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Malaysian Venture Capital Berhad (Mavcap): The Journey So Far (2001-2013)

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Abstract: In a knowledge-driven economy, economic growth is increasingly dependent upon technology entrepreneurship and growth of technology based firms (TBFs) whereby ability of these entrepreneurs to raise capital for commercial growth is a huge challenge that usually impedes development. However, the government of Malaysia has identified Venture Capital (VC) as being among the most vital technology financing mechanisms assisting research and development (R & D) activities, from encouragement of rudimentary scientific research to technology development and commercialization. The objective of this study is to review the activities of Malaysian Venture Capital Berhad (MAVCAP) from inception about 12 years ago and find out if the main purpose of establishing the organization has been achieved. The methodology adopted here is a single case study based on an in-depth review of empirical literature, newspapers, secondary data and document analysis of the activities of the case study organization. This study concludes that the main purpose of establishing the Malaysian Venture Capital Management Berhad has so far been achieved. Though there is room for improvement in certain areas which has already been identified by those in the helm of affairs.

Key words: Innovation · SMES · Commercialization · Technology Based Firms · Research & Development

INTRODUCTION

Venture Capital was encouraged to commence in Malaysia as a result of the rapid build-up of the national innovation policies in the country around the year 1990 by the Malaysian government through the Ministry of Science, Technology and Innovation [1, 2, 3]. The encouragement and development of innovation has passed through four phases ever since. The first phase (from 1957-1970) has been characterized by concentrating the researches on cultivation. The second phase (1970-mid 1980s) was marked by starting to build up university research facilities. Although foreign direct investments (FDI) existed, there is less indication that large flows of FDI had significant impact on the development of local technological capabilities in Malaysia [1, 4, 5]. From mid 1980s to 1990s, the third phase, the Malaysia government concentrated its effort on technology transfer by appointing the first science advisor to the prime minister and activating research within government owned universities [1, 6]. However, the rapid expansion of the economy in some countries has lead to the competitive nature of technology business activities in many countries [7-11]. Technology innovation plays a very vital role in developing economic growth through focusing on science and technology-based knowledge [5, 12] and has become an essential tonic for growth in both advanced and growing nations. Some of which are the root course of the slow pace of growth encountered in this sector, hence, the motivation of the researcher to carry out an in-depth study of this industry. In Malaysia and other part of the world, VC was acknowledged as being among the most important technology financing instruments supporting R & D activities, from boosting elementary scientific research to technology development and commercialization [2, 13-15]. Venture Capital which is described as independently managed, dedicated pools of capital that focus on equity and equity linked investments in privately held, high-growth firms, play an essential role in the emergence of new sectors by creating and supporting innovative firms which later dominate these industries [16]. The aim

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of this research is to conduct an in-depth study of the activities of the largest venture capital company in Malaysia and review empirical literature with the aim of seeing if the main reasons for establishing the organization have been achieved so far. This article shall discuss mainly the broad essentials of technology business financing and venture capital financing. The discussion will comprise of definitions of main terms and the relationships among the broad elements as found in previous researches. The first section is the background of the study which will look at the areas of financing technology based firms, followed an overview of venture capital firms in other context, then the perception of venture capital financing in the eyes of MAVCAP shall be critically reviewed. Various efforts of Malaysian government to promote TBFs financing and commercialization shall be critically investigated through the eyes of MAVCAP as the case company. The next section will then present the methodology for this research after which we shall conclude by presenting the discussion, conclusion and implication for research.

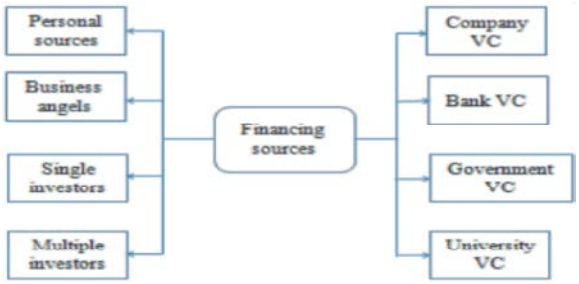

Fig. 1: Financing Sources for Technology Based Firms
Source: Researcher's Construct

