

Enhancing SME Access to Finance

Case Studies



About the SME Finance Forum

The SME Finance Forum works to expand access to finance for small and medium enterprises—a critical engine of job creation in emerging economies.

The Forum brings together financial institutions, technology companies, and development finance institutions to share knowledge, spur innovation, and promote the growth of SMEs.

Managed by IFC, the SME Finance Forum was established by the G-20 in 2012.

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Foreword

These case studies are the result of a global effort to collect and codify real-life examples of policy interventions and regulatory changes that promote the growth of small and medium enterprises (SMEs) through improved access to finance.

In aftermath of the financial crisis, the need for policy and regulatory support for SMEs came sharply into focus. Many countries enacted policy reforms intended to promote SME growth. Yet little was really known about which policy levers are most effective in different contexts to promote the growth of SMEs.

Even as progress has been made in recent years to identify current gaps and challenges for SME finance, and highlight the important contribution SMEs must make to new job creation, little solid evidence exists on policy interventions that work. The Global Partnership for Financial Inclusion (GPII) SME Sub-group initiated this project to capture successful policy initiatives from G-20 and other countries in response to that need.

The resulting case studies cover a range of policy interventions from direct funding for SME finance and loan guarantees to help shore up finance for SMEs, to regulatory reform, and policies and support for infrastructure. They include several innovative mechanisms for securitization, e-money, mandatory targets, and the collateralization of movable assets and establishment of effective registries.

We are grateful to the government and non-government officials from G-20 countries and Alliance for Financial Inclusion (AFI) members who submitted contributions. This report is a tribute to their genuine commitment to learn from one another.

We would particularly like to acknowledge the work of the SME Finance Forum in pulling together, and publishing this report.

We hope that these case studies contribute to global learning on good policy practices in SME finance, and chart a course for future policy interventions that help SMEs to grow and contribute to economic development.

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Acronyms

ADB	Asian Development Bank
BFP	Business Finance Partnership (U.K.)
BSP	Bangko Sentral ng Pilipinas (The Philippines)
CFCU	Central Finance and Contracts Unit (Turkey)
CMAC	Municipal Non-Banking Institutions (Peru)
CRAC	Rural Non-Banking Institutions (Peru)
EFG	Enterprise Finance Guarantee (U.K.)
EIB	European Investment Bank Group
EIF	European Investment Fund
EMP	Electronic Means of Payment (Russian Federation)
ESNI	Euro Secured Notes Issuer (France/Europe)
FG	Fondo di Garanzia (Italy)
IDB	Inter-American Development Bank
IFC	International Finance Corporation
IPA	Instrument for Pre-Accession Assistance (Turkey)
iVCI	Istanbul Venture Capital Initiative (Turkey)
KDB	Korea Development Bank
KOBI VCIT	Kobi Venture Capital Investment Trust (Turkey)
KOSGEB	Small and Medium Enterprise Development Organization (Turkey)
KPO	Korea Patent Office
MFO	Microfinance Organizations (Russian Federation)
MSME	Micro, Small, and Medium Enterprise

NBFI	Nonbank Financial Institutions
NBG	National Bank of Greece Group
NGO	Nongovernmental Organization
OJSC	Open Joint-Stock Company (Russian Federation)
PPKD	Credit Guarantee Corporations (Indonesia)
RCC	Consolidated Credit Report (Peru)
RCD	Debtors Credit Report (Peru)
RCO	Credit Report by Operations (Peru)
SBS	Superintendency of Banking, Insurance and Pension Funds of Peru
SCA	Swazi Commercial Amadoda (Swaziland)
SCB	Scheduled Commercial Banks (India)
SFLG	Small Firms Loan Guarantee (U.K.)
SIDC	Swaziland Industrial Development Company
SLBC	State Level Bankers Committee (India)
SME	Small and Medium Enterprise
SMESPD	SME & Special Programmes Department (Bangladesh)
SPV	Special Purpose Vehicle
TKB	Development Bank of Turkey
TTGV	Technology Development Foundation of Turkey
UNIDO	United Nations Industrial Development Organization

Introduction

In the last few years, there has been growing recognition of the importance of small and medium enterprises (SMEs) for job creation and economic development, not just in emerging economies but in developed countries as well. The impact of the financial crisis that began in 2008 highlighted the importance of access to finance for the SME sector as particularly in need of attention.¹ Notwithstanding this increase in interest, there is still limited information available on best practices to support SMEs, particularly on effective policy tools to support SME access to finance.

Research conducted under the aegis of the G-20 Global Partnership for Financial Inclusion (GPFI), IFC, and others during the last four years points to some clear findings.² SMEs are critical for job growth, but the level of growth depends significantly on SME access to finance, and on the so-called “gazelles,” the fast-growing SMEs that produce the majority of new jobs.

SMEs themselves report lack of access to finance to be one of the greatest barriers to their growth. Half of SMEs in emerging markets are credit constrained. Seventy percent of micro, small, and medium enterprises (MSMEs) have no access to external finance, and another 15 percent are under-financed. All this adds up to an estimated credit gap of US\$3.2-US\$3.9 trillion (US\$2.1-US\$2.6 trillion in emerging markets).³

Informality also hinders SME growth. But there are few examples of effective incentives for informal businesses to formalize. Lack of information on how to register an

enterprise, complicated and time-consuming procedures to complete the process, as well as taxes that registered businesses are required to pay, and stricter labor regulations may all hold back informal businesses from registering. Yet, measures to simplify business registration and reduce such costs have shown little impact. Paying firms to register has not worked either. Further research is needed to find out how to get businesses to register.⁴

Other barriers to SME growth that are particularly acute in developing countries include a lack of infrastructure for finance and, on the lender side, a lack of good data to enable effective risk management. To overcome these problems, regulatory reforms to support an enabling environment and strengthening financial infrastructure are critical. In addition, public programs and private initiatives specifically tailored for SMEs (e.g., enabling the use of collateral through both laws and registries) are needed.

In that context, the GPFI SME Finance sub-group called attention in 2013 to the importance of policy and regulatory support, especially for financial markets infrastructure development and for innovations involving data-driven approaches for SME finance.⁵ The sub-group determined that a set of case studies of successful policy initiatives from G-20 and other countries was needed that could inspire further reforms.

The resulting case studies presented here are intended to promote the wider adoption of good policy practices in SME finance. They capture the strengths and weaknesses of

1. The recent crisis also made access to finance more difficult because of increased risk concerns, especially for SMEs, with certain government policies tending to have negative impacts (BASEL II/III norms for credit risk restricting SMEs and with banks becoming more restrictive even ahead of BASEL timetables).

2. See, for example: IFC, *Scaling-Up SME Access to Financial Services in the Developing World*, 2010; IFC, *SME Finance Policy Guide*, 2010; IFC, *Strengthening Access to Finance for Women-Owned SMEs in Developing Countries*, 2011; IFC, *Scaling Up Access to Finance for Agricultural SMEs: Policy Review and Recommendations*, 2011; and GPFI/IFC, *Small and Medium Enterprise Finance: New Findings, Trends and G-20/Global Partnership for Financial Inclusion Progress*, 2013.

3. IFC/McKinsey & Company, *Two Trillion and Counting: Assessing the Credit Gap for Formal and Informal SMEs*, 2013, p. 3.

4. IFC, *Closing the Credit Gap for Formal and Informal Micro, Small and Medium Enterprises*, 2013.

5. GPFI/IFC, *Small and Medium Enterprise Finance: New Findings, Trends and G-20/Global Partnership for Financial Inclusion Progress*, 2013.

current and on-going policy initiatives and, since high-level government officials mainly submitted them, often reflect the reality of implementing initiatives that involve interested parties in the private sector and a range of government entities.

The case studies have been grouped along four main types of policy intervention: Loan Guarantees for SMEs; Government Funding for SME Finance; Regulations Requiring SME Finance; and Policies and Infrastructure for SME Finance.

Loan Guarantees for SMEs

In the 20-plus case studies submitted by AFI and G-20 countries, loan guarantees are one of the two most frequent types of interventions, but there are many different varieties of loan guarantees. In Indonesia, for example, loan guarantees are seen primarily as substitutes for limited collateral and as tools to mitigate credit risk, and guarantee entities are created at regional levels by provincial governments after sufficient interest has been mobilized to initiate them. In fact, even with laws and regulations in place, promoting interest and coordination among stakeholders has been a major challenge, requiring workshops and other means of disseminating information and facilitating discussion. In addition, initial capital has to be provided by provincial governments, so that they must be convinced that the guarantee entities can operate in a sustainable manner. Bankers must also see them as useful tools for reducing risk.

As of 2014, only eight of Indonesia's 34 provinces have them, but another four are approved, and 10 more are in process of getting approval by their local governments. Nonetheless, from 2010 to the end of 2013, more than 53,000 MSMEs have been reached with guaranteed loans amounting to US\$101 million and guarantee coverage reaching US\$85 million – and with credit, amounts guaranteed, numbers of borrowers and employment generated all increasing by at least a factor of four from 2010 to 2013.

The loan guarantee example from Italy, where the government's loan guarantee entity was created in 2000, only became important with the onset of the financial crisis in 2008. In fact, only US\$15 billion of guarantees were created from 2000 through 2008, but US\$55 billion from 2009 through 2013, with more than 77,000 loans to more than 51,000 firms guaranteed in 2013 alone. The loan guarantee entity was created for the usual reasons that SMEs lack both collateral and adequate financial statements. While it is under Italy's Ministry of Economic Development, it is managed by

a committee whose members include representatives from firms and bank associations.

The maximum amount guaranteed by the fund for a single borrower is less than US\$3.3 million, and the guarantee covers a maximum of 80 percent of the loan. The characteristics of the loan (interest rate or duration) are settled between the bank and borrower. Application procedures are quite cumbersome, notwithstanding the use of a scoring system. To investigate the impact of the fund, the Bank of Italy conducted an external evaluation, which found that the guarantee fund has a positive impact on the volume of bank loans and even a slight impact on interest rates.

In the case of El Salvador, loan guarantees existed but were not taken seriously because of a lack of adequate funding to pay guarantees, the lack of laws to deal with movable collateral, and haphazard operations such as lengthy delays in guarantee processing. However, the financial crisis beginning in 2008 and the acquisition of several important local banks by foreign banks made access to credit much more difficult for SMEs, especially for those SMEs that had not formalized. Given this situation, government entities responded, with BANDESAL (a government development bank) and the Central Bank coming together, and with support from a new law on guarantees passed by the Legislative Assembly, to help overcome the difficulties that SMEs were experiencing by offering an apparently highly effective loan guarantee program.

The resulting major improvements in program operations (e.g., in transparency and speed in the processing of claims, together with a model to estimate risks and expected losses) led to a quick response with 4,117 guarantees for US\$18.8 million covering loans totalling US\$32.4 million by June 2013, increasing to 10,087 guarantees for US\$42.2 million covering loans totalling US\$74.4 million by April 2014. With this rapid increase, an average loan size of somewhat over US\$7,000 and an average guarantee of slightly over US\$4,000 the guarantee program not only indicates its initial success but also a focus on SMEs and a reasonable distribution of risks. Of course, given the very recent initiation of this new loan guarantee program it is not yet possible to assess losses rates.

The central government of the Russian Federation has supplied capital to regional guarantee funds in 80 provinces that has enabled them to provide support for SMEs, guaranteeing up to 70 percent of an SME's liabilities. The total capitalization of these guarantee funds reached US\$1.2

billion as of the beginning of 2014, and with this it has issued over 39,000 guarantees for a total of US\$3.6 billion, thereby attracting over US\$7.7 billion in loans for these SMEs. In 2013 alone, more than 7,000 guarantees were provided to SMEs for US\$9 billion, which supported more than US\$2 billion in loans. The Russian Ministry of Economic Development rates the efficiency of these regional funds by the ratio of capital to the amount of loan guarantees and, while the average is 3, more than 10 regional funds have multipliers for loans that are between 5 and 7 times capital.

As in various other countries, the Enterprise Finance Guarantee (EFG) in the United Kingdom was established in 2009 in response to the financial crisis that began in 2008, with a focus on SMEs that had adequate cash flows but lacked adequate security. The guarantee process is totally driven by lenders, with the government having no role in the decision-making process and providing only the financial backing. Guarantees are for 75 percent of the value of the loan, with lenders required to undertake all collection procedures, including the realization of security, before turning to the EFG for reimbursement. Because of the earlier existence of a similar loan guarantee system and the beginning of the financial crisis in 2008, there was no opposition to the EFG and start-up was very quick, with just three months between the idea and its operational realization. Between 2009 and late 2013 some 20,000 businesses accessed more than US\$3.3 billion in guarantees. An external assessment conducted by Durham University Business School in 2013 was highly favorable.⁶

Government Funding for SME Finance

Direct financing of SMEs has also been undertaken in several countries, including the United Kingdom, Turkey, Russia, and Tanzania, but in quite different ways. In the United Kingdom, the Business Finance Partnership (BFP) has mainly helped medium-sized firms that do not have easy access to capital markets, but doing so on fully commercial terms and in conjunction with the private sector. Although most businesses had hoped for quick access to funding, the usual time period for processing has been rather long, 12 to 18 months. On the other hand, while BFP funds could be made available up to 50 percent of the total amount requested, the average amount supplied with BFP funds was actually only about 20 percent because private funders found collaboration quite attractive. In the two years that

these operations have been active, US\$2.2 billion has been made available to 32 mid-sized businesses, of which US\$410 million was supplied by the U.K. government and the remainder by the private sector.

Turkey has four separate government investment operations that provide funding for SMEs. The first, called the “Angel Investment Scheme,” is designed to provide financing and technical assistance for small, start-up SMEs that lack adequate collateral and also need help with the essentials of good business practices. The Turkish Treasury, with the undersecretary in charge, offers tax incentives for angel investors (75 percent of the amount invested can be deducted from taxes, and up to 100 percent in the case of SMEs that are involved in government-supported technical projects). Angel investors can own up to 50 percent of the shares in the SME, with the shares held for at least two years, and are also expected to provide technical assistance to their SMEs. The minimum amount to be invested is just under US\$10,000, while the maximum is just over US\$475,000. During the first year of the program, 182 business angels have been licensed and several networks of angel investors are also being added to the program. This fairly rapid start-up can be attributed to efforts to mobilize supporters, in both the public and private sectors, with the enabling legislation also being prepared with similar support. During just the first year of the program, there have been five angel investments for slightly under US\$850,000 and for an average of about US\$170,000, with others currently being assessed for support.

The second Turkish program is a venture capital fund for the 43 provinces of Anatolia, funded primarily by EU’s Instrument for Pre-Accession Assistance (IPA), with the collaboration of two Turkish government agencies, the Ministry of Science, Industry, and Technology as the operating structure, and the Small and Medium Enterprises Development Organization (KOSGEB) as the recipient of assistance. The European Investment Fund (EIF) is the trustee administrator for the EIF-IPA Commitment. An initial agreement was signed in August 2011, with a further agreement in December, and operations starting at the end of 2013. The fund manager and the Istanbul Venture Capital Initiative (iVCi) are also investors in the fund. Although research for investments in SMEs has started, no funds have as yet been disbursed.

