangalore amit_garg@mxv.in	**Jacob Mathew** Bangalore jacob@mapegroup.com
Amit Garg	Jacob Mathew	**Shalabh Agrawal** New Delhi shalabh_agrawal@mxv.in	**Abhishek Gupta** Mumbai abhishek.gupta@mapegroup.com
Dhritiman Borkakoti	Abhishek Gupta	**Kim Bingham** New York kim_bingham@mxv.in	**Prabodh DP** Bangalore prabodh@mapegroup.com
	Prabodh DP		