Background of the Study

Financing Technology Based Firms: There are different types of financing possibilities available to TBFs. These categories of firms often depend on family financing, loan from friends, overdrafts or personal loan from commercial banks (otherwise known as Financial Bootstrapping). However, there are two methods to adopt in FB; (a) adopting strategies that reduce cash requirement by securing resources at little or no cost. TBF managers may for instance depend on their personal relationship to secure free access to certain financial resources. They may adopt strategy to secure resources without making use of commercial bank funding or external equity funding. They may also obtain capital through subsidy financing or personal sources of finance, [17, 18]. (b) However, for other projects with high growth potentials, a TBF owner can access funds from private investors known as VCs and or BAs. Several authors have reported that more than 90% of technology entrepreneurs finance their ventures through informal sources and about 60% source their early capital as contribution from the venture founders, [18-20]. Although many publications have been focused on the formal sources of finance, mainly in the area of equity [19, 21] and further in the area of debt finance [22]. Lam posited that FB is actually the most informal source of financing TBFs and that both equity and debt sources are formal in nature because of the official and strict screening criteria (due diligence, business proposal screening) they adopt before funding is allocated to TBFs [20]. Although many entrepreneurs are found to adopt a combination of debt and equity sources of financing, still, a vast number of studies reports that equity financing remain the best form of development capital for technology based firms. The Figure 1 shows the different types of financing sources for TBFs that is potentially available to finance emerging companies.

Meaning of Venture Capital: Venture Capitalists are specialized intermediaries that direct capital to firms and professional services to companies that might otherwise be excluded from the corporate debt market and other sources of private finance [14, 15, 23]. Kiribati [24] in her study of VCs evaluation in Japan refer to VCs as individuals directly involved in the VC investment process from scouting and screening activities to post-investment and exit and excluding employees of the VC firms who are engaged in general duties that are unrelated to investment process for example general personnel affairs. VC financing is used to invest mainly in technology SMEs with good growth and exit potential [25, 26] while private equity finances changes of ownership in established businesses, often supported by debt capital. Further definition of VC [27] views it as early stages of equity investments including later stage mezzanine, turnaround and buyout investments typically associated with private equity investments in the West. Cumming and Dai [28] posits that VCs operate across countries and time zones, providing capital and skills to entrepreneurial firms competing in global markets. This is particularly in the early staged VC where technology transcends geographic boundaries [29, 25]. Typically VCFs concentrate on industries with a great deal of uncertainty, where information asymmetry (gaps) among entrepreneurs and VCs are commonplace. These ventures are identified as financially constrained. TBFs rely on VC

as one of their main sources of funding. Recent empirical research found that the effects of VC on the success of these ventures are considerable. The value of venture capital investment is borne out by figures which show that VC backed firms grow on average twice as fast as those not backed by VCFs [30]. This category of equity investors focuses on particular region, or single country when searching for corporations that deserve financial backing.

Methodology of the Research: This particular research is a single case study mainly based on reviews of empirical studies on technology based firms financing and venture capital. Furthermore, the authors' reviews available information on the website of Malaysian Venture Capital Berhad coupled with some hard copy document and newspapers analysis we could lay our hands on. The authors shall compare this information with the aim of discussing the findings and finally conclude the paper with implications for future research.

RESULT AND DISCUSSIONS

MAVCAP's Perception of Venture Capital: Based on the information available on the web portal of the Malaysian Venture Capital Company, a government backed VCF established some 12 years ago to promote and develop the VC culture in the country. The concept of venture capital is perceived to mean a kind of private equity fund made available to young and technology based companies to develop through their successive stages of life cycle. However, MAVCAP main aim is to build fantastic ROI through exit of the investee companies. Such cash out may be in such a way as trade sale, IPO or buyouts. VCs are mostly people organizations who stake in their capital into high risk ventures with the aim of reaping huge returns from the firms, their capital outlay is mostly in the form of cash in exchange for preference shares in the invested firms [6]. The team of VCs provide their knowledge and financial capital to help boost the corporate governance of investee companies along with boosting the integrity of such firms in such a way that it becomes attractive to other financial investors to get encouraged to bring in more cash. Venture capital is also regarded as pooled investment mechanism that mainly invests the cash from other co-investors in TBFs that are ordinarily perceived as too risky for the conventional investors [31]. In exchange for the high risk that potential VCs undertake when putting in their money on smaller TBFs, young TBFs with limited track records which are

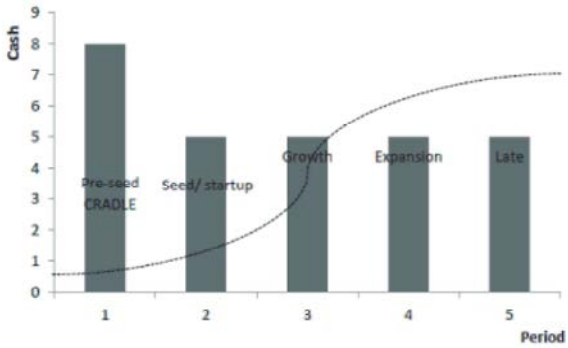

Fig. 2: VCFs Growth curve
Source: Adapted from MAVCAP [6].

too small to attract growth fund from the public market and could not secure commercial bank finance will find VC funding a highly alluring alternative.