6. https://www.gov.uk/government/uploads/system/uploads/attachment_data/file/85761/13-600-economic-evaluation-of-the-efg-scheme.pdf

The third Turkish program, the KOBİ Venture Capital Investment Trust, began operations in 2006 with three main partners, including both the public and private sectors (KOSGEB, TOBB, and Halkbank), with the purpose of investing in local SMEs that show high potential for innovation. In providing both financial and managerial support to qualifying SMEs, KOBİ's investments are limited to 49 percent of the SME's capital and can range from US\$250,000 up to US\$1 million, depending mainly on the wide range of business types supported. Potential investments are based on a detailed list of specific criteria and also include a position on the SME's managerial board. Thus, after the investment is made, KOBİ remains highly involved: preparing and implementing business plans, carefully measuring both targets and accomplishments and, at times, even in day-to-day operations. Given this extreme care, investing in only 10 of 2,124 applicants, it is not surprising that these 10 businesses are all highly successful, with sales and profits increasing every year in virtually every case, and their excellent growth often requiring substantial additional investments.

The fourth Turkish program, the Istanbul Venture Capital Initiative (iVCI), established in 2007, is also partly funded by the EU through its European Investment Fund, along with the National Bank of Greece Group (NBG), Garanti Bank, and various Turkish government entities, including KOSGEB, the Technology Development Foundation of Turkey (TTGV) and the Development Bank of Turkey (TKB). The iVCI invests for a long time horizon, six to 10 years, and in private equity and venture capital funds, as well as directly, along with other funds, in SMEs. As of the end of March 2014, it had invested over US\$95 million, with commitments of over US\$195 million. As a "fund of funds," iVCI believes that its main contribution has been to stimulate the development of various other funds by demonstrating what can be done directly, as well as by investing in other funds. Fourteen SMEs had benefited directly from iVCI investments as of the end of March 2014, with 25 percent of its investments ultimately going to SMEs.

In addition to the case study on loan guarantees discussed above, Russia has also provided two examples of direct financing for SMEs in a single case study. The first of these is based on the law "On Microfinance," but where microfinance also includes both SME and consumer loans, with an upper limit on loan size of just over US\$30,000. Two types of entities are involved, Microfinance Organizations (MFOs), which include both government organizations and private entities, and credit cooperatives, which are called Microfinance Institutions (MFIs). The government entity in

charge, the Ministry of Economic Development, supports only MFOs whose founders are regional or municipal government bodies and provides them with funds for on-lending to clients. Clients receive loans from these MFOs on quite favorable terms, mainly at interest rates of 10 percent, but limited to 12 months duration. Beginning in 2005, government funding was only US\$85 million for use in 16 regions, but had increased to US\$72.4 million in 35 regions by 2013. At the end of 2013, there were 3,860 MFOs, but only the 130 governmental MFOs receive government funding. Some 58 percent of MFO loan portfolios now go to SMEs, with an average loan size of just over US\$16,000. Overdue percentages on loans from government MFOs amount to just 6.4 percent, as compared to 7.1 percent for MFOs overall.

The second program included in this case is carried out by the OJSC "SME Bank," which evolved in 2011 from an earlier government banking entity. The OJSC "SME Bank" provides funding for a range of entities and activities including private and government banks, leasing and factoring companies, and both MFOs and MFIs. It operates in 82 regions, working with 134 partner banks and with 150 other types of financial entities, and with a particular focus on SMEs that are in the manufacturing sector, are innovation driven, or in regions with difficult socio-economic situations. By early 2014, funding provided to SMEs by the OJSC "SME Bank" had reached over US\$2.7 billion and, unlike the other program, has a focus on longer-term loans of one to two years (48 percent) and on more than two years (50 percent), and with interest rates around 15 percent rather than at the market rate for SMEs of over 20 percent.

The only case from Africa is from Swaziland and also involves the financing of SMEs. Although the main governmental entity involved is called the Micro Finance Unit, the main focus of the program is SMEs, which are seen in general to have difficulty in accessing bank credit in spite of excess liquidity in local banks. The Swaziland Industrial Development Company (SIDC), the country's development finance institution (DFI), implements the program, which is based on a facility of US\$1 million. However, the SIDC has had some administrative challenges due to the range and volume of requests for funding without any standardized format. As a result, standards were subsequently introduced, including financial modelling to test for feasibility and various measures of risk, along with mentoring for potential SME clients that enabled some of them to produce basic business plans. The average loan size requested was only about US\$5,000, but many of the smaller businesses could not present the needed information, so that the average loan

granted was about US\$33,000, with only 56 percent of the funds available being lent and just to 17 SMEs. An important challenge, which is beginning to be met, is to convince more of the applicants that presenting a loan request is a serious activity. In addition, the SIDC is encouraging the development of better information and more appropriate loan products (e.g., involving value chains and invoice financing).

Cases Involving Policies and Infrastructure in Support of SME Finance

Given the significant involvement of government officials in the production of case studies, including especially central bankers and other regulators of financial entities, and given that all the remaining cases provide examples of initiatives in areas of policy and infrastructure, it is perhaps somewhat surprising that there are no cases that deal directly with the traditional regulatory issues of risk and risk management, with Basel initiatives rarely mentioned. In fact, some cases that involve financial policies to promote SME finance are focused on requiring lenders to provide financial services to SMEs.

Required Lending Targeted to SMEs

Targeted lending to SMEs is a policy approach that has been used in some countries, Bangladesh in particular, where government officials were concerned that SMEs were receiving only a small share of credit relative to their importance in the economy. After listing a variety of barriers to SME finance, policy makers decided to adopt a system where banks and nonbank financial institutions (NBFIs) would participate in establishing annual targets for loan disbursements to SMEs, of which at least 40 percent would go to small enterprises, and women would also be favored. Achievement of these targets by banks and NBFIs would influence the licensing of their branches and determination of their CAMELS ratings.

Banks and NBFIs also participate in high-level discussions with Central Bank officials to see the benefits from establishing units dedicated to SME finance and their profitability, while receiving funding support. In addition, the Central Bank organized activities to encourage the participation of nonfinancial entities in supporting SMEs and has also obtained support in this from various international development agencies.

Goals for SME finance were set initially in 2010 and have been increased significantly each year so that they have more than doubled by 2014, with achievement ratios of at least 115 percent (except for 2011 when it was only 94 percent). Rural lending has increased impressively, attributed to the focus on smaller SMEs, as well as on the rural areas themselves. However, notwithstanding special attention to the barriers facing women entrepreneurs and, even with significant increases in SME loans to women, these have not yet surpassed 4 percent of total SME lending.

The SME case study from India also provides an example of targeting, but of a rather different type, indicating first a requirement that every village with more than 2,000 inhabitants is to have a bank branch of some type. Moreover, to overcome the major barrier to financial services for SMEs, seen to be mainly credit risks due to lack of information, government policy makers have decided that policy must involve compulsion, specifically targeting “clusters” of enterprises in contiguous areas producing similar products or services.

The Reserve Bank of India has taken the lead in this, instructing the State Level Bankers Committees (SLBCs) to focus primarily on the 388 clusters identified by the United Nations, supplemented by a focus on 121 “Minority Concentration Districts,” areas with difficulties designated by Indian government agencies. As part of the promotion of this approach, SLBC member banks are required to display lists of these clusters on their websites, as well as maintain specialized branches and have specially trained personnel. In addition, regional offices of the Reserve Bank of India are to hold promotional meetings in cluster areas, especially those that are under-banked. The results of all this as monitored by the Reserve Bank of India is showing positive results, as the numbers of branches and numbers of loan accounts at both public and private banks have increased substantially from 2011 to 2013, and the amounts lent even more so, from US\$30.5 billion in 2011 to US\$44.8 billion in 2013.

Innovative SME Case Studies Involving Policies and Infrastructure

Korea has presented an innovative case study, which falls in the category of “removing barriers to women entrepreneurs’ access to finance,” and which is called “Certification of Family-Friendly Companies,” but which may in fact have wider applications. A scoring system for the “family friendliness” of SMEs has been created, which includes such variables as flexible work hours, support programs for

child birth, child care and education, as well as support for dependent family members and even for employees.

The Ministry of Gender Equality and Family is in charge of certifications and, in addition to SMEs, public agencies and local government are eligible to participate, with SMEs accounting for over one-third of participants. SMEs with scores exceeding a certain level can receive benefits from various government agencies including: subsidized interest rates for accident prevention and procurement of equipment; special offers of loans for SMEs; a discount for the fee for a technical evaluation; expansion of guarantee limits; and lower interest rate loans from two commercial banks. The program was initiated in 2008, with an increase in its annual operating budget for 2014, which covers promotional activities and various fees, to over US\$1.1 billion. In a recent evaluation by an independent agency, “Certified Family-Friendly Companies” showed superior performance to uncertified companies in several areas, including growth and profitability, as well as improvements in debt ratios and capital adequacy.

A second innovative case study from Korea, called the “Win-Win Package Loan,” falls into the category of “the use of marketing channels to provide financing” and was introduced in 2010. It allows SMEs to draw on the “financial creditability” of the larger firms they deal with (as suppliers in particular) and thereby to secure better credit terms. Typically the larger firm takes charge of fund raising and arranges for the partnering SME to obtain credit from the lending financial institution at a lower interest rate, as accounts receivable essentially become collateral. In 2013, the amount of such loans had already reached US\$32 billion, with 355 large firms having signed agreements with partnering SMEs.

A third innovative case study from Korea also involves collateral and falls closest to the category of “the securitization of moveable assets,” although in this case the assets are intellectual property rights (IP) held by an SME. These assets are property rights recognized by the relevant legislation as “patent rights, trademark rights, design rights and copyright.” The IP secured loan was introduced only recently, in September 2013, with the process of evaluating the IP developed by the Korea Intellectual Property Office, plus the formation of a fund to facilitate investments in and collection of IP secured loans with support from the Korea Development Bank and the Korea Patent Office. By the end of 2013, fifteen companies had already benefited from such loans, with an amount outstanding equal to US\$15.4 million. In addition, another IP Fund has been created that

raised US\$90 million in 2013 to invest in IP, and, as of April 2014, 10 companies had already received investments of US\$46 million. Furthermore, the largest company with expertise in IP not only promises to purchase secured IP but also to respond to patent-related lawsuits filed by foreign companies, with the development of a valuation model for such IP remaining the main challenge for promotion of a market.

Securitization of Movable Assets and Reducing Barriers to Formalization

Another case study that falls in the area of improving of “collateralization of movable assets and the establishment of effective registries,” can be of particular interest for two reasons: the case is from two small islands in the Pacific, thereby showing that even small countries can move forward; and it also demonstrates how both collateralization and registries are essential for success. SMEs in these islands found it virtually impossible to access bank credit without fixed property as collateral, and the process of reform was not simple as it required both economic and legal analysis as well as convincing a variety of participants of the value of these reforms.

Developing an efficient legal basis for using movable property as collateral required completely new legislation, as the existing framework was not only costly but also not fully secure. On the other hand, replacing the existing physical registries with online ones was primarily a matter of taking advantage of new electronic technologies, which now provide both public notice and a priority date. Results have shown impressive increases in the use of registries for both filings and searches on security interests, especially in Vanuatu but also in the Solomon Islands. The access of women-owned SMEs to bank credit appears to have improved, but access in rural areas has not yet increased significantly in either country. Although there is now a wide consensus on the value of these reforms, and especially their use by NBFIs, commercial banks have still tended to require land as collateral, with much higher rates of nonperforming loans resulting—and with a further challenge to increase the awareness of the potential value of these reforms among SMEs.

A parallel case study emerges from two Pacific Island countries (the Solomon Islands and Samoa) on “reducing the barriers to finance that the lack of formalization creates,” which shows how the inconveniences and high costs of registration of an SME (or any business) can be overcome.

Again, success required the involvement of both lawyers and economists, as well as bringing together interested parties to mobilize support, and to recognize clearly the unnecessary legal complexities and other delays, including even a required trip to the capital city to register, all of which favored informality.

The new Companies Act that was adopted includes a model set of rules that a company can easily adopt for registration, but which can also include innovative company structures, while registration itself can be done online. As a result, the numbers of new registrations increased dramatically in the two countries, first in the Solomon Island and somewhat later in Samoa. Furthermore, the standardized information in these online registrations can readily be accessed by banks and other potential lenders, thereby providing important information for lending decisions and thus significantly reducing such costs—while also allowing other legitimately interested parties to obtain information.

France provides another case study that involves securitization in order to increase SME access to finance. This case involves major participation by France’s Central Bank, which plays an especially important role by providing credit assessments of companies, noting that SMEs have been a resilient source of collateral for credit operations with central banks even during the crisis. In fact, SME credit qualifications are validated by the Central Bank, which has an internal credit assessment system that covers some 300,000 companies, so that these debts can readily be securitized as “Euro Secured Note Issues” (ESNI) and thus provide a source of liquidity for banks that lend to SMEs.

Widespread support is indicated by the number of banking and professional entities involved, as well as representatives of regulatory and supervisory agencies, such that the process of design and implementation could be completed in one year, with existing standard legal frameworks for securitization and collateral already being used. In fact, the first issuance of ESNI securities took place in April 2014 for some US\$3.5 billion. Furthermore, given such standardization, costs to both public agencies and the private sector have been negligible, nor would it be costly to extend to other jurisdictions. In addition, because of the credibility of the parties involved and the simplicity of instrument, the involvement of credit bureaus or other rating agencies has not been seen as necessary.

Ongoing Improvements in Data for Risk Management that Can Help SMEs

Another case study also focuses on improved infrastructure for SME finance, but in an entirely different aspect: “enhancing the credit report system, enabling better access to micro, small and medium enterprises (MSMEs) financial information.” In 1997 the Peruvian Superintendency of Banking began a long series of changes that made credit bureaus there far more effective in reducing risks and costs in lending, and to MSMEs in particular. The two most important initial changes were the inclusion of all loans, not just large loans, in the required information and the extension of coverage to a range of nonbank entities (municipal banks, rural banks, and micro and SME developmental lenders).

By 2001 further important changes had been made, including especially the availability of this information to private credit bureaus and the inclusion of an even wider range of debts and, most importantly in 2004, the disclosure of positive as well as negative information. For lending to MSMEs, this has meant far lower costs and better risk management. In 2001 there were 1.2 million clients with debts under US\$5,000 who had no credit records previous to that date. By the end of 2013, there were 4.4 million. These changes also led to a more competitive market and a significant decrease in interest rates. Of course, there are challenges that remain such as the technical demands of handling increasing amounts of data, the need to continue improving timeliness of data and maintaining its quality, as well as the fact that neither credit unions nor nonprofit entities are as yet required to participate, although some of them already voluntarily provide information.

Attempts to Introduce E-Money that Could Help SMEs, Especially in Rural Areas

A third Russian case study has a totally different focus: the use of electronic payment systems, which is based on a law adopted quite recently in 2011. Although this law with its accompanying regulations was fully supported by the Central Bank, the legislature, and the private sector as an important innovation, there has been little implementation as yet. The lack of use appears to be mainly a result of concerns about some of the regulations initially put in place that are seen to be unnecessarily restrictive, so that businesses do not see the value of using the electronic payment system as it currently exists.

