



## HOW STARTUPS IN INDIA ARE BECOMING HARBINGER OF INNOVATIVE FUNDING FOR MSMEs

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**Abstract:** The objective of this study is to find out how Startups are contributing in building a new India by providing funding to MSMEs by adopting innovative and customized modes of funding. The study focusses on two “Startups” which have gone beyond traditional ways of funding and have been successful in covering untouched methods of lending such as lease based asset financing and collateral free lending. Both these startups have shown the way by going beyond dotted lines.

The research analyses business models of these startups and how they have performed until now and what is the contribution made by these startups in MSMEs funding ecosystem. The methodology used in the research revolves around data analysis available regarding these companies, customer experience and interaction with owners of the business in online and offline mode. Various business news published regarding these companies have also been used in this report.

Finding of the study shows that funding in India has moved away from the traditional lending methods but is yet to pick up in a big way. Traditional players still dominate the market but these startups are signaling arrival of a new era in lending. Usage of technology for lending and providing support to MSMEs has acquired new dimensions in recent times and there is no doubt about it. The idea of government of India to promote startup seems to have paid off as business run by these startups are flourishing.

**Keywords:** Startups, MSMEs, Collateral free lending, Fintech, Government Schemes, Leasing, Capital requirement

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**Introduction:** Micro, Small and Medium Enterprises (MSMEs) play a key role in the Indian economy. The criticality of the role of MSMEs lies not just in the fact that they contribute significantly in India’s GDP size and its growth, but also in employment generation, which is one of the most pressing requirement

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that our economy has today, given the fact that the population of our economy has been rising at a fast pace. Role of MSMEs in taking Indian economy to the next level has always been recognized by the Government of India and various state governments. No wonder, the governments, at both center and states, has rolled out many program for MSMEs ranging from training for MSMEs, grant of subsidies for various schemes, marketing schemes and technological assistance for the sector etc.

**Government schemes MSMEs:** There is no need to exaggerate that for MSMEs to grow, the first and the most critical requirement is availability of capital, which should be made available at a cheap cost as well. Using the financial system comprising of nationalized banks, private sector banks and institutions like SIDBI the government has rolled out various lending schemes from time to time. An institution called CGTMSE was set up 17 years back, to help provide collateral free loan to MSMEs. As per website of CGTMSE ,”The main objective of CGTMSE is that the lender should give importance to project viability and secure the credit facility purely on the primary security of the assets financed. The Credit Guarantee scheme (CGS) seeks to reassure the lender that, in the event of a MSE unit, which availed collateral free credit facilities, fails to discharge its liabilities to the lender, the Guarantee Trust would make good the loss incurred by the lender up to 50/75/80/85 per cent of the credit facility.”

CGTMSE was helpful in providing loans to many MSMEs as member lending institution felt secured by the guarantee that is provided to them. However, considering the size of MSME sector, it probably could not achieve desired results to the extent it was required.

When a new government was formed in the month of May 2014 led by Prime Minister Mr. Narendra Modi, it was thought MSMEs in India would need funding which should be available easily to them. With easy availability of capital to MSMEs in mind, the current government

started a new entity called as “MUDRA”. Micro Units Development and Refinance Agency Ltd. [MUDRA] is an NBFC supporting development of micro enterprise sector in the country. MUDRA provides refinance support to Banks / MFIs for lending to micro units having loan requirement upto 10 lakh. MUDRA provides refinance to micro business under the Scheme of Pradhan Mantri MUDRA Yojana. Under the aegis of Pradhan Mantri Mudra Yojana (PMMY), MUDRA has created products / schemes. The interventions have been named 'Shishu', 'Kishor' and 'Tarun' to signify the stage of growth / development and funding needs of the beneficiary micro unit / entrepreneur and also provide a reference point for the next phase of graduation / growth to look forward to :

Shishu : covering loans upto 50,000/-

Kishor : covering loans above 50,000/- and upto 5 lakh

Tarun : covering loans above 5 lakh and upto 10 lakh

It is also important to note that the maximum credit facility available under CGTMSE scheme was enhanced from Rs. 1 crore to Rs.2 crore.

**Challenges faced by MSMEs in raising capital:** In spite of the efforts made by various governments at Center and States in India, MSMEs still found it challenging to avail loans from traditional banks and financial institutions. Some of the key reasons behind this, are:

- Inability of MSMEs to provide requisite collateral to borrow money because most of the MSMEs are individual owned and do not have sufficient collateral with them. Collateral based lending is preferred by the banks as it reduces risk and also reduces requirement of capital.
- Challenges related to documentation, as banks and financial institutions insist on documents as per standard compliance requirements and it has been found that MSMEs don't have some documents especially documents detailing financials of business and cash flows.

- Traditional banks and financial institutions are mostly not open to new ideas of business, which has growing very fast recently. Businesses have turned unconventional and move away from brick and mortar model.
- It is difficult to get customized solutions from banks and financial institutions for loan requirements, which can be very specific to a business. For example, lease financing for acquiring an equipment on lease is not available as a product offered by many traditional financial institutions.