How MAVCAP help TBFs: Venture capitalists focus on value creation which is achieved by the speeding up of technology products and services with greater market penetration. This group of financial investors shares their knowledge capital, as well as provides corporate governance on important management decisions to improve the performance of investee companies. Mavcap VCs are committed personnel who are determined to empower technopreneurs to build their young ventures. This commitment is the main reason they are able to harness the inherent capabilities of TBFs. Figure 2 shows a typical development life cycle of how Malaysian Venture Capital Berhad fund companies in Malaysia.

Graduate Internship Scheme (GIS): MAVCAP also try to build adequate pool of venture capitalists by offering opportunities to Malaysian graduates to under-go a one year intensive practical training and mentorship as venture capitalists. This is a strategy of keeping with their core mandate to nurture and groom more venture capitalists in the industry. Currently, dynamic and motivated university graduates are offered job placements as interns with postings to various outsource partners of MAVCAP. Among the training they lucky interns undergo are sourcing investment deals, deal evaluation, proposal approval and monitoring and management of portfolio. This moves is consistent with what authors in many publications have recommended as a way to bridge the gap in the VC industry [2, 3, 14] Since it has been acknowledged that among the problems encountered in areas of financing more deals in Malaysia is because of the inadequate number of qualified venture capitalists to evaluate and nurture investee companies [3, 6].

What MAVCAP is as a VC FIRM?: The ICT sector in Malaysia has been witnessing consistent growth for over twenty years. The emphasis of government is among the top reason for this strong performance which has ensured that the sector plays a strong role in supporting the country's dream of becoming a knowledge-driven economy. Government has recognized the hardship small or budding ICT firms go through to compete for market penetration due to the little finances at their disposal. In view of this, Malaysia Venture Capital Management Berhad was set up in 2001 [1]. MAVCAP is currently perceived as the biggest VC firm in Malaysia with funds spread across the ICT sector and other technology based industries [6]. This organization is a wholly owned subsidiary of the Ministry of Finance. Malaysian Venture Capital Berhad was established to help achieve the vision to assist ICT firms and building the VC culture in Malaysia. MAVCAP goes to a great length to invest in TBFs that have potentials and to assist technopreneurs with great passion for success. This is also done by committing themselves to making available strong platform for technopreneurs to take their ventures to a greater level. The Government Backed Venture Capital Company was allocated RM970 million under its management. The firm provides an alternative source of high-risk financing for start-ups, seed capital and early stage ventures in the ICT sector and high-growth industries. Initial investments of RM1 million – RM3 million are complemented with Mezzanine allocations valued at RM5 million – RM10 million to fund companies through to the pre-IPO stage. In later stage investments, MAVCAP typically invests between 3 - 5 years [31, 32]. MAVCAP is the most active investor in the ICT and high tech industry, through its direct and seed ventures and has invested in close to 90 companies. This statement is supported by [29, 25] who argue that VCs are people who build early staged companies by focussing on areas with a great deal of uncertainty, where information asymmetry (gaps) among entrepreneurs and VCs are commonplace. The core emphasis of MAVCAP is:

- 70% direct investments in Malaysian incorporated companies.
- 30% investments in foreign companies with business interests in Malaysia.

Until recently they succeeded in the listing of 6 portfolio companies in exchanges in Malaysia, Singapore and the United Kingdom. Since 2001, the MAVCAP has financed over 258 entrepreneurs and provide over 1,200 jobs in the technology based firms sector in Malaysia. Through MAVCAP's investee firms, they have as at December 31, 2007, generated over 100 TBFs' products and services which have penetrated markets in China, Vietnam, Philippines, Indonesia and the United States. This is in line with findings of Cumming and Dai [28] who put forward that VCs operate across countries and time zones, providing capital and skills to entrepreneurial firms competing in global markets. This is particularly in the early staged VC where technology transcends geographic boundaries [29, 30].