Moving into SME Space Requires More Than Just Success in Microfinance

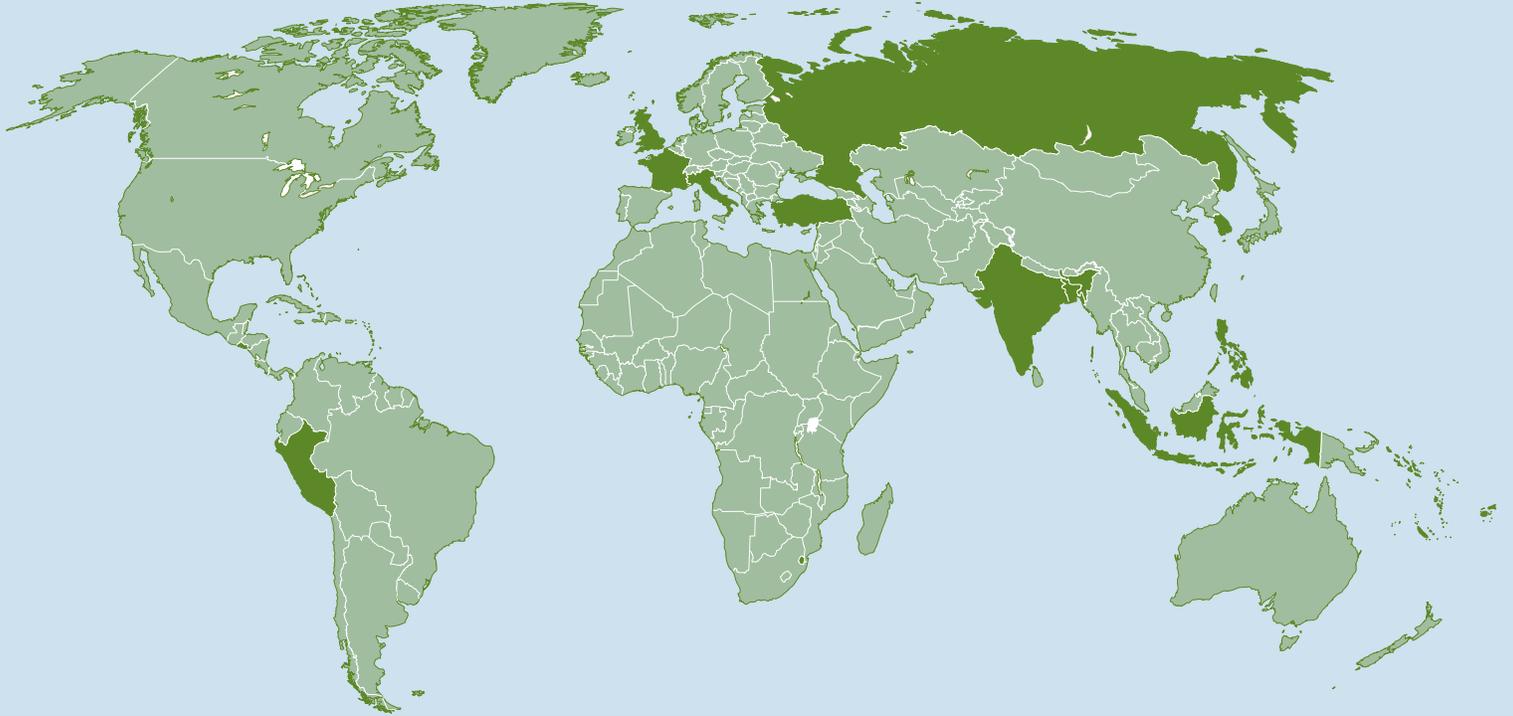
Based on its significant success in microfinance, the Philippines has made efforts to move up-market into SME finance, clearly recognizing the existence of a “missing middle” and the need to overcome this as a major part of its financial inclusion goals. But this has been less than fully successful as this case study shows. After initiating its efforts in microfinance in 2001, by 2002 119 banks were already engaged in microfinance, lending to over 390,000 micro-borrowers some US\$57 million. Moreover, by the end of 2013 there were 182 banks participating and reaching over a million clients with about US\$200 million in loans. On the other hand, its SME lending, which is called “Microfinance Plus” and allows loans twice as large (PhP300,000 rather than the limit of PhP150,000 on microloans), had only 20 banks offering Microfinance Plus loans by the end of 2013, reaching just 6,000 clients with only about US\$2.5 million in loans. Philippines officials state that they hope that ongoing work toward the establishment of a comprehensive credit information system and a collateral registry may eventually enable banks to ascertain the creditworthiness of potential SMEs.

Summary and Conclusion

Following the financial crisis that began in 2008, many governments turned to what seemed likely to have the most direct and immediate impact: loan guarantees and direct infusions of funds for lending to SMEs. Thus, a substantial number of the present case studies focus on such interventions. Nonetheless, a significant number of the current case studies take a longer-run view and focus on financial infrastructure or policies that can promote lending to SMEs, even though such new infrastructure and policies may take more time to put in place and then to have an impact on SME access to financial services.

Among the impressive efforts described in the case studies are the development of credit bureaus that can help to measure the likely risks of lending to specific SMEs, or improving the collateralization process that can reduce risks through improved laws and registries. Some of these innovative cases involve using intellectual property rights as collateral or formalizing the debts that arise in marketing chains as collateral to reduce the risks in lending to the smaller participants. Another case study describes a highly innovative program that rewards SMEs that give better treatment to women and other family members and even to employees, which then show better growth, profitability, and improvements in debt ratios and capital adequacy. Finally, one case even reveals the need to “do something more for SMEs” through improved policies and infrastructure—in this case simply allowing even highly successful micro-lenders to move “up-market” to SMEs—has so far led to little lender participation or added finance for SMEs.





Case Studies

Loan Guarantees

El Salvador: Loan Guarantee Fund for MSMEs

Indonesia: Establishment of Regional Credit Guarantee System

Italy: Loan Guarantee Fund for SMEs

The Russian Federation: State Program for SME Support

United Kingdom: Enterprise Finance Guarantee

Government Funding for SME Finance

Swaziland: Access to Finance for Local Indigenous SMEs

The Russian Federation: Federal Law on Microfinance/SMEs

Turkey: Angel Investment Scheme

Turkey: G43 Anatolian Venture Capital Fund

Turkey: Istanbul Venture Capital Initiative

Turkey: Venture Capital Investments

United Kingdom: Business Finance Partnership

Regulations Requiring SME Finance

Bangladesh: Accelerating SMEs' Access to Finance through Targeted Lending With Greater Women's Participation

India: Policy Initiatives in Cluster Financing

Policies and Infrastructure for SME Finance

France/Europe: Improving Financial Infrastructure through a Common Securitization Vehicle

Pacific Islands: Pacific Private Sector Development Initiative I

Pacific Islands: Pacific Private Sector Development Initiative II

Peru: Credit Bureau Implementation

Republic of Korea: Improving Women's Access to Finance Through Family-Friendly Companies

Republic of Korea: Win-Win Loan Package

Republic of Korea: Intellectual Property for Secured Loans

The Philippines: Policies to Implement Microfinance Plus

The Russian Federation: Laws and Regulations for Electronic Means of Payment

El Salvador: Loan Guarantee Fund for MSMEs

Started in 2012

Implementing parties: BANDESAL (Development Bank of El Salvador), Central Bank of El Salvador.

Background and Rationale

The financial crisis that began in 2008 had an especially adverse impact on small and medium enterprises (SMEs) and their access to finance. In addition, and perhaps even more significant, several important local banks were acquired by foreign banks. SME loans were then sent to foreign headquarters where the SME borrowers were unknown. The credit policies of these international banks have been stricter for all types of credit, due in part to informality, which impacts SMEs in particular. Furthermore, laws in El Salvador were not adequate for dealing with movable collateral, so this could not mitigate risks. Although El Salvador did have various guarantee programs, they were often undercapitalized, and required lengthy bureaucratic practices.

Description of the Intervention

A new law was quickly passed by the Legislative Assembly to strengthen the loan guarantee system. BANDESAL, El Salvador's well-regarded second-tier bank, is in charge of the loan guarantee intervention.

The need for an improved guarantee system was fully accepted by the banking system and bank regulators. When 23 financial entities were asked about their support for the new loan guarantee system, 15 immediately responded favorably (five commercial banks, two cooperative banks and eight "cajas de credito"). Of those responding, 93 percent said they intended to use it, and 77 percent stated that they were having good experiences with its functioning.

Results and Lessons Learned

As of June 2013, there were 4,117 guarantees amounting to US\$18.8 million, covering loans worth US\$32.4 million with an average guarantee of US\$4,566 (note again the small average loan size, suggesting many SMEs among the clients). Later figures from BANDESAL for March 2014 show the numbers of guarantees and the amounts guaranteed doubling.

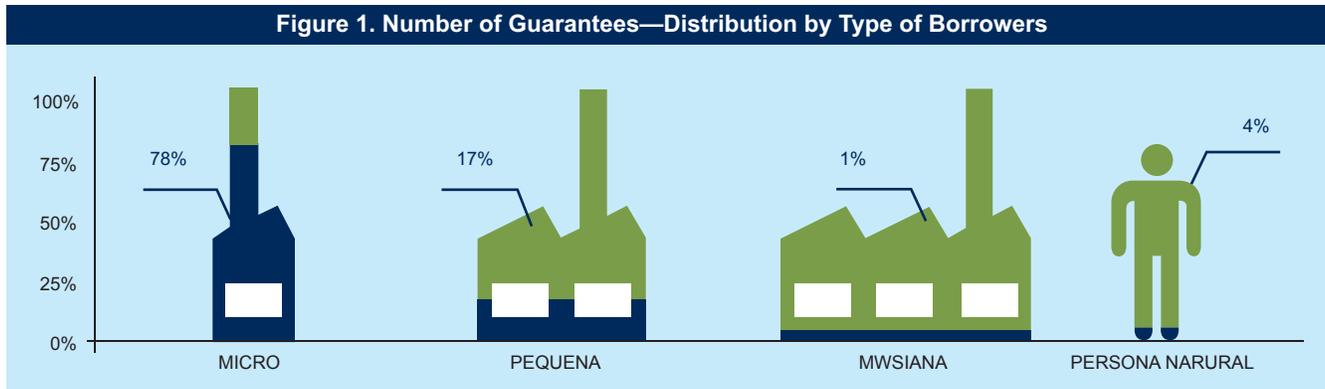
As of April 2014:

Amount of loans with participating financial institutions:

- US\$74.4 million
- Amount guaranteed: US\$42.2 million
- Number of guarantees given: 10,087
- Average amount of loans: US\$7,380
- Average amount of guarantees: US\$4,180
- Average percent of coverage: 56.65 percent
- Average period of guarantee: 31 months

During 2013, the amount of the loans guaranteed ranged from US\$1,311 to US\$35,711, with an average of US\$8,000, indicating clearly that it is serving small borrowers. Furthermore, less than 1 percent of claims were rejected.

One of the main points made by users of loan guarantees was that BANDESAL and Central Bank staff were strongly



Source: BANDESAL

committed to the effective design and functioning of the loan guarantee system and that there was an operating manual that was both transparent and followed what the users saw to be “best practices.”

Unlike earlier loan guarantee programs, the Central Bank and BANDESAL worked together under the new law. The

new program is adequately capitalized and more efficiently run (e.g., with transparency and rapid processing of claims). Moreover, the new loan guarantee system pays close attention to risks and has a model to estimate expected losses.

Submitted by:
Ricardo Contreras Perla, Senior Financial System Analyst
Central Bank of El Salvador

Indonesia: Establishment of Regional Credit Guarantee System

Started in 2007

Implementing parties: Ministry for Economic Affairs, Ministry of Cooperatives and SMEs, Ministry of Home Affairs, Bank Indonesia, and Indonesia Financial Services Authority.

Background and Rationale

Micro, small, and medium enterprises (MSMEs) in Indonesia comprise 99.9 percent of total business units in the country, or 56.5 million business units. MSMEs contribute around 57.9 percent to GDP, and account for a very high proportion of employment (97.2 percent), significant shares in investment (50 percent), and a significant proportion of exports (16.4 percent).

Thus, MSMEs have an important strategic role to help achieve equitable economic development. However, their access to finance is still limited. Financial access is crucial to MSMEs for expanding their businesses so that they can increase their contribution to the economy.

One of the main barriers for MSMEs in accessing finance from banks is the limited ownership of assets to be used as collateral. A survey conducted by Bank Indonesia in 2010 indicated that limited collateral was the largest barrier for MSMEs in accessing finance, followed by the lack of guarantee corporations and MSMEs' lack of knowledge.

Loan guarantee schemes can substitute for MSMEs' limited collateral, and help banks mitigate credit risk. Regional credit guarantee systems will help banks disburse sustainable loans to MSMEs and reduce the barriers to finance caused by businesses' lack of collateral. The establishment of regional credit guarantee corporations (at the provincial level) seeks to address these barriers to finance, and to increase MSMEs' role in achieving equitable economic development.

Description of the Intervention

Presidential Instruction No. 6/2007, concerning The Policy of Accelerating the Development of the Real Sector and small and medium enterprises, and Presidential Regulation No. 2/2008, concerning guarantee institutions created the legal basis for establishing regional credit guarantee corporations. Implementing these regulations to establish credit guarantee corporations (PPKD) required close coordination among stakeholders. In light of this, a joint effort at the national level was initiated by the Ministry of Cooperatives and SMEs, Ministry of Home Affairs, Bank Indonesia, and the Capital Market and Financial Institution Supervisory Agency (now Financial Supervisory Agency). The effort was coordinated by the Coordinating Ministry for Economic Affairs. It carried out the following activities:

- Issued regulations related to the establishment of PPKD. Regulation of the Minister of Finance No. 222/PMK.010/2008 has been issued as guidelines for establishing PPKD. The regulation was then amended by regulation No. 99/PMK.010/2011, which adjusted the capital requirement for PPKD, from IDR50 billion to IDR25 billion, to further enhance PPKD establishments. To encourage banks to guarantee their MSME loans, Bank Indonesia issued Bank Indonesia circular No. 13/6/DPNP dated Feb. 18, 2011, concerning Guidance for the Calculation of Risk-Based Asset for Credit Risk using a standard approach. Banks may get lower risk-weighted assets.
- Promoted and increased awareness of the stakeholders regarding the benefit of regional credit guarantee corporations, including increased access to finance by MSMEs.

- Held workshops to disseminate information and facilitate discussion among stakeholders, which include local governments, legislators, academics, MSMEs, and banks.
- Disseminated information. A guideline book covering PPKD establishment was issued as a reference for local governments that intend to establish regional credit guarantee corporations.

There were many challenges to establishing the credit guarantee system. Some of these included:

- The need for sufficient amounts of capital provided by local governments to establish PPKDs.
- The need to assure the related stakeholders about the importance and benefit of PPKDs for supporting access to finance by MSMEs.
- Achieving both profit and social objectives. By helping MSMEs’ access finance, expand their businesses, and create jobs, PPKDs could contribute to regional economic development. However, PPKDs bear the risk of loss if loans guaranteed to MSMEs are nonperforming, thus impacting the ability of the PPKDs to generate profit and be sustainable.

In addition, supporters of the intervention needed to be mobilized to make implementation successful through socialization, workshops, and focus group discussions. The targets of this mobilization were local governments, parliament, banks, academics, and MSMEs, with the objective of promoting the importance and benefit of PPKDs, and disseminating rules and regulations regarding their establishment.

Communication and coordination with stakeholders are important, particularly among executive and legislative branches to promote the legislature’s approval for establishing PPKDs and their capital fund.

Communication and socialization with MSMEs, as well as banks, was also important so that banks would be willing to use the guarantee system to mitigate risk and increase loan disbursements to MSMEs. Additional benefits are provided through banking regulations that provide incentives for banks to use credit guarantee schemes as tools to mitigate credit risk.

The following steps were taken to cope with the challenges:

- Revised regulations to lower the capital requirements for establishing PPKDs.
- Built communications with stakeholders.
- Issued regulations to support the use of the guarantee system.