#### **Need for funding by Startups**

• Startup is the new buzzword in Indian economy these days. Over a period of last couple of years, startups have grown rapidly in India. However, most people confuse startups just an online technology company offering various kinds of solutions. Department of Industrial Policy and Promotion (DIPP) has defined startup. While the definition focusses on investment parameter as well as the timeframe for which a business has been in existence, the crux of definition in the nature and scope of activities that startups should do. As per the definition startups should be Working towards innovation, development or improvement of products or processes or services, or if it is a scalable business model with a high potential of employment generation or wealth creation. Having looked at the basic understanding of what is a startup, let us look two interesting startups who are funding MSMEs in India and how that is helping MSMEs grow. The first startup is that is being covered is “Origa Leasing” and the second one is “Capital Float”. Origa and Capital Float are fulfilling two different requirements of MSMEs, which a typical traditional lending institution generally does not do. While Origa provides equipment financing through lease, Capital Float provides collateral free loans.

#### ORIGA Leasing: India’s first innovative equipment leasing company

As mentioned earlier, capital is one of the key requirements for running a business. But a person running should also understand what is the adequate amount of capital that is required to run a business successfully because capital comes at a cost. For a business, which is just shaping up too much of investments in fixed asset is highly unwarranted because this is likely to block capital. Assets such as machines and equipments also face challenges related to depreciation, which reduces their value over a period of time. Looking at some of these constraints, ORIGA Leasing provides a solution for MSMEs in India, which has been until, recently was more of a western idea than reality.

**How ORIGA is different from traditional mode of funding:** As per a report available on [www.inventiva.co.in](http://www.inventiva.co.in) ,” ORIGA LEASING, is India’s first Fintech in equipment leasing. It is also India’s first leasing company to provide complete Asset Life Cycle Management (ALCM) – right from selection of the asset, to finance it, to maintain it and to recycle it at the end of the tenure. With its focus on Asset Life Cycle Management, clients can devote their entire focus on business and need not worry about asset. It provides a very innovative solution called Operating Lease. Through the leasing solutions, it helps the SMEs covert its capital expenses into operating expenses and thereby enjoy significant level of flexibility in financing its growth”.

Therefore, the details above give a clear insight into the fact that ORIGA is in the business of providing operating lease of assets, which means a business, which wants to acquire assets, need not block full money to buy assets, it can just pay the cost of lease and run the business. The second and equally important aspect of business model of ORIGA is that it only provides operating lease for revenue generating assets, which is very natural because repayment of lease amount is critical for business and hence non-revenue generating business will give rise to

non-payment risks. ORIGA currently operates in the western and southern region of India and focuses on boutique MSMEs, which are having healthcare setups and sub hundred and fifty crores revenues manufacturing companies. It leases between the ticket sizes of INR 2 million to INR 20 million for a tenure between 3 and 5 years.

Another important point that needs mention here is that ORIGA provides a hassle free borrowing experience for the customers, which is provided through online, offline, as well as mobile enabled platform. This is where the company is adding that missing connect with the customers which traditional lenders very often struggle to provide, But the most important thing that ORIGA brings to table is that it is changing the thinking that business owners typically have, And that is idea of owning assets. ORIGA is giving the message that owning an asset is not necessary to run a business.

**Corporate philosophy of ORIGA:** Corporate philosophy of ORIGA is manifested in three critical things, vision statement, mission statement and business model of the company. Mission statement of the company provides first insight into this. The mission statement of ORIGA is as follows, " Bridging the gap between new age businesses and traditional financing system and become their trustworthy partner throughout their journey of growth." Vision statement of the company further clarifies its corporate philosophy, which is as follows, " Provide asset financing solution to growing companies to fuel their growth, and in turn contribute towards building sustainable capabilities leading to job and income creation." Corporate philosophy of the company gets demonstrated further in the fact that the company is focused on providing hand holding to MSMEs by doing entire asset management on their behalf.

**Social relevance and feasibility of ORIGA:** ORIGA brings to table a new idea of lease financing for business, which essentially means a departure from the traditional lending

mechanism. It is also like to provide value to MSMEs by effectively reducing the need for blocking capital. The growing business of ORIGA and the funding that it has received over a period shows that the business model of ORIGA is feasible. Nothing sums up contribution made by ORIGA better than the statement which is as follows, "Financing through asset leasing for revenue generating assets creates capacities, capacities creates jobs and income, which finally goes towards contributing to the GDP of the nation".

**Capital Float: Fulfilling the need for collateral free lending:** The entire idea behind a new innovative startup doing funding of MSMEs can be understood by going through the mission statement of Capital Float, which is as follows" At Capital Float, we believe SMEs have 3 basic demands: simple access to credit, collateral-free terms and a trustworthy partner. Our mission is to bridge the current gap in the market with innovative and flexible credit products for SMEs, delivered in an efficient and customer-friendly manner."