MAVCAP Investment Scheme: As a dedicated Government Backed Venture Company aimed at helping to build the VC culture in Malaysia and also growing the information technology sector. MAVCAP supports investment at the seed, start-up and early-stage firms and other TBFs with high growth possibilities. MAVCAP is committed to:

- Strengthen technopreneurs to generate wealth
- Build superior returns on investment (ROI)
- Mentor a large pool of quality VC and PE managers in Malaysia

A typical length of period they invest their funds with TBFs is between 3 to 8 years in seed, start-ups and early-stage ventures. MAVCAP do not only put in their money in the ventures but also go further by holding equity positions in firms they finance and actively involved in strategic decision making. They are positioned as both strategic and professional partner who technopreneurs can turn to for sound judgment and advice. Malaysian Venture Capital Berhad is strongly guided by the willingness to nurture investee firms to greater performance standard. As a other venture capital firms, they are eager to take risks that traditional commercial banks are not willing to get involved in. The ideal partners of MAVCAP are TBFs that usually find it difficult to secure funding probably as a result of the smallness in size or because they are too young in the venture and lack management experience.

Investment Criteria of MAVCAP: It is a tradition that before investment decision is made, the VC will strictly access the potential prospect and the anticipated ROI of each technology. The VCs go extra length to check the nitty gritty of the potential investee firm to ensure the they produce fantastic returns. Many important factors will be considered in selecting the potential of the TBFs. They include:

- Composition, integrity and capability of the founders and management team
- Market opportunity, fantastic growth and scalability
- Strength of Product or service.
- Anticipated cash out strategy within the funding life
- Proven technology with strong competitive edge
- Ownership of significant IP with market values

MAVCAP's investments often take the form of equity involvement in the potential TBFs. They propose different kind of instruments which could be either by ordinary shares or convertible preference shares. Hence, their investments take either of direct capital investment or outsource partners program.

Direct Capital Investment: MAVCAP invest directly and involve fully in the management and operations of the TBFs by:

- Being in the lookout for partnership opportunities with TBFs and early-stage ventures cum expansion of growth firms.
- By implementing their financial and knowledge capital, they speed up the growth and development of TBFs until they can fruitfully cash out.

The primary aim of MAVCAP is to divest to other portfolio such that there will be complementarities and synergistic gathering TBFs as investees. MAVCAP think the synergies between the partnering firms they put in their money will yield better business returns. They are also willing to syndicate with the venture capital firms and other investors. Table 1 shows the typical investment offering of Malaysia Venture Capital Management Berhad.

The Outsource Partners Program: The Outsource Partners Scheme 1 and 2 were introduced in the year 2001 and 2006 respectively. The aim of the scheme is to allocate a certain amount of fund to selected private VCFs who in turn shall re-invest in TBFs.

This Scheme allows MAVCAP to:

- Develop wide industry contacts .
- Create and solidify relationships within the industry.
- Increase ROI.

The prosperity of the OSP is revealed by the beneficial response from several domestic and foreign, organizational and individual investors who have dedicated more than RM100 million in the MAVCAP-promoted VC funds. Since its establishment under the OSP plan and in collaboration with its OSP's have trained and mentored several VC professionals. Table 2 below shows some of the companies that have benefited from investment offerings of Malaysian Venture Capital Management Berhad since inception.

Table 1: Typical Investment Offering of MAVCAP

	MAVCAP 100 (51% Minimum Bumiputra Stake)	MAVCAP 110	MAVCAP 120
Typical investment size	• RM1 million-RM10 million • Seed and start-up deal stages	• RM3 million-RM15 million • Early & expansion deal stages	• RM5 million-RM20 million • Late deal stages
Target sector	• General ICT-hardware/software • Various domains • Multimedia service • Providers/application service • Providers (MSPs/ASPs)	• New media • Games • E-content • Community & networking • Wireless & mobile	• Software application & service • Digital content (animation, games & high definition)

Source: Compiled from Malaysian Venture Capital Berhard [6]

Table 2: Selected Portfolio of MAVCAP

Name of Company	Specialization	Location
FIBON advance composites Sdn Bhd	Polymer matrix fiber	Malaysia
Boston web academy Sdn Bhd	IT Education & Training	Malaysia
Aexio Software Sdn Bhd	Network optimization software	Malaysia
GS Productions Sdn Bhd	High definition documentaries	Malaysia
CPK Solutions	Software for logistics companies	Malaysia
B'Smart Solutions	Wireless devices design	Malaysia. Oman. Indonesia. South Africa. Thailand. China.
CMTS	Software for online cinema ticketing	China
Element Ventures Sdn Bhd	Digital sound productions studio	Malaysia
Global Odyssey Corporation Sdn Bhd	KPI monitoring solutions	Malaysia
CYNGUS Technologies Sdn Bhd	Toll free network service software	Malaysia