Results and Lessons Learned

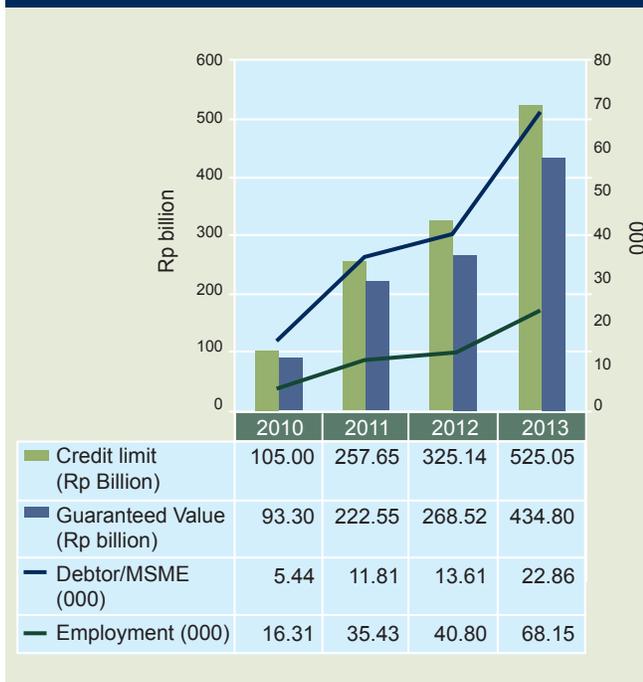
Results are measured by the number of PPKDs established. The coordinator at the national level arranges regular meetings for evaluation and monitoring, as well as identification of constraints and problems. However, there is still a need for further evaluation and monitoring to determine the impact of PPKDs on MSMEs receiving credit from banks.

Currently, there are eight PPKDs operating in eight out of the 34 provinces in the country. There are another four provinces that already have approval from parliament and are in the process of getting licenses from the Financial Supervisory Authority (FSA), while 10 other provinces are in the process of getting approval from parliament.

PPKD	Year of establishment
PT. Jamkrida Jawa Timur	2010
PT. Jamkrida Bali Mandara	2010
PT. Jamkrida Riau	2012
PT. Jamkrida NTB Bersaing	2012
PT. Jamkrida Jawa Barat	2013
PT. Jamkrida Sumatera Barat	2013
PT. Jamkrida Sumatera Selatan	2014
PT. Jamkrida Kalimantan Selatan	2014

There is increased use of the guarantee scheme by banks, as shown in Figure 1 by the increase in credit limits and values guaranteed for PT Jamkrida Jawa Timur in East Java Province. The guarantee scheme reached 53,725 MSMEs, which received loans from banks totaling IDR1.2 trillion (US\$101 million). The total guarantee coverage by the PPKD reached IDR1.1 trillion (US\$85 million). The total number of these MSMEs could absorb about 160,701 employees, based on information from the PPKD.

Figure 1. Trend of Loans for MSMEs Guaranteed by PPKD Jawa Timur



One lesson learned from the East Java Province is that success of a PPKD is mainly due to a strong commitment from the government and the link between the PPKD and local banks (especially rural banks and the regional development bank). Some reasons that a PPKD was not more successful were that banks were unwilling to join the program because of a lack of adequate incentives, and because of competition from other government guaranteed programs.

Another lesson learned is that stakeholders do not always have similar views regarding the importance of PPKDs, and PPKD establishment depends on approval by parliament. Post approval, a PPKD might still have obstacles in operating due to the failure of the regional government (either provincial or municipal) to provide adequate capital for the PPKD or in selecting qualified personnel for the board of directors.

Success of the PPKDs will depend on:

- approval from parliament;
- capacity of the regional governments to provide capital;
- commitment of the shareholders to provide additional capital when needed;
- willingness by banks to trust and use the credit guarantee system; and
- ability, willingness, and discipline of MSMEs to pay their obligations.

Recommendations to accelerate the use of credit guarantee schemes:

- Urge the re-guarantee mechanism to increase the capacity of PPKDs.
- Issue a new guarantee act to provide a stronger legal basis.

Submitted by:

Ms. Wini Purwanti A., Deputy Director, Bank Indonesia

Italy: Loan Guarantee Fund for SMEs

Started in 2010

Implementing parties: Ministry of Economic Development, Banks and Mutual Guarantee Fund, Management Committee of the Fund.

Background and Rationale

Fondo di garanzia (FG) aims to ease the access to credit for creditworthy but financially constrained SMEs. The rationale of the intervention is related to some characteristics of SMEs that exacerbate the problem of asymmetric information in a lending relationship (e.g. lack of information in financial statements, lack of collateral). These are long-standing and well-known issues, but they became prominent during the two recessions experienced by Italy over the last five years when the increase in borrowers' credit risk was coupled with increasing risk aversion by lenders. These developments help to explain the much greater role assumed by the FG during the economic downturn, as illustrated below.

Description of the Intervention

The scheme involves three parties: the FG, a firm, and a bank (or a mutual guarantee fund). FG is controlled by the Ministry of Economic Development and is managed on its behalf by a committee that includes representatives of associations of both firms and banks.

Eligible firms are financially and economically sound non-financial SMEs (as evaluated by data on the last two balance sheets). Some sectors such as agriculture, mining, automobiles, and transportation are excluded. The guarantee could be direct on a loan (requested by the lender) or could be a counter-guarantee (requested by a mutual guarantee fund).

The FG does not intervene in the characteristics of the loan (such as interest rate or length), which are determined by

the parties. The guarantee can be requested for loans aimed at covering both investment and/or working capital needs. The amount of the total loan guarantee could be up to €2.5 million, and the guarantee covers a maximum amount of 80 percent of the loan. Since 2009, the FG has benefited from a counter-guarantee by the Italian government, allowing banks to have a zero capital requirement for loans guaranteed by the FG.

The expected benefits coming from the use of the public guarantee funds were related to easing of credit constraints, as banks had the possibility to share credit risk and thus reduce the impact of lending to SMEs on regulatory capital.

The main potential risk related to this instrument concerns its effectiveness in terms of the additional lending induced. If the firms that receive the guarantee would have been financed anyway, there would be scarcely any impact on private sector access to credit. Moreover, the scheme has to be designed to avoid banks' moral hazard due to the limited liability mechanism and the related costs for government finances. Using their private information on borrowers' quality, in fact, banks could be prone to asking for the guarantee for firms closer to defaulting.

By using regression discontinuity techniques, a preliminary evaluation was performed by the Bank of Italy (which is not involved in the management of the fund). Based on firm-level information, it found that, at the threshold between eligible and non-eligible firms, the program had a positive impact on the volume of bank loans to firms, with a more muted impact on the interest rate charged by the banks. No relevant effects were found for firm investments and sales, although the FG considerably eased the financing of working capital.

Results and Lessons Learned

Since FG began in 2000, the volume of bank loans guaranteed has gradually gone up. With the inception of the economic and financial crises, the recourse to the FG increased greatly. From 2009 to 2013, more than €41 billion (more than US\$55 billion) of loans to SMEs benefited from the public guarantee (about 9 percent of loans below 250,000 euros, a proxy for loans to SMEs). The total amount of guaranteed loans between 2000 and 2013 was €52 billion (about US\$70 billion).

Data are available on the number of loans backed by the FG from 2007 to 2013 (around 300,000). The number of firms that benefited is lower, as firms can obtain a guarantee from other banks. In 2013, over 77,000 loans were guaranteed, and more than 51,000 firms benefited from the FG interventions.

The greatly increasing role of the FG after the financial crisis in 2008 and the subsequent recessions reflect the growing importance of this supporting measure to facilitate SMEs' access to credit. It represented by far the main instrument to achieve this objective. The increase in resources granted to the FG and the guarantee of the Italian government since 2009 were two important factors in ensuring the use of the FG by banks. The public guarantee funds also proved crucial in leveraging as much as possible the limited government resources.

A few aspects of interventions by the FG needed refinement, which were partly implemented over the last few years. For instance, before 2012, banks were authorized to demand the FG guarantee also after having already granted the loans to their borrowers. In these cases the effective transmission of the benefits of FG intervention to firms (in terms of lower interest rates or more credit) was extremely uncertain. Since 2012, banks have to ask for the guarantee before the firms' financing, and they must signal the interest rates that the firm would have to pay in both cases (i.e. with and without the guarantee).

Application procedures remain complicated and costly, so it is mainly larger banks that rely on it.

The main issue that arose during the crisis and challenged policy makers was the change in the threshold that distinguished eligible from non-eligible firms. On one hand, an increase was needed due to the general worsening of firms' financial conditions. On the other hand, an excessive opening of the selection process would have resulted in a large impact on the FG's funds.

*Submitted by:
Antonio De Socio, Economist
Bank of Italy*



Loan Guarantees

The Russian Federation: State Program for SME Support

Started in 2009



Implementing parties: Russian Ministry of Economic Development.

Description of the Intervention

The Ministry of Economic Development of the Russian Federation has developed a program to ensure SMEs access to financial services. The federal budget funds are provided as a subsidy to regions (on the principles of co-financing with the regional budget) for establishment and capitalization of regional guarantee institutions (regional guarantee funds). Regional guarantee institutions were established in 80 regions of the Russian Federation to provide guarantees for loan obligations of SMEs.

Guarantees are provided for credit, loan, leasing (financial lease) and bank guarantee contracts of SMEs. Liability of regional guarantee funds under the guarantee contracts shall not exceed 70 percent of an SME's obligations.

Results and Lessons Learned

As of Jan. 1, 2014, the total capitalization of the guarantee institutions is about US\$ 1.2 billion. Six funds (in Moscow, St. Petersburg, Samara, Novosibirsk, Rostov regions, and Khanty - Mansiysk Autonomous Okrug) have capitalization over US\$31 million.

Since the beginning of their activities, regional guarantee institutions have issued more than 39,000 guarantees totaling US\$3.6 billion. This volume of guarantees has allowed SMEs to attract loans in the amount of more than US\$ 7.7 billion.

In 2013, SMEs were given more than 7,000 guarantees in the amount of US\$0.9 billion, which allowed them to attract loans of more than US\$2 billion. As of Jan. 1, 2014, the outstanding portfolio of loans issued under the guarantee of regional guarantee institutions was US\$3.5 billion, which is 2.2 percent of the outstanding loans to SMEs in the Russian Federation (US\$158 billion as of Jan 1, 2014). These are guaranteed thorough guarantee institutions that are part of the Ministry of Economic Development of Russia program. This is a good coverage ratio. Other SMEs find their own sources to provide guarantees of loan repayment for banks—collateral or guarantees of third parties (individuals, etc.).

The Ministry of Economic Development of Russia estimates the efficiency of guarantee programs in each guarantee institution by the following “efficiency rate:” volume of loans to SMEs secured by guarantees to the capitalization of the guarantee institution. The average at the national level is 3. In more than 40 regional guarantee institutions the volume of loans secured by guarantees exceeds the capitalization by three or more times. In particular, in Voronezh, Kostroma, Murmansk, Saratov, Ulyanovsk and Yaroslavl Regions, Karachay-Cherkessia, Altai and Komi Republics, as well as in Zabaykalsky Krai and Stavropol Krai, the guarantee programs all received ratios between 5 and 7.

*Submitted by:
Elena Stratyeva, Director
Russian Microfinance Center*



Loan Guarantees

United Kingdom: Enterprise Finance Guarantee

Started in 2007



Implementing parties: Capital for Enterprise Ltd., British Business Bank.

Background and Rationale

SMEs with viable propositions have difficulty accessing finance as they lack the adequate security for normal commercial loans. The Enterprise Finance Guarantee (EFG) aims to increase the supply of debt finance to viable SMEs who fail to meet lenders' borrowing criteria.

Description of the Intervention

The EFG is a loan guarantee scheme to encourage banks to make additional lending to viable SMEs. Participating lenders determine whether a business is viable (able to meet the monthly loan repayments and repay the loan in full) but lacking adequate security to meet the lender's standard lending requirements. Lenders can then consider using EFG to facilitate provision of a loan.

The scheme is demand-led and acts as a complement to commercial lending, rather than a replacement. The delivery of EFG, including all lending decisions, is fully delegated to the lender who will decide whether use of EFG is appropriate. While the government provides a guarantee to the lender, it has no role in the decision-making process with respect to individual loans.

Lenders are provided with a government-backed guarantee for 75 percent of the value of each individual loan, which provides additional security to the lender in the event of default by the borrower. If defaults occur, the lender is obliged to follow its standard commercial recovery procedure, including the realization of security, before it can make a claim against the government guarantee.

Participating lending institutions were already involved with the predecessor Small Firms Loan Guarantee (SFLG) scheme and so were generally content to shift to using the new intervention. Although the overall extent of the guarantee cover provided was less generous, the approach to operating the intervention was more closely aligned with their normal commercial lending processes. SME representative and lobbying groups were also generally positive. There were few opponents as, at the time the intervention was launched, there was an almost unanimous view that government should act to assist SMEs facing difficulties accessing finance. Where there was adverse comment it tended to be because the commentator wished to see greater intervention, rather than objecting to the intervention provided.

The principal challenge to implementing the scheme related to the timeframe in which politicians demanded that the intervention be delivered. The idea was floated in late November 2008, the main parameters were agreed shortly before Christmas that year, and the intervention was to be operational from mid-January 2009.

An important secondary challenge concerned communications. Politicians were particularly keen to see the intervention operational and to promote it to business as government responding to the impact of the financial crisis on SMEs. As a result, there were instances of it being presented as a solution to other difficulties beyond the inadequacy of security. The lesson learned for other policy makers would be to focus on clarity of objectives, and to ensure consistent application of those objectives in all aspects of operational design, partner engagement, and wider communications.

Results and Lessons Learned

More than 20,000 businesses have accessed £2 billion of borrowing that would not otherwise have been possible. The wider economic benefits have been examined via an independent external evaluation conducted by Durham University Business School.⁷

To date, EFG has facilitated over \$3.3bn of lending to SMEs since launch in January 2009 to Q3 2013. In total, nearly 20,000 EFG loans have been drawn since launch.

At the outset, the objective was to have an intervention in place and available to service demand, rather than for it to be driven towards delivering specific numerical outcomes. Capacity was provided to meet all reasonable demand, so the principal objective was to maximize appropriate lending while ensuring that the lending was additional and that the guarantee was not simply facilitating the transfer to government of commercial risk that the lender would have otherwise carried in the normal course of its SME lending.

*Submitted by
Emma Sharp, Senior Policy Advisor
British Business Bank Strategy and Finance*

7. https://www.gov.uk/government/uploads/system/uploads/attachment_data/file/85761/13-600-economic-evaluation-of-the-efg-scheme.pdf

Swaziland: Access to Finance for Local Indigenous SMEs

Started in 2013

Implementing parties: Microfinance Unit, Swazi Commercial Amadoda, Swaziland Industrial Development (SIDC), SAMKHO Corporate Services.

Background and Rationale

According to the “Making Access Possible Diagnostic Study for Swaziland” conducted by CENFRI⁸ (2014), about 15 percent of the local adult residents are self-employed. It is estimated that 84 percent of these businesses are micro. The government’s goal is to support the promotion of the MSME sector to promote economic growth, particularly employment. Despite the local banks being high in liquidity, access to finance for the MSMEs has been recognized as a key constraint.

The Swaziland Industrial Development Company (SIDC) is a local development finance institution that provides leasing and equity finance. Its target group is mainly bigger businesses. Realizing the need to extend to the MSME sector, SIDC in 2012 expressed its intention to support the Swazi Commercial Amadoda (SCA) by extending credit to the micro and small entrepreneurs.⁹ A facility of SZL10.0 million (US\$1 million) was proposed. The SCA has a membership of about 12,000 entrepreneurs mostly involved in retail, services, and transport.