The company describes itself as follows , " Capital Float is an online platform that provides working capital finance to SMEs in India. We offer flexible, short-term loans that can be used to purchase inventory, service new orders or optimize cash cycles. Borrowers can apply online in minutes, select desired repayment terms and receive funds in their bank accounts in 3 days with minimal hassle."

So what it is that Capital Float provides to MSMEs which traditional lenders typically don't provide. The USP of the company is the collateral free lending, which essentially means that a big headache of businesses, that is arranging collateral, is taken care of by the company. Arranging collateral is often considered as a bottleneck in launching and running businesses. However, it is important to note that the company does not encourage reckless borrowing. It has a series of processes, which are well defined and help borrowers to get the funding that they need. So, how does the

company access the borrowers that need to be funded? As per the website of the company, it

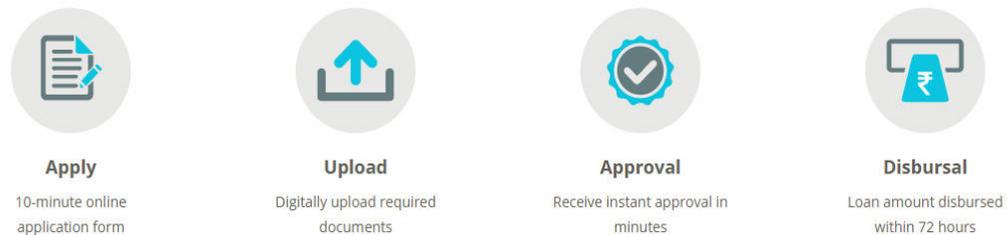
follows a process which is different from other types of borrowers and is as follows:

	Capital Float	PSU Banks	Private Banks	Traditional NBFCs	Money Lenders
Time to get funds	<1 Week	4-6 Weeks	1-2 Weeks	1-2 Weeks	<5 Days
Apply anywhere, any time!	Yes	No	No	No	No
Hassle-free documentation & processing	10 minute online application	3 months	1 week	Doc intensive	Unregulated

Source: Capital Float

To avail loan from Capital Float, any business must have an existence of atleast one year. The company provides loan for typically shorter-term period, which ranges from 1-12 months and does not fund for long term, which is obvious given the nature of lending.

**How Is Capital Float different from other lenders?:** Capital Float provides loan, which have a quicker processing time and have online assessment process, The online application process of the company is as follows as per the website of the company:



Source: Capital Float

Usage of technology for lending is hallmark of the company and the end-to-end automation in lending is how it reduces the time required to borrow funds.

has tied up with Amazon Business and Metro Cash and Carry from where a large number of merchants source their products.

This mechanism of online application makes application process streamlined and hassle free. However, what drives the lending process of Capital Float is much more interesting. As a company, Capital Float uses data acquired from different sources to take a quick decision on lending. As per a report published Capital Float

This becomes a data source for the company because it uses this kind of data for decision-making. As per a report in the Economic Times, Mr. Gaurav Hinduja co-founder of Capital Float had said “ “With the availability of data from these partner organizations and by quickly analyzing it through our technology platform, we can decide a credit amount for these

borrowers and actually disburse it within 5 to 10 minutes,”

He went on to add further, “Since most of these players do not have a CIBIL score, we have to rely on alternate data points for deciding their credit worthiness.” But Capital Float provides loan a higher rate of interest than most of the traditional lenders like banks and financial institutions do. The rate of interest is around 2%-3% more than what traditional lenders typically provide.

**Social relevance and feasibility of Capital Float:** Capital Float is providing loans to smaller business entities such as Kirana stores and other similar smaller MSMEs. This helps these businesses get an organized source of finance. The doorstep solution also makes the financing less cumbersome.

Capital Float has been growing as a business over the year, though it has been loss making till now. However, as it keeps on getting funds from various investors it is able to expand the business faster. As per the latest available data, having disbursed around 2,000 loans in September, 2017 across 20 to 25 cities, the lending startup plans to expand operations to 50 top cities of India and add 5,000 borrowers per month. Capital Float is targeting a loan book of Rs 500 crore in the next 12-18 months from the segment

**Findings and Conclusion:** The study of these two startups provide the following interesting findings:

- Startups in India are bringing disruption in the way which lending is done in India.
- They are creating scope for those borrowers who have felt marginalized in the existing lending ecosystem.

- These startups know the real issues that MSMEs face and have designed their offerings to take care of business requirements of MSMEs
- They are ready to take risk and expand market reach.
- MSMEs are gradually accepting them, which is reflected in business growth these startups have experienced.

There is a need to encourage these startups in India to help growth of businesses, especially MSMEs. Various stakeholders such as the government, industry bodies, capacity builders such as CAs, subject matter experts need to come together to help these startups grow further.

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