Source: Adapted from MAVCAP (2013)

***MAVCAP Outsource Partners*:**

- ✓ Ethos Capital Sdn Bhd
- ✓ QMA Capital Sdn Bhd
- ✓ DTA Ventures Management Sdn Bhd
- ✓ Astra Capital Sdn Bhd
- ✓ Teak Capital Sdn Bhd
- ✓ Expedient Equity Sdn Bhd
- ✓ Musharaka Tech Venture Sdn Bhd
- ✓ Photonics Venture Capital Sdn Bhd
- ✓ ISpring Capital Sdn Bhd

Successes of the OSP Scheme: As part of the redirected focus of MAVCAP to operate more like a VCF, by taking up high risk investments in young firms with the successes it has achieved with the initial RM500 million it commenced business with under the 8th Malaysian Plan, part of a series of five-year national development plans. Further funding was allocated to MAVCAP under the 9th Malaysian Plan [1, 6]. However, in the third year of the 10th Malaysian Plan, the agency still has about RM100 million left over from its 9th Malaysian Plan allocation [31]. However, more capital is been requested for under the 10th Malaysian Plan to further expand into the next phase of the Outsource Partners (OSP3) program. MAVCAP is asking for another RM300 million from the Ministry of Finance [31]. Furthermore, according to [30], MAVCAP has invested up to RM509M from funds worth RM1B managed by the agency that was attributed to 87 companies in Malaysia. A typical investment size is RM5M to RM15M, but they had done RM20m investment on a company before [32]. She highlighted further that only 5% of the companies MAVCAP had invested were from women entrepreneurs, that is to say 5 out of 87 companies that MAVCAP has invested in so far were owned by women, translating to RM42M worth of investment. MAVCAP is reported to target investing in 6-8 companies in the current year with capital worth RM30-120M in investment. The next ambition of MAVCAP is to behave more like a VC firm by taking up higher risks like the private VC firms so that they can repay government fund after harvesting their investment from investee firms. However, MAVCAP has helped so far in building industry capabilities and ensuring there are enough private VCs that MAVCAP can co-invest with in startups and hopes they can continue to do more. They hope to continue to help grow the VC ecosystem in the country and to hopefully spark more private VC companies to sprout. The negative lessons learnt from the OSP 2 will serve as a platform in launching the next phase of OSP 3 by strengthening further the many in active private VCs that have closed shop after investing their main capital under management hence making TBFs to suffer from lack of further funding.

CONCLUSION

This research study makes use of the past publications in reputable database, websites of Case Study Company, newspapers and hard copy document analysis to draw conclusion on this research. While there are several research on technology based firms and venture capital financing in Malaysia and other countries, no such study have since the inception of MAVCAP done a review of this company. The outcome of this study will contribute immensely to the body of theoretical knowledge on VC in Malaysia by throwing up the challenge on the activities of MAVCAP to the research community both in Malaysia and globally with an aim to encourage other researchers to adopt other approach to evaluate and investigate the activities of venture capital in Malaysia with particular emphasis on government backed VCs and MAVCAP in particular. This research to the best of our knowledge is the only study that have reviewed the activities of MAVCAP since inception 12 years ago by exposing the relationship between the investee companies and MAVCAP and the impact of such relation has on the funding ecosystems in Malaysia. The findings from this study however, provide a theoretical basis to understand the relationship and interaction between VCFs and TBFs in Malaysia. Finally, this research will add to the many archive of study in this area because until now, search through academic databases have returned little information as regards this subject of investigation in Malaysia. The major limitation of this research is that it is mainly based on secondary information sourced from past empirical studies, newspaper reviews, website reviews and document analysis. Findings from this study shows that MAVCAP in agreeing that Malaysia lacks enough and qualified VCs have set up programs aimed at boosting the pool of VCs in the country through the GIS. Furthermore, there is an acknowledgement that foreign VCs are reluctant to fund Malaysian TBFs based on the belief that innovations from this country are not fit to compete in global markets. Hence, effors are been made to encourage Malaysian researchers and innovators to develop a global mindset in their research and innovation since Malaysia is a small country and must continue to rely on other international markets to sell its products and services. The nature of

research on venture capital financing as an area of study is such in a manner that findings provided shall add abundant value through their applicability in an organizational setting and adoption by public policy makers in Malaysia. However, based on the revelation from the discussions and findings section of this article, the authors would conclude that the main aim of this research has been achieved.

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