The loan requests included start-up capital, working capital, and asset leasing for the business sector. Since the applicants

did not follow a certain form for the applications, there was a challenge for the appraisal process, as SIDC did not have the capacity to deal with the large volume of varied applications.

Description of the Intervention

The Micro Finance Unit¹⁰ identified the need to help SIDC come up with an appropriate financial product that would accelerate the screening, appraisal, and decision on loan requests.

The financial product includes:

- **Standardized Administration.** This includes legal contracts, credit procedures, application process flows, and automation where possible to reduce administrative costs.
- **Product Feasibility.** Financial modeling to determine feasibility and ensure SIDC profit criteria are also met.
- **Scorecard Metrics.** Collateral/security provided, insurance, business history, contribution by business owner, business industry, loan required, etc.

8. A comprehensive study of the demand and supply situation for access to financial services in the country, conducted by the National Statistical Bureau with support from the FinMark Trust in South Africa, which engaged the Centre for Financial Regulation and Inclusion to assist in developing a Financial Inclusion Strategy.

9. According to the Revised MSME Policy a micro entrepreneur has 0-3 employees, assets valued at US\$5,000 and an annual turnover of US\$6,000. The small entrepreneur employs 4–10 people, with value of assets up to US\$200,000 and annual turnover up to US\$300,000. The medium enterprise employs 11–50 people, asset value up to US\$500,000 and an annual turnover up to US\$800,000.

10. The Micro Finance Unit is the entity of the Ministry of Finance that has been mandated to facilitate the development of an enabling environment for access to finance for SMEs, which entails working with the Ministry of Commerce to improve business start-up and their growth, and the Central Bank to make it easier for banks and nonbanks to extend outreach.

- **Risk Profiling.** High, medium, and low (e.g. previous loan experience, risk classification, loan size, feasibility, auto accept/reject, credit committee, and accept/reject).
- **Loan Amount.** New or veteran applicant, loan size, and the repayment period.
- **General Issues.** Commensurate interest rates, provision for bad debts and the cost of the product (both cost of capital and the operation), and the mentoring of the entrepreneurs.

The Micro Finance Unit supported building capacity in business management skills for entrepreneurs interested in accessing credit. The training entailed capacity in business idea generation, market research, business feasibility, cash-flow analysis, bookkeeping, and costing and pricing. This culminated in a process in which the entrepreneur could conceptualize and write a simple business plan.

The Micro Finance Unit provided intensive leadership and business management training for 30 committee leaders for all 12 SCA branches to enhance the operations of their branches and provide advisory services to entrepreneurs that would present loan applications. Also provided was engagement with Samkho Corporate Services and Altersol Consultants (business support entities) for mentoring and coaching to the entrepreneurs.

The responsible entities include: Micro Finance Unit, SCA, SIDC, Samkho Corporate Services and Altersol Consultancy Services.

Some of the challenges faced during implementation included:

- **Volume:** a large number of applications for credit.
- **Loan size:** the average loan requested was about US\$5,000, hence high administration and transaction cost.
- **Information asymmetry:** insufficient information on the businesses and the owners (lack of financial statements and good records).
- **Bankable business plans:** the lack of data to justify market share and revenue.
- **Fragmentation:** the wide dispersion and small size of the businesses.

During the implementation, there was an initial misunderstanding about the requirement for applying for the loan relative to the need for a simple business plan. Training for applicants in use of a simple business plan format helped. The low level of literacy of some potential applicants was also a challenge. Some entrepreneurs thought that since the credit facility targeted the group, all of the applicants would be granted the credit. Further, SIDC did not have sufficient staff capacity to conduct visits, and this was also not cost effective, given the dispersion and limited size of the businesses. Applicants were also disappointed by the long response time on loan applications.

It would be prudent for government policy to support the development of an effective database system that could provide accurate and timely data on the market situation and price information for key business sectors. It could also facilitate a framework that could enable credit information service providers to better assess credit history, and support the development of appropriate lending products for the MSMEs, such as the value-chain, and asset-based and invoice financing.

There was also a need to mobilize the entrepreneurs for business management training to ensure that they provided simple business plans. Some of the entrepreneurs withdrew, as they could not provide sufficient information to justify their business plans.

Results and Lessons Learned

It was mostly the bigger MSMEs that were able to benefit from the credit facility. US\$560,000 was disbursed to 17 businesses, representing 56 percent of the original target. The lack of information and the fragmentation of the small businesses required other complimentary mechanisms that would facilitate the pre-screening of the loan applicants and pooling together of the microloans to reduce transaction costs for SIDC.

The intention is to develop the capacity of intermediaries that will receive the wholesale amount to manage the documentation required for authorizing the disbursements through established supply chains.

The intermediaries will monitor the performance of these loans and develop data on the various types of businesses. The loan recipients will individually be responsible for repayment, which will reduce the transaction and

administration costs for the banks. The evaluation of the interventions is based on monitoring by the implementing agencies.

The experience from this intervention indicated that the need to address the lack of access to credit for the MSME sector requires collaboration with various sectors, such as the government (policy environment), entrepreneurs, and

business support entities. The financial product provided the right mechanism for SIDC to disburse the credit facility. Larger businesses have a better chance to receive finance as the businesses might have better data to support their business plans and some credit track record.

*Submitted by:
David Mfanimpela Myeni, National Programme Director
Micro Finance Unit, Swaziland*



The Russian Federation: Federal Law on Microfinance/SMEs

Started in 2010



Implementing parties: Russian Ministry of Finance, Russian Ministry for Economic Development.

Background and Rationale

The microfinance sector in the Russian Federation includes not only loans to SMEs, but also consumer loans. The term “micro” refers not to the division between micro and other enterprises, but to the division between micro (loans up to RUR 1 mln. or US\$30,620 as of Jan. 1, 2014, which are defined as “microloans” in the Federal Law N 151-FZ of July 7, 2010 “On Microfinance Activity and Microfinance Organizations”) and other loans.

The microfinance sector is represented by the following financial institutions: microfinance organizations (hereinafter – MFOs, as defined by the Federal Law N 151-FZ of July 7, 2010) and credit cooperatives (hereinafter – CCs, Federal Law N 190-FZ as of July 18, 2009, “On Credit Cooperation”), both referred to as microfinance institutions (MFIs).

The government program for SME development, implemented by the Ministry of Economic Development of the Russian Federation, has many ongoing activities, one of which is a program for the development of microfinance organizations. This program helps provide access to loans for small businesses that for some reason cannot use traditional banking products (e.g., due to small loan amounts, lack of credit history, remote business area).

A second program in this area provides financial support for SMEs through financing at reduced interest rates.

1. Support Program for SMEs Through Microfinance No 1 – the Ministry of Economic Development of the Russian Federation

Description of the Intervention

The ministry supports only microfinance organizations whose founders are regional (or municipal) government bodies. Such organizations are able to lend to small businesses relatively quickly and on favorable terms, resulting in bigger profits not only for an entrepreneur, but also for the microfinance organization.

Microfinancing of businesses, especially small businesses, can be deemed the best option for getting funds to establish and develop an enterprise, provided that loans to SMEs do not exceed 1 million rubles (or US\$30,620 as of Jan. 1, 2014—the maximum size of “microloan” is determined by Federal Law N 151-FZ of July 7, 2010) and the loan term is not more than 12 months. The term is determined by the rules of the microfinance support program for SMEs of the Ministry of Economic Development of Russia.

Subsidies to regions for the development of microfinance have been provided since the start of the program in 2005. The system works as follows:

- Money goes from the federal budget to the regional budget.
- Money from the regional budget is then distributed to regional MFOs (the founders of these MFOs should be the regional (or municipal) government bodies).
- MFOs then provide microloans to local SMEs.

Results and Lessons Learned from MFO Program

The volume of support to MFOs under the program has been increasing year on year. In 2005, subsidies from the federal budget in the amount of 23.5 million rubles (US\$0.85 million at the exchange rate on June 1, 2005) were allocated to implement the program in 16 regions of Russia. By 2011 and 2012 this figure had increased to more than 2.1 billion rubles annually (US\$69.2 million at the exchange rate on June 1, 2011 and US\$65.2 million at the exchange rate on June 1, 2012). In 2013, 2.2 billion rubles (US\$72.4 million at the exchange rate on June 1, 2013) were allocated for the development of microfinance in 35 regions of Russia. The major part of these regional subsidies from the federal budget (on the principle of co-financing with the regional budget) was for creation and capitalization of state (regional and municipal) MFOs. There were 3,860 MFOs in the registry as of Jan. 1, 2014, which issue both consumer and SME loans, but only state MFOs receive such support.

As of Jan. 1, 2014, there are more than 70 regional MFOs (a founder of a regional MFO is a regional government body) and more than 60 municipal MFOs (a founder of a municipal MFO is a municipal government body) created under the program of the Ministry of Economic Development of the Russian Federation with total capitalization of 18 billion rubles (US\$551.2 million). The existing loan portfolio is 10.5 billion rubles (US\$321.5 mn, 24,500 loans), which means that the share of state MFOs is around 29 percent of the loan portfolio of all MFOs, and 58 percent of the MFOs' portfolio of loans to SMEs. The state MFOs provide microloans at an interest rate of 10–12 percent. The program has a restriction on the margin of no more than 10 percent for loans given under the program. More than 10 percent is allowed in the case that an MFO borrows from additional sources.

As of Jan. 1, the share of overdue loans in the total loan portfolios of state MFOs is 6.4 percent, which is 0.7 percent lower than the national average for all MFOs (on Jan. 1, 2014 – 7.1 percent). An average loan amounts to 524 thousand rubles (US\$16,045).

As of Jan. 1, 67.5 percent of microloans have been provided to SMEs in the non-trading sector, including: 18.2 percent for SMEs in manufacturing, 13 percent in agriculture, 7.8 percent in consumer services, and 28.5 percent in construction, transport, and other areas.

The share of microloans with terms of 6 months to 1 year is 76.1 percent.

2. Support Program for SMEs Through Microfinance No 2 – Open Joint-Stock Company “Russian Bank for Small and Medium Enterprises Support”

Description of the Intervention

Open Joint-Stock Company “Russian Bank for Small and Medium Enterprises Support” (since 2011 – OJSM “SME Bank”) was established in 1999. One hundred percent of the bank shares are owned by the state corporation, Bank for Development and Foreign Economic Affairs (Vnesheconombank). Vnesheconombank is part of the government's plan to diversify the Russian economy, and to do so it receives funds directly from the general state budget.

OJSC “SME Bank” implements a program of financial support for SMEs, including the provision of financing for private and state banks, leasing and factoring companies, microfinance institutions (first- and second-tier MFOs and CCs) at reduced interest rates.

The bank focuses on the priority areas of the program. It supports SMEs in the manufacturing sector; innovation-driven SMEs; and entrepreneurs in regions with difficult socioeconomic situations. Two microfinance products for SMEs are particularly noteworthy: microcredit (up to 3 million rubles), implemented through banks, and microloan (to 1 million rubles), implemented through first- and second-tier MFIs (MFOs and CCs).

OJSC “SME Bank” started to support SMEs through MFIs in 2009. As of Feb. 1, 2014, the bank has cooperated with 26 MFIs. Up to now, MFIs have received 5,884 million rubles (US\$167.3 million) in loan funds, from which 7,189 SMEs have received more than 5,943 million rubles of support in the form of soft microloans (at the decreased interest rate). The outstanding loan portfolio under agreements with SMEs amounted to 1,442 million rubles. The number of active borrowers was 3,627.

Since 2010, support has been provided through banks that include microcredit in their product lines. As of Feb. 1, OJSC “SME Bank” has cooperated with 35 banks of this type. Upon receipt of 7,154 million rubles (US\$203.4 million) in loan funds, it has provided soft microcredits to 3,303 SMEs amounting to more than 5,621 million rubles (US\$159.8 million). Outstanding credit portfolios under agreements with SMEs amounted to 2,288 million rubles (US\$65 million), and the number of active borrowers to 2,137.

Results and Lessons Learned: OJSC

The following results have been achieved by the OJSC “SME Bank” (as of Feb. 1, 2014):

- Total amount of support provided to SMEs is about 96,713 million rubles (US\$2,749.1 million).
- The program has expanded to 82 regions of Russia.
- There are 134 active partner banks: 12,884 existing support agreements with SMEs. SMEs’ liability under these agreements is 76.40 billion rubles (US\$2.2 billion).
- There are 150 active partner infrastructure institutions (leasing and factoring companies, microfinance institutions (first- and second-tier MFOs and CCs) and

11,566 existing support agreements with SMEs. SMEs’ liability under these agreements is 20.32 billion rubles (US\$0.6 billion).

- 0.15 billion rubles (US\$4.3 million) were allocated to create financial infrastructure for SMEs’ support.
- Number of partners in the program for the entire period of its implementation totaled 247 banks, and 198 financial infrastructure institutions.
- Number of loan agreements between partners and SMEs for the entire period of program implementation totaled more than 65,000.

Submitted by:

Elena Strateyeva, Director, Russian Microfinance Center

Turkey: Angel Investment Scheme

Started in 2013



Implementing parties: Undersecretary of Treasury, Ministry of Finance-Revenue Administration.

Background and Rationale

SMEs and early stage firms in Turkey have limited access to finance because of their small size and lack of collateral required by traditional financing sources, such as banks. They also need mentorship to develop their business. In this context, a business angel scheme is a crucial mechanism to ease access to finance for entrepreneurs, increasing professionalism and improving business culture and ethics in this market. Government support has been essential to boost this sector.

Description of the Intervention

The law regarding the promotion of business angel investments was enacted by Parliament June 13, 2012, and the secondary legislation for implementation was put in force Feb. 15, 2013. The law encourages angel investments, which provide capital for SMEs by licensed business angels and introduces a new system for entrepreneurs and early stage companies having difficulties in accessing finance.

The Turkish Treasury licenses business angels who want to benefit from tax incentives for their investments. The Undersecretariat of Treasury is in charge and has conducted the activities and research concerning legislation for the business angel scheme. The undersecretary is also responsible for executing all activities regarding this legislation. Revenue Administration is in charge of providing tax support for the investments of licensed business angels. For this reason, the opinion of the administration was taken into account while the legislation was being prepared. Also, the Small and Medium Enterprise Development Organization (KOSGEB), other related public institutions, and private

sector entities (specifically angel networks and the union of trade chambers) all participated in preparing the legislation by sharing their experiences, knowledge, expectations, and views.

According to the law, business angels can either be experienced investors or high net worth individuals in order to be licensed. Licensed angel investors can deduct 75 percent of the capital they invest in certain SMEs from their annual tax base. This deduction ratio will be 100 percent for those investors investing in SMEs whose projects are supported by the Ministry of Science, Industry and Technology, the Scientific and Technological Research Council of Turkey, and the Small and Medium Enterprises Development Organization during the past five years.

In this system, business angels can hold less than 50 percent of the SME's shares, and the acquired shares must be held by investors for at least two years. An individual angel investment amount for an SME is a minimum of 20,000 TL (US\$8.928) and a maximum of 1,000,000 TL (US\$446.376).

Business angel networks are defined in the legislation and accredited by the undersecretary in accordance with the business angel scheme legislation. They are the Treasury's most important partners for the performance of the new angel investment system in terms of increasing entrepreneurial culture, awareness of the system, and the number of angel investors and investments. Since January 2014, license applications have been taken on accredited business angel networks.

Support for the intervention had to be mobilized. All related public institutions and private sector actors were asked to

share their experiences, expectations, and problems with entrepreneurship, SMEs, and the start-up of the sector. Then the legislation and other related actions for the system were prepared in compliance with the views of all possible supporters. Also, numerous meetings and seminars were arranged to increase awareness of the need for the angel investment scheme. Thus, supporters of the intervention have been mobilized by enabling all related actors to participate in the creation of the system and by communicating explicitly why the system is crucial for the success of Turkey's financial system.

