

India SGB Finance Learning Lab Webinar Series

“Demystifying Blended Finance”

Exploring Masala Bonds

9 Sep 2019 | 5:30pm IST

Part 1: Introduction to Masala Bonds

Speaker: Harsha Rawal, Chartered Accountant

About the Speaker:

Harsha is an experienced Tax Consultant with over 17 years' of domestic and international tax experience. Her experience encompasses a broad range of industries including infrastructure, healthcare, transportation and logistics, manufacturing, automobiles, financial- services, socio-economic venture funds, foundations. She has helped domestic companies and multinationals in developing appropriate strategies for setting up presence, international tax planning and restructuring and has closely worked with start-ups for their fundraising and their entry and exit structuring.

KEY TAKEAWAYS

Introduction

- We mostly hear of large organisations that raise money through masala bonds but they can be raised by smaller organisations as well
- Equity as an option (even for mature organisations) might not be suitable for working capital requirements.

Features

- Why are masala bonds not popular? Two broad reasons can be identified:
 1. Has been in use majorly by larger organisations
 2. The larger public sentiment is that private placement for masala bonds is not possible.

Advantages

1. Interest is tax deductible for borrowers/entrepreneurs. Tax rate is as low as 5%
2. From an Investor standpoint (the broader range of 5- 12%) return rate is much better than what can be normally seen in the US and Europe market
3. Eased out regulations and tax efficiency – for both people to fund into India or looking to raise funds in the country

Framework

- Companies which can take an FDI and Section 8 companies eligible to take masala bonds
- In general, the tenure of masala bonds is 3 to 5 years
- Does not take too long to structure, only initial research phase is time consuming. Can be designed and implemented in around 2-3 months

Closing remarks by the speaker

- INR ECB and Masala Bonds are both efficient financial instruments

Part 2: Understanding the feasibility from a social enterprise lens

Speaker: Abhishek Sen

About the Speaker:

Abhishek is a prominent social entrepreneur with a medical background (M.B.B.S., Medicine –TN Medical College and B.Y.L. Nair Ch. Hospital, Mumbai | MTech Bioengineering -IIT, Mumbai). Since 2008, he is the leading (CEO & Co-founder) Biosense Technologies Pvt. Ltd. which is a new age healthcare company, offering innovative and customer-centric POCT devices to B2B business segments through a knowledgeable team, effective technology, and robust processes.

KEY TAKEAWAYS

When do you raise money through a masala bond?

- Masala Bond being a debt instrument - an entrepreneur must have a **revenue generating model** in place that can service interest.
- If its a product based company- one has to be mindful of raising money through MB only after the product-market fit has been identified as risks would be significantly lower post that stage.
- If its a service based company – use when you have contracts in place but are not able to meet those requirements.
- Research and Development based expenditure is not encouraged to be funded through Masala Bonds
- Focus on the investor who are aligned to your mission – to meet working capital needs and also scale the growth of your enterprise

What other sources can be considered for entrepreneurs?

Source	Associated Pros and Cons
CGTMSE scheme	Con- Has an upper cap of upto 2 crores
Banks	Con- Require collateral besides current assets
NBFCs	In the absence of collateral, interest rates can soar upto 22% which can raise the constraints for entrepreneurs.

What advice can be given to entrepreneurs looking to raise money through Masala Bonds?

- The process takes 2 to 4 months but it's important to get advisors.
- Advisors that helped streamline the process for Biosense- Deloitte and AS(co)
- Possible foundations to also reach out to - Grand Challenges Canada

Part 3: The Investor perspective

Speaker: Prachi Windlass Jain and Sietse Wouters

About the Speakers:

Prachi Windlass Jain is a Director at Michael & Susan Dell Foundation India LLP. As a member of the leadership team, she manages a portfolio of start-ups, NGOs and large-scale government partnerships. Prachi is on the board of several for-profit education companies and advisory committees to state governments and education departments and has spearheaded the foundation's work in incubating service providers, creating role model states for classroom based assessments and embedding student learning based accountability in all portfolio companies. She has over 15 years of diverse set of operational and leadership experience in India and US.

Sietse Wouters is responsible for Social Finance programs at UBS Optimus Foundation focusing on financial, legal and operational aspects of programs. Most recently he has worked on the Utkrisht Maternal and Newborn Health Development Impact Bond (DIB) in India, the Quality Education India DIB as well as on various Impact loan programs. He is also actively engaged in broadening the foundation's ability to invest using other instruments such as equity and guarantees. Prior to his current role, he worked within UBS & Society, an umbrella platform within UBS Group, to grow the Bank into a leader in sustainable banking as well as within strategy development at UBS Asset Management.

KEY NOTES

Debt vs Equity and when?

Prachi Windlass Jain- MSDF

1. Working Capital requirement cannot provide equity based returns and preferably should be funded out of debt.
2. Special scenarios when debt is preferred over equity:
 - Specific projects linked to specific goals and outcomes
 - Medium to high risk projects

Sietse Wouters, UBS

- UBS Optimus Foundation- Primarily grantmaking-- pivoted to DIBs-- use equity and debt previously (looking to explore debt now)
- Social enterprises looking to raise money through debt- Impact narrative of the enterprise should be very clear

At what stage can debt be raised?

Prachi Windlass Jain- MSDF

- Stage: Late stage (predictable revenue stream to ensure debt can be raised), In case of an early stage company- companies or models familiar to the investors
- Diff between equity and debt funding – in debt, you have to be extremely confident in revenue streams of the company

Sietse Wouters, UBS

- Stage: Proven revenue form/ specific program with a specific impact narrative

How can investors use Masala Bonds to amplify impact?

- Create a structure on delivering on impact and linking that to the interest rate. If the outcome is achieved, we can reduce the interest rate.
- A good foundation of impact measurement and what those impact targets can look like

Part 4: Q&A session

Q1) Can an IOT cloud company raise money through Masala Bonds?

Yes, there is no end use or sector wise restriction on Masala Bonds. Working capital requirement is sector agnostic

Q2) What is the minimum size for the issuance of masala bonds?

There is no minimum size (\$100K) under the regulation. General range from Investors ranges from 2 crore to 4 to 5 crore

Q3) Big listed companies have ratings or connections with investors to say raise masala bonds. What provides confidence for small companies apart from third party due diligence and operational traction?

- Surety of revenue streams
- Financial due diligence looks more closely at Cash flow statement than just P&L account.

Q4) What is the difference between Rupee denominated ECBs and Masala Bonds

- Aug 2019 guidelines - INR denominated ECBs- Masala Bonds are more tax efficient

Q5) Is collateral needed in CGTMSE scheme?

- No collateral is not required but there is an upper cap of 2 crores and hence it cannot be used beyond this amount.

Closing Comments

- **Good option to consider at a stage (when you can service it)**
- **Finding a funder can be a challenge** and its **important to engage with an advisor** (the process is simple but cannot be run alone without an advisor's help)
- More Investors should consider Masala Bonds as the **transactional costs as well process time (2-3 months) are reducing.**
- **For investors** -Org/enterprise needs to adhere to business plan (diligence – involves contracts, past history of payments, cash flow more than PnL, in addition to the checks investor usually one does for equity funding)