Since the law entered into force, this regulation has often been reported in the press. Providing tax support has also had a positive impact on the sector. The government expects an increase in the number of angel investors and the volume of angel investments supporting early stage companies in terms of institutionalization, guidance, and financing. This mechanism will encourage the establishment of innovative start-ups, increase the dynamism of the economy, and contribute to stronger and more sustainable economic growth.

Major challenges that we anticipated include lack of solid entrepreneurial culture, low levels of awareness concerning the business angel scheme, and the risk that angel investors might take control of firms.

In fact, no major challenges were encountered during the implementation due to detailed planning, and the active participation of all the relevant stakeholders to create the legislation.

Results and Lessons Learned

Since February 2013, 250 business angels have been licensed, and five business angel networks have been accredited. Applications of three other angel networks are being evaluated. Also, seven angel investments of 2.950.882TL (US\$1.318.454) have been approved for tax support, and two investments of 420.000TL (Sept. 22, 2014, US\$187.572) are being assessed for tax support.

The number of licensing applications from business angels exceeded expectations for the first year. Success was driven mainly by having sufficient resources, the capacity and commitment of the implementers to respond quickly to the problems of all actors in the system, and activities to increase awareness of the program. Also, commitment and full support of other related public institutions and private sector actors have increased the success of intervention.

Submitted by:

*Hakan Ertürk, Undersecretary of Turkey, and
Kübra Öcal, Assistant Turkey Expert, Republic of Turkey*

Turkey: G43 Anatolian Venture Capital Fund

Started in 2011



Implementing parties: Ministry of Science, Industry, and Technology, Small and Medium Enterprise Development Organization (KOSGEB), the European Investment Fund.

Background and Rationale

The G43 Anatolian Venture Capital Fund Project (G43 Project) aims to develop financing instruments, and is being implemented under the European Union's Instrument for Pre-Accession Assistance (IPA)-Regional Competitiveness Operational Programme (Council Regulation (EC) No. 1085/2006 of July 17, 2006). The project was developed to improve the alternative investment market in Turkey, focusing especially on SMEs.

Description of the Intervention

The Ministry of Science, Industry, and Technology is the Operating Structure for IPA funds allocated for the Regional Competitiveness Operational Programme. KOSGEB, the leading organization for the support to SMEs in Turkey, is a key partner in the project and the End Recipient of the Assistance. KOSGEB is responsible for the management and performance of the operation. The EIF, through a Contribution Agreement, is the trustee administrator of the EIF-IPA Commitment. iVCi is the first dedicated fund of funds and co-investment programme, established in November 2007, for the benefit of the development of venture capital in Turkey. iVCi is used for the G43 Anatolian VC Fund project as it is an established investment platform created by both public and private actors for the benefit of the development of venture capital in Turkey. G43 leverages on iVCi which is directly supported by KOSGEB, the Technology Development Foundation of Turkey (TTGV),

and the Development Bank of Turkey (Türkiye Kalkınma Bankası AI). Garanti Bank, NBG Group, and the EIF are also partners in iVCi.

Functions and roles of all governing bodies in iVCi also apply to the programme, specifically the Investment Committee, the Board of Directors, and the Advisory Board. The iVCi Investment Committee is responsible for the approval of investments submitted by EIF. The implementation of the Operation will be monitored by the Steering Committee.

The results of the G43 project are identified as the establishment of a venture capital fund (by year 3) and equity capital provided to SMEs. The fund was established in 2012. The project will end in 2017. The term of the fund is determined as 10(+1) years.

Results and Lessons Learned

The project was activated with the signing of the Contribution Agreement Aug. 31, 2011, between CFCU (later the Ministry of Science, Industry and Technology), EIF and the EU. The fund was established under the platform of iVCi with the collaboration of EIF in 2012. Following the completion of the selection process, the fund manager was introduced to the region on Nov. 29, 2013, and it has started its research for investing in SMEs.

Submitted by:
KOSGEB SME Finance Department

Turkey: Istanbul Venture Capital Initiative

Started in 2007



Implementing parties: Istanbul Venture Capital Initiative (Specialised Investment Fund Company).

Background and Rationale

Entrepreneurs in Turkey have great difficulty in obtaining the financial resources they require for putting their business ideas into practice. Apart from financing the companies in which they invest, venture capital funds offer managerial and strategic support, which in turn makes a significant contribution to each company's growth prospects.

Description of the Intervention

iVCi, founded in 2007, was Turkey's first dedicated fund of funds and co-investment program. The investors in iVCi are KOSGEB, the Technology Development Foundation of Turkey (TTGV), the Development Bank of Turkey (TKB), Garanti Bank, the National Bank of Greece Group (NBG) and the EIF, which is the advisor to iVCi.

iVCi leverages the experience of the EIF, the EU's specialized financial body for SMEs and the risk capital arm of the European Investment Bank Group (EIB Group). iVCi's objective is to invest in assets representing risk capital over a long investment horizon (6-10 years). iVCi intends to achieve its objectives by constructing a balanced portfolio and investing primarily in:

- funds that invest their assets in private equity or venture capital (including first time funds, established funds, experienced funds, portfolio funds), and
- direct co-investments, alongside other pre-selected funds (co-investors) in companies or undertakings.

The venture capital and private equity (VC/PE) market was a nascent market when the initiative started in Turkey. The purpose of the program is to develop alternative investment vehicles in an undercapitalized market.

The total amount of commitments of iVCi is EUR 160 million with the contribution of the investors. Total funds raised by iVCi portfolio funds reached EUR 1.5 billion. iVCi has signed 10 commitments including a co-investment amounting to EUR 1,527 million. The total number of investments performed by iVCi's portfolio funds reached 33 companies. According to the subscription agreement of iVCi, it is envisaged that at least 25 percent of aggregate commitments shall be invested into other funds or in direct co-investments having SMEs as end beneficiaries.

Results and Lessons Learned

Already 45 percent of aggregate commitments have gone to SMEs (leveraged US\$92,128,088) as of March 31, 2014.

Fourteen SMEs have been reached as of March 31, 2014.

KOSGEB has had a considerable impact on the market. When iVCi was established, there were only two independently managed VC/PE funds in the market. iVCi stimulated the market and enabled several first-time teams to establish funds serving the market. In addition to the capital these funds provide to SMEs, they are instrumental in maintaining financial discipline and corporate governance, two traits that are becoming more important for international competitiveness.

The current net aggregate investment of iVCI into companies is EUR 74 million. This has leveraged EUR 525 million of investment into companies.

iVCI as a fund of funds has been instrumental in stimulating the VC/PE market. VC/PE investments are hands-on investments with a long-term horizon (typically three to five years). With the potential success of underlying portfolio funds, Turkey will have a number of funds with good track records, and will be proven as a PE market. As a result, more investors will be willing to invest in funds targeting

the country, further easing the access to finance problems of SMEs. VC/PE funds look for companies with high-growth potential and therefore target a niche segment of SMEs or companies. While such investments are very much needed in a country like Turkey, involvement of public agencies require a very good understanding of the long term, private, and exclusive nature of the asset class.

Submitted by:

KOSGEB (Small and Medium Enterprise Development Organization) SME Finance Department

Turkey: Venture Capital Investments

Started in 2006

Implementing parties: KOBİ Venture Capital Investment Trust

Background and Rationale

Currently in Turkey, it is virtually impossible for entrepreneurs who do not have adequate experience, capital, or collateral to provide the initial capital required to begin a business, or the additional capital necessary for expanding their businesses through the traditional means of utilizing various bank resources. Our company was set up by three main partners: TOBB, Halkbank, and KOSGEB to invest in local SMEs with innovative ideas that offer high growth potential by entering new markets, using new technology, or introducing new products and new ways of production.

Description of the Intervention

KOBİ VCIT provides financial and managerial support to SMEs that lack resources or capacity, even though they have an advantage over their competitors in terms of production and services. This support is given by the authority and supervision of our main partners, with SMEs then receiving both financial and managerial support. These amounts range from US\$1 million-US\$5 million, based on the evaluation of the SME. The investment is such that the company acquires a minority-preferred share of the SME for a planned period of five to six years.

Regional and sectorial presentations and meetings take place from time to time when the need arises. The purpose is to make our presence known to the market where our resources and knowhow can be used if and when the applying SME meets KOBİ VCIT's investment criteria.

The project applications are evaluated in line with KOBİ VCIT's following investment criteria:

- Entrepreneurial companies should comply with the definition of an SME (The definition under the latest published declaration by the Ministry of Industry).
- A project must be capable of creating differences and providing competitive advantages in the market or presenting a new product/service portfolio with a potential for development.
- The company should not have any outstanding tax, social insurance, or bank debt for immediate payment that is not seen to be payable when compared with expected short-term cash flow.
- The owners of projects should be knowledgeable of the relevant technicalities of their business and also have knowledge about the market, the company's customers, and business administration.
- The project owners should have a feasible business plan.
- The owners of projects and their respective team members should be innovative, experienced, active, and honest.
- KOBİ VCIT may exit from the project in five to six years. The company should be aware of this plan.

KOBİ VCIT invests up to 49 percent in a company, and prefers to be the minority holder at all times. Investment is made depending on the project's capital needs and also on the following: for projects at start-up stage, approximately US\$250,000; for information technology sector projects

with an existing company, at least US\$500,000; and for other sectors, a minimum of US\$500,000 and a ceiling of US\$1 million.

To date, we have made 10 investments with SMEs operating in sectors ranging from machinery to medical, plastic, and lighting. The main challenges include preparing and implementing business plans, following the company's strategy and even, at times, their day-to-day operations. The respective business plans have even been modified for some companies.

The main two challenges are to set up a manageable business plan, operate according to that plan, and to modify the plan when necessary. As each Turkish SME has its own particular challenges and difficulties, so do the sectors in which they operate. In other words, a "one-size-fits-all" business plan is impossible to implement. We often, if not always, face the situation where the business plans or models of each investment have had to be modified according to the company, sector, or economic need. This also includes injecting further capital into respective investments or subsidiaries if the need arises.

Results and Lessons Learned

Since 2006, KOBİ VCİT has allocated approximately 34.8 million TL (US\$20.5 million) to its investments or subsidiaries in the Turkish SME market, including both original investments and latter capital injections.

There have been 2,124 applications by SMEs, but only 10 have received investments. Even though this is a major area of criticism, the reason for such low numbers is that KOBİ VCİT's strict investment criteria have been set forth in our establishing notes by our main partners, which we heavily rely on.

The successes of the SME investments are measured based on their mid and year-end figures and to the extent that they have managed to meet the targets set forth in their business plans. All of our subsidiaries have increased their year-end sales figures dramatically since the investment date. This is largely due to KOBİ VCİT's successful strategic decisions and our major effect on their access to capital/finance, either through us or their credit lines via public and private banks.

All investments have proven to promote higher sales figures. Access to capital via KOBİ VCİT, combined with our managerial help, have allowed these companies to achieve higher returns. In cases where we have had to make major strategic decisions, including the demise of certain areas of operation or production, the SME was better able to focus on income-generating areas, and better allocate labor and financial resources, all fruitful for the company's financial results. The success of respective SMEs comes from easier access to finance via KOBİ VCİT, and the ability of KOBİ VCİT to supply managerial assistance through its presence on the managerial board of each company.

*Submitted by:
Onur Oktem, Deputy Manager Business Development
KOBİ Venture Capital Investment Trust*



United Kingdom: Business Finance Partnership

Started in 2012



Implementing parties: HM Treasury.

Background and Rationale

The government is investing alongside private sector investors on fully commercial terms through managed funds that lend directly to mid-sized businesses in the United Kingdom. The Business Finance Partnership (BFP) aims to ease the flow of credit to businesses in the country by helping to diversify the sources of finance available.

The BFP forms part of a package of credit-easing measures to support smaller and mid-sized businesses that do not have ready access to capital markets. This summary refers to the scheme for mid-sized businesses. There is also a much smaller scheme targeting smaller businesses.

Description of the Intervention

The government invested in new loan funds that can lend directly to mid-sized businesses, and offered to co-invest up to a maximum of 50 percent of any such fund. There is no sectoral restriction on where BFP funds can be invested and no blanket cap on the government funding that can be invested in any particular project. But, in order to ensure a spread of loans, limits of 10-20 percent of the total fund that could be invested in individual businesses or sectors were established.

Fund managers participating in the BFP can only lend to U.K. businesses with turnover of up to around £500m.

The scheme helped to create a deeper market and as such did not disadvantage existing players directly. As an example, one of the few existing funds in the market only created its second fund on the back of HMT funding. They confirmed

that without the investment they would not have established a subsequent fund.

Expected results were achieved with less funding than anticipated. The market is now attracting much higher levels of private funding than were required under the terms of the scheme. The results are measured by the activity of the funds and by actual loans made. We have full sight of the evidence as HMT is required to draw down funds for each loan as and when required. The funds are obliged to share information about the loan including name of the business, annual turnover, number of employees, and terms of the loan. This provides a good overview of activity and regular performance reports are provided by the funds.

The main challenges were linked to the timing of fundraising in the private sector versus a political desire to complete the investments quickly. It is not unusual for fundraising to take 12-18 months and managing expectations was difficult.

Results and Lessons Learned

Thirty-two loans have been made to date by six funds to 32 mid-sized businesses across a wide range of sectors. The loans have enabled these businesses to expand with loans over tenors that are generally longer and offer more flexibility than those offered by banks (10 years).

Expected results were achieved with less funding than anticipated. The market is now attracting much higher levels of private funding than were required under the terms of the scheme.

Having invested in six funds, we anticipated that HM Treasury would be investing 50 percent of each loan made to businesses. These expectations have been exceeded to date with HMT contributing less than 20 percent and therefore leveraging a greater percentage of private sector investment.

To date, a little over US\$2.2 billion has been generated, including matching private sector funds (HMT has contributed \$410 million). Over the life of the scheme, there is the potential for more than US\$6 billion to be generated.

While the program has been successful, there remains a limited appetite from U.K. investors in this asset class. It is important not to flood the market with too many opportunities at once as this could undermine the entire scheme as multiple funds were seeking co-investment from the same pool of investors. By phasing the investment across two tranches and six funds we were able to minimize this risk. But there was evidence that a seventh fund struggled to attract investment as a result of the six successful funds having already tapped the market.

Submitted by:

Matthew Gill, Head of Enterprise Policy, HM Treasury

Bangladesh: Accelerating SMEs' Access to Finance through Targeted Lending with Greater Women's Participation Bangladesh

Started in 2010

Implementing parties: 56 Scheduled commercial banks

Background and Rationale

Reducing poverty remains a formidable challenge for Bangladesh. Although Bangladesh experienced a stable growth rate of more than six percent on average during fiscal years 2007-13, steps are needed to increase this rate. Acceleration of the growth rate, however, requires substantial increases in private investment. Given the structure of private enterprises in Bangladesh, micro, small, and medium enterprises (SMEs) dominate and any development initiative must take them into consideration.

Bangladesh Bank, the Central Bank of Bangladesh, has undertaken numerous policy initiatives, regulations, and other activities for the development of SMEs by intervening specifically to reduce barriers that limit their access to finance and reduce or remove barriers to women entrepreneurs' access to finance.

There was market failure in targeting the sector by the market participants prior to Bangladesh Bank interventions. The share of SME credit to total loans and advances remained at a low level of 22 percent. Finance from banks and nonbank financial institutions (NBFIs) to SMEs did not match SMEs' contribution to GDP. This mismatch is due to their limited access to formal finance in terms of collateral, loan maturity periods, and lack of regulatory support systems. In addition, banks and NBFIs working in Bangladesh did not consider the SME segment as a profitable business line due to the perceived higher risk associated with SME financing.

Description of the Intervention

Bangladesh Bank created the SME & Special Programmes Department (SMESPD) with a focus on enhancing access to financial services by the underserved or unserved millions of micro and small entrepreneurs so that the financial services are extended to more people. The department started its journey toward the development of SMEs in Bangladesh by improving the existing environment in the banking sector through regulatory and policy interventions. Among others, the following interventions tremendously increased the level of MSMEs' access to finance:

1. Target-based lending activities by all banks and NBFIs.
2. Women's entrepreneurship development strategies.

1. Target-Based Lending

For the first time in the history of the financial sector of Bangladesh, a target-based SME lending program was initiated by Bangladesh Bank in 2010. Target-based lending has two distinct dimensions:

Target-1: Annual credit disbursement target to SMEs.

Target-2: Credit disbursement target to small enterprises (at least 40 percent).

The banks and NBFIs independently decide their targets. Bangladesh Bank simply monitors the achievement with predetermined indicators (achievement of disbursements to SMEs; loans to the small sector; disbursements to women

entrepreneurs; disbursements to manufacturing, service, and trading concerns; nonperforming loan ratios; and percentage of SME loan to total loans outstanding).

All 57 scheduled banks and 31 NBFIs have to set an annual target for credit disbursements to SMEs. The performance in achieving these targets is considered while licensing branches of each bank and NBFIs. Bangladesh Bank also puts significant weight on the performance of targets and achievements (including women entrepreneurs’ financing) in determining the CAMELS rating of banks.

The SMESPD conducted several meetings with all banks and NBFIs and motivated them to take MSME business as a separate business segment. The department encouraged the banks and NBFIs to promote MSME banking through high-level policy dialogue and seminars with chief executive officers, boards and training programs for bank officials to showcase how MSME banking can be made a profitable business.

It also provided liquidity and funding support to the accredited banks and NBFIs at the refinance and pre-finance facilities bank rate (currently five percent). With the efforts and interventions of SMESPD, all banks and NBFIs have opened a separate department for dealing with SMEs. They now consider the MSME segment as a profitable business. Moreover, there have been a number of banks and NBFIs that have specialized in SME banking, such as BRAC Bank Ltd. and IDLC Finance Ltd.

In addition to these supply-side interventions, Bangladesh Bank came forward with demand-driven endeavors with different organizations, chambers, and stakeholders to boost entrepreneurship. With the help of all banks and NBFIs and other MSME organizations, Bangladesh Bank is also organizing seminars, workshops, and training and skill development for MSME entrepreneurs. Most significantly, Bangladesh Bank also joined with different associations (e.g., Dhaka Chamber of Commerce and Industries (DCCI) and Institute of Diploma Engineers Bangladesh (IDEB))

to promote entrepreneurship and to help create new entrepreneurs.

With the help of JICA, the IFC, and the Asian Development Bank (ADB), Bangladesh Bank has trained more than 1,000 entrepreneurs countrywide. Recently, Bangladesh Bank also signed a project agreement with ADB to provide market-oriented training to 10,000 youths over three years.

Results and Lessons Learned

In 2010, a target of BDT 388.58 billion was set up for all banks and NBFIs. They disbursed BDT 535.45 billion to 308,950 enterprises (which was 138 percent of the target). The target for MSME credit disbursement for 2013 was fixed at BDT 741.87 billion, (BDT 151.75 billion higher than for 2012). All banks and NBFIs together disbursed BDT 853.23 billion to 744,228 enterprises, which was 115 percent of the annual target for 2013. For 2014, all banks and NBFIs have set an indicative annual target of BDT 887.53 billion for extending credit to MSME clients. This success is clearly attributable to the target-based lending approach along with promotional activities and indirect incentives in loan provisioning.

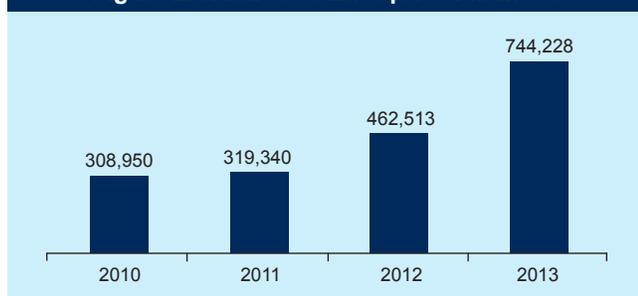
As a result of this intervention, an increasing number of enterprises now have access to formal financial institutions, and the trend has shown momentum in recent years. During the last four years, 1.84 million enterprises were financed with an amount of BDT 2623.40 billion (Figure 2).

The vast majority of micro and small enterprises are scattered throughout the rural areas of the country and play a critical role in creating employment and rural development. Bangladesh Bank therefore puts major emphasis on small enterprise financing by its SME Credit Policies & Programmes. In 2010, it instructed all banks and NBFIs

Year	Target (BDT in billions)	Disbursement		Achievement
		No. of Enterprises	Amount (BDT in billions)	
2010	388.58	308,950	535.44	138%
2011	569.40	319,340	537.19	94%
2012	590.13	462,513	697.53	118%
2013	741.87	744,228	853.23	115%
2014	887.53	–	–	–

Source: Bangladesh Bank



Figure 2. Number of Enterprise Financed

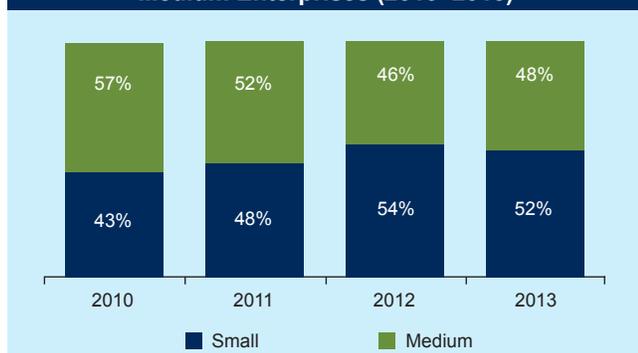
to disburse at least 40 percent of their credit to the small segment of SMEs. This has helped link rural, micro, and small enterprises, the vast majority of which are in rural areas, to formal financial services.

In this regard, Bangladesh Bank exempted banks and NBFIs having SME ratings of disbursing credit up to BDT 3.0 million to the small segment of SMEs. The bank instead established a mechanism for measuring the performance of SME financing by all scheduled commercial banks.

As a result, banks and NBFIs have extended their attention to financing rural SMEs, which in turn increased the share of small enterprise financing in total SME credit from 43 percent in 2010 to 52 percent in 2013 (see Figure 3).

2. Women Entrepreneurs' Financing and Development

The ratio of financing to small enterprises reached its highest level of 54 percent in 2012, but declined slightly to 52 percent in 2013. However, the number of small enterprises and the amount of disbursements grew significantly by 68.43 percent and 17.14 percent respectively in 2013. On the other hand, the number of medium enterprises financed in 2013 grew by 37.32 percent from 2012.

Figure 3. Ratio of financing to Small and Medium Enterprises (2010–2013)

Description of the Intervention

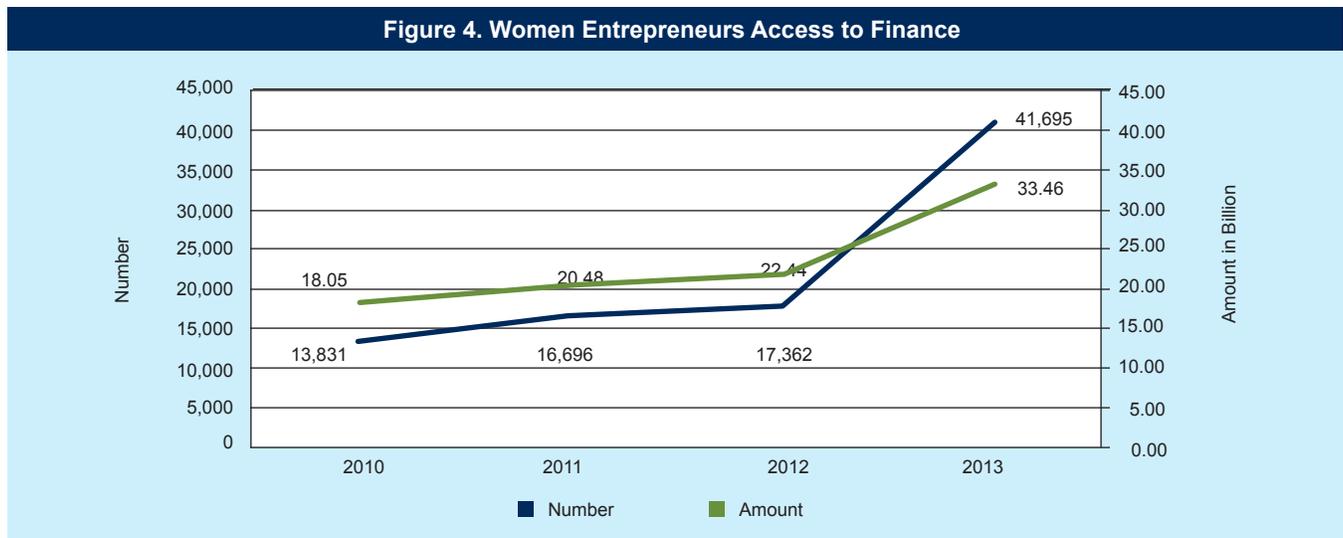
In Bangladesh, more than half of the population is women. Empowerment for women is one of our millennium development goals. We cannot progress as a nation if we leave women behind. Women face stricter requirements in accessing financial services from formal financial institutions. One of the priority areas for Bangladesh Bank is broadening financial inclusion to achieve inclusive economic growth. Promoting women's entrepreneurship was chosen as a tool for broadening financial inclusion, job creation, and women's economic emancipation.

A number of policy initiatives for women entrepreneurs have been taken so far to address the constraints causing the lack of access to finance, such as inadequate business knowledge and imperfect marketing policies. They include:

- Bangladesh Bank is managing several refinance funds for entrepreneurs. Fifteen percent of the total refinance funds for the SME sector has been allocated to women at a capped interest rate of the bank rate plus 5 percent (currently 10 percent).
- There is a provision for extending collateral-free loans to women entrepreneurs up to an amount of BDT 2.5 million.
- Group-based lending is allowed so that micro level women entrepreneurs have wider access to the formal financial system.

At the outset, banks and NBFIs were not much encouraged to finance women entrepreneurs. One of the reasons for their reluctance was that women entrepreneurs lack the ability to provide collateral. Women entrepreneurs also sometimes lack knowledge of business.

In this regard, Bangladesh Bank emphasized motivational measures for both bankers and prospective women entrepreneurs. To make bankers engage with women entrepreneurs in financing, Bangladesh Bank used "moral persuasion" at meetings with bankers. While providing refinancing to banks and NBFIs to cover their financing, priority was given to the cases of women entrepreneurs. Through December 2013, BDT 7.54 billion were refinanced to 9,612 women entrepreneurs, which was 22 percent of total refinancing. However, the share of women entrepreneurs financing to total SME financing by banks and NBFIs was only 3.60 percent. Thus, to create demand for women entrepreneurs' credit, Bangladesh Bank has



launched an awareness-building campaign through road shows, encouraging women’s chambers, and also providing training.

Results and Lessons Learned

The result of these initiatives is clearly shown in disbursements of SME credit to women entrepreneurs from 2010 to 2013 (Figure 4). Compared to 2010, the number of women entrepreneurs financed and the amount of financing increased by 201 percent and 85 percent, respectively, as of the end of 2013.

The private sector credit by the banking system in Bangladesh is still concentrated toward large enterprises or corporate sector financing. The results-oriented initiatives of Bangladesh Bank, especially its target-based lending and women’s enterprise development strategy, greatly increased access to formal finance by SMEs. Bangladesh Bank expects to pursue this results-driven approach to SME growth in the future.

Submitted by:
Md. Masum Patwary, General Manager; Md. Ashraf Alam
Deputy General Manager; and Syed Nazrul Islam
Deputy Director, Bangladesh Bank

India: Policy Initiatives in Cluster Financing

Started in 2004

Implementing parties: Ministry of Micro, Small and Medium Enterprises, Government of India, Reserve Bank of India, Banks and Financial Institutions.

Background and Rationale

In India, the MSME sector plays a vital role in manufacturing, exports, and employment generation, employing an estimated 59.7 million people spread over 26.1 million enterprises. The MSME sector accounts for about 45 percent of manufacturing output and 40 percent of total exports of the country. Public policy has accorded high priority to this sector to achieve balanced, sustainable, equitable, and inclusive growth in the country.

MSMEs primarily rely on bank finance for their operations, and so a timely and adequate flow of credit to the sector has been an important public policy objective. Over the years there has been a significant increase in credit extended to this sector by banks. At the end of March 2013, the total outstanding credit provided by all Scheduled Commercial Banks (SCBs) to the micro and small enterprises (MSEs) sector stood at Rs. 6,848 billion (US\$114.13 billion) as against Rs. 5,277 billion (US\$87.95 billion) in March 2012, an increase of 29.77 percent. Nonetheless, access to adequate and timely credit is still one of the constraints faced by the sector.

To expand access to banking services in all parts of the country, banks were advised to develop a roadmap for providing services through an outlet in every unbanked village with a population of over 2,000 by March 2012. The Reserve Bank of India advised banks that such banking services need not necessarily be extended through a brick-and-mortar branch but could be provided through business correspondents (BCs) or through any of the various forms of Information and Communication Technology (ICT). In addition, the Reserve Bank of India has advised banks to roll

out financial inclusion plans for drawing up an action plan to provide banking facilities in villages with populations of less than 2,000 through multiple channels. Progress is being closely monitored by the Reserve Bank of India.

Lenders are constrained from providing services to MSEs for a number of reasons, the foremost of which arises from a general perception among banks that the credit risk in lending to small and medium borrowers is very high. MSEs' lack of accounting records and inadequate financial statements or business plans also make it difficult for potential creditors to assess the creditworthiness of MSE applicants. In addition, high transaction costs for lending small amounts reduces the attraction for banks for MSE financing.

Recognizing the important role played by MSMEs in economic development and their contribution to employment and GDP, and realizing that financial access is critical for MSME growth and development, the Indian government and the Reserve Bank of India are taking the lead in supporting initiatives that improve access to finance. Financial inclusion, including MSME finance, and the drive to universal access is a national mandate, and so improving MSME access to finance is no longer a policy choice, but an imperative.

Description of the Intervention

India has adopted the cluster development approach as a key strategy for enhancing productivity and competitiveness, as well as capacity building, of MSEs. This approach was developed to provide banking services more economically, reducing costs and improving availability of services to MSEs.

A cluster is a group of enterprises located within an identifiable and, as far as practicable, contiguous area and producing the same or similar products or services. The essential characteristics of enterprises in a cluster are: similarity or complementarity in methods of production, quality control and testing, energy consumption, pollution control; similar levels of technology and marketing strategies or practice; channels for communication among the members of the cluster; and common challenges and opportunities.

Banks have been advised that a full-service approach to catering to the diverse needs of the MSE sector may be achieved through extending banking services to recognized MSE clusters by adopting a 4-C approach: customer focus, cost control, cross selling, and containing risk. Banks have been advised by the Reserve Bank to increasingly adopt the cluster-based approach for SME financing, since it can reduce transaction costs and mitigate risks. A cluster-based approach to lending is more beneficial for the following reasons:

- Banks deal with well-defined and recognized groups.
- There is appropriate information for risk assessment.
- Clusters can be monitored by lending institutions.

Clusters are to be identified based on factors such as trade records, competitiveness, growth prospects, or other cluster-specific data.

The entities involved in the implementation of the cluster-based approach include the government of India, which has identified the clusters; the Reserve Bank of India, which has issued policy guidelines to banks to encourage cluster financing; and the scheduled commercial banks that are implementing the guidelines. There has been no opposition to the initiative, as the guidelines have been issued by the Reserve Bank in its capacity as regulator of the commercial banks.

Adoption of the cluster approach by the government and the Reserve Bank has resulted in implementation of the following measures:

- At the state level, there is the State Level Bankers Committee (SLBC), the highest body of bankers, which discusses state-specific issues relating to credit flow. Such committees have been advised by the Reserve Bank to review the institutional arrangements for delivering credit to the MSME sector, especially for the 388 clusters identified by United Nations Industrial Development

Organization (UNIDO), which are spread over 21 states in various parts of the country.

- The Ministry of Micro, Small and Medium Enterprises has also approved a list of clusters under the scheme to improve the credit flow to identified clusters of micro and small entrepreneurs in 121 Minorities Communities Concentration Districts. In order to ensure smooth implementation of cluster financing by banks, the SLBC convener banks have also been advised to display on their respective websites the list of clusters identified by the Office of the Development Commissioner (MSME). They are also asked to identify MSME clusters where banking facilities are inadequate, to enable banks in the state to come forward to provide services in these clusters.
- Banks have been advised to open more MSE-focused branch offices near different MSE clusters. Banks have also been permitted to categorize their general banking branches having 60 percent or more of their advances to MSME sector as specialized MSME branches. Public sector banks will maintain specialized MSME branches in identified clusters or centers with a preponderance of small enterprises. To allow entrepreneurs to have easy access to bank credit and bank personnel with the requisite expertise. Although their core competence will be used to extend finance and other services to the MSME sector, they will also have operational flexibility to extend finance and render other services to other sectors and borrowers.
- To reach out to MSE entrepreneurs, the regional offices of the Reserve Bank have been advised to organize two to three town hall meetings each year in MSME cluster areas, preferably unbanked or under-banked clusters, to create awareness of banking facilities among MSEs and link them to the formal banking system. The idea is also to obtain feedback on problems faced by enterprises in accessing bank finance and thus create a base for two-way communication among stakeholders.

Results and Lessons Learned

The results of the initiative have been measured by the Reserve Bank of India. Tables 1, 2, and 3 reflect data received from 22 major public sector banks, 10 private sector banks, and 32 domestic commercial banks.

Outstanding credit from branches in MSME clusters stood at US\$44,818.93 million as of March 31, 2013, with public and private sector banks accounting for US\$31,451.14 million

Table 1. 22 Major Public Sector Banks

Date as on	No. of Branches	No. of Accounts	Amount Outstanding (Rs in Crores)	Amount Outstanding * (USD in millions)
31.3.2011	14032	1228435	143520.4	23920.07
31.3.2012	15288	1272439	163171.52	27195.25
31.3.2013	16524	1364431	188706.85	31451.14

Table 2. 10 Private Sector Banks

Date as on	No. of Branches	No. of Accounts	Amount Outstanding (Rs in Crores)	Amount Outstanding * (USD in millions)
31.3.2011	3255	369157	39690.77	6615.13
31.3.2012	3633	559439	64006.73	10667.79
31.3.2013	4219	718403	80206.74	13367.79

Table 3. 32 Domestic Commercial Banks

Date as on	No. of Branches	No. of Accounts	Amount Outstanding (Rs in Crores)	Amount Outstanding * (USD in millions)
31.3.2011	17287	1597592	183211.17	30535.20
31.3.2012	18921	1831878	227178.25	37863.04
31.3.2013	20743	2082834	268913.59	44818.93

*USD 1 = INR 60

and US\$13,367.79 million, respectively. Outstanding loans by MSME branches of the 32 domestic commercial banks located in clusters constitute roughly 40 percent of the total outstanding MSME credit by these banks.

There has been an increase in the number of branches in MSME clusters, the number of accounts, and outstanding credit of 17.76 percent, 11.07 percent and 31.48 percent, respectively, from March 31, 2011, to March 31, 2013 in the major public sector banks. The corresponding figures for the 10 select private sector banks were 29.62 percent, 94.61 percent, and 102.08 percent, respectively, during the same period. The strong growth in credit can largely be attributed to this initiative.

The success of the initiative can be attributed to the capacity and commitment of the implementing agencies. The active participation by public and private sector banks resulted in a win-win situation for the banks as well as the units in the MSME sector, with banks getting bankable projects and the MSME units getting access to timely and adequate credit.

Notwithstanding these measures by the government of India and the Reserve Bank, many of the clusters still suffer from problems arising from infrastructure bottlenecks. India's new manufacturing policy aims to address these issues wherever industry is able to organize itself into clusters and adopt a model of self-regulation.

*Submitted by:
Aridaman Kumar, Deputy General Manager
Reserve Bank of India*



France/Europe: Improving Financial Infrastructure through a Common Securitization Vehicle

Started in 2013

Implementing parties: Banque de France, international banks, Fédération Bancaire Française (French banking association), SNPP Securities Services, others.

The Euro Secured Notes Issuer (ESNI) initiative established a common securitization vehicle that:

- facilitates the refinancing on interbank markets of bank loans to SMEs; and
- relies on Banque de France's credit assessment of nonfinancial companies (nearly 300, 000 companies in France) and on banks' internal ratings-based (IRB) approach, validated by supervisors to ensure the high credit quality of the underlying assets.

Background and Rationale

In Europe, most SMEs do not have direct access to financial markets, and therefore they depend on banks for access to finance. At the same time, banks face difficulties refinancing SME loans on the financial markets.

In this context, French banks were looking to identify the conditions under which the use of credit claims as collateral could be increased, especially between credit institutions.

Bank loans to nonfinance companies, and to SMEs in particular, have proven to be a resilient source of collateral in credit operations with central banks during the financial crisis. However, they are underused as collateral both with central banks and their use is close to *nil* in a cross-border context.

The ESNI initiative offers a new way to mobilize credit claims in the form of securities. It aims to finance the real economy, especially SMEs, by allowing banks to use these loans as collateral to obtain liquidity, either on the market or from

the central banks (Eurosystem eligibility assessment under review).

Supporting a more efficient mobilization of credit claims to SMEs in the form of securities for collateral purposes is expected to increase the liquidity of these bank loans and to ease credit provision to nonfinance companies.

Increasing the overall amount of collateral that can be mobilized on the interbank market through the securitization of credit claims will offer banks more flexibility to manage their collateral baskets and address the additional needs for collateral that they face following the financial crisis.

Description of the Intervention

The French "Haut Comité de Place" (High Level Market Place Committee) began to explore the possibility of setting up a marketplace structure facilitating the refinancing of SME loans in 2012. This high-level committee is chaired by the Ministry of Finance and composed of representatives of the banking and financial sectors. The ESNI initiative is thus a private sector initiative that has benefited from strong support from Banque de France. A single and standardized Special Purpose Vehicle (SPV)—the ESNI—was established by several private banking groups in March 2014.

The first securities issuance performed by the ESNI took place on April 11, 2014, for EUR 2.65 billion. This is expected to be followed by additional issuances in 2014.

The sponsoring banks were strong drivers of this initiative, setting up the structure and issuing the first securities. But

the scheme also benefited from the input of several working groups involving a range of market participants (i.e., French credit institutions and other European banks active in France, as well as professional associations including the French Banking Federation). Representatives from the securities, regulatory, and banking supervisory authority have also been involved to ensure that the envisaged scheme is compliant with existing regulations.

After the first issuance, the banks began to promote the use of these securities as collateral (and potentially as an investment product in later stages) on the interbank market for repo operations, as well as for margin calls to increase the exchange of these securities as collateral.

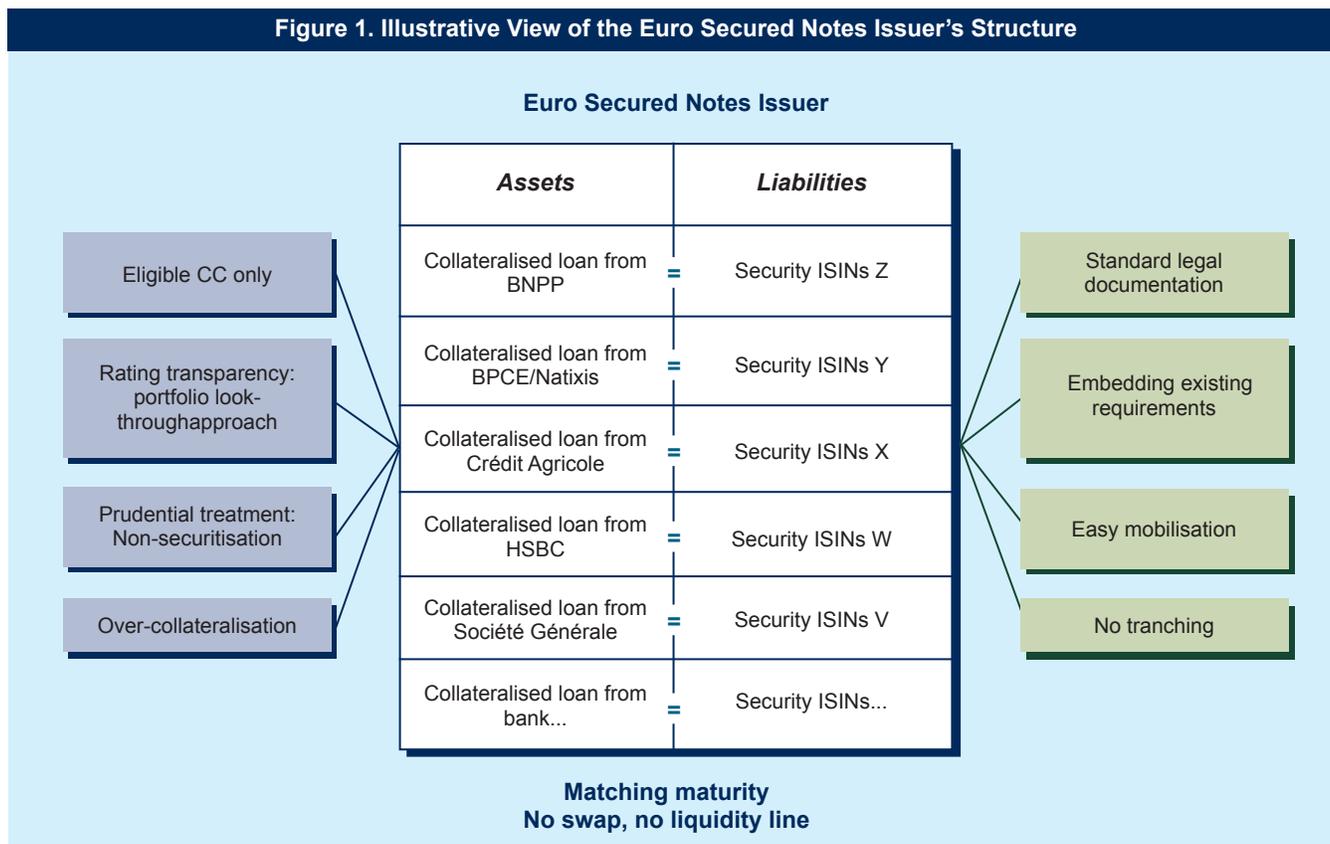
Finally, the Eurosystem is analyzing the conditions under which this type of asset could be accepted as eligible collateral in Eurosystem monetary policy operations.

ENSI created a simple (no tranching) and transparent instrument that aims at being replicated in several jurisdictions.

A single and standardized SPV was set up and shared by several banks. Each participating credit institution has its own independent compartment(s)¹¹ in the single SPV. Each compartment is bankruptcy remote from the other compartments of the SPV and is not submitted to any tranching. The issuance process consists in the issuance of securities by the credit institution’s dedicated compartment, these securities being secured by the credit claims collateralized in favor of the considered compartment (See Figure 1).

Banque de France provides information on the credit quality of the SME loans, as it operates an internal credit assessment system that covers nearly 300,000 companies in France. The use of Banque de France’s internal credit assessment system, complemented by the banks’ IRB, has allowed the issuance independent of rating agencies.

Figure 1. Illustrative View of the Euro Secured Notes Issuer’s Structure



11. Each credit institution can have one or several compartments in the SPV. The compartments of a bank are fully segregated from the compartment(s) held by other banks participating in the SPV, hence ensuring bankruptcy remoteness.

The ESNI has been designed to be as simple, secured, and as transparent as possible. This approach has allowed implementation of the structure and performance of the first issuances within a relatively short timeframe (about one year between the first version of the blueprint and the first issuance of securities).

No legal impediment was identified in setting up the ESNI¹², as this SPV relies on the standard legal securitization and collateral framework. Setting up a common structure based on standard legal and contractual documentation used by all participating banks paves the way for an increasing use of the vehicle in a cost effective manner.

Results and Lessons Learned

It is still too early to assess results. More time will be needed to measure the use of these securities as collateral on the interbank market and the impact on credit provision to SMEs.

However, the first issuance is promising, given the significant amounts issued and the involvement of the participating banks. Initial feedback from the market is positive.

In the future, indicators such as new issuances; the number of new banks participating in the process from France or elsewhere; the amount of trading of the securities on the repo market and their use for margin calls; as well as the impact on credit provided to companies, will be scrutinized to assess the success of the initiative.

The significant commitment of the French banking community and select international banks has been key to setting up the ESNI. This ensures that the vehicle is open to every bank.

This kind of initiative can be implemented at no extra cost for public authorities, and costs borne by the private

sector are very limited, thanks to the standardization of the legal and operational structure, as well as the simplicity of the structure. In jurisdictions providing a securitization framework, legal and regulatory adaptations are either very limited or unnecessary.

One potential concern with this model could be the absence of rating from a credit rating agency. However, several interested counterparties have attested that this was not an impediment in practice, given the transparency and simplicity of the instrument and the credit assessment performed by banks and central banks on the underlying assets. The promotion and development of alternative credit assessment systems (either central banks' systems or commercial banks' IRB) may be key for gaining independence from credit rating agencies.

The acceptance of these securities as collateral for central banks' operations would send a powerful signal regarding the willingness of public authorities to gain independence from credit rating agencies.

Other banks (French or international) are expected to join this vehicle as soon as possible, and after seeing the performance of the first issuance several new banks have expressed interest in joining. Meanwhile work on duplicating the scheme in other jurisdictions is underway. The scheme could be particularly instrumental in countries where the use of credit claims is not widespread, either due to legal constraints for the direct mobilization of credit claims to the Eurosystem or due to operational impediments faced by the central bank.

The stock of loans that could be covered by this initiative in France alone amount to several tens of billions EUR/USD.

Submitted by:

Alexandre Gautier, Head of Market Operations Department, and Thomas Ros, Deputy Head of Monetary Implementation Division, Banque de France

12. Some clarifications were necessary from the tax authorities, but this did not lead to identifying any roadblocks.



Pacific Islands: Pacific Private Sector Development Initiative I

Started in 2007

Implementing parties:¹³ Governments of the Solomon Islands and Vanuatu, Asian Development Bank.

Background and Rationale

The vast majority of businesses in Pacific island economies are either formal SMEs or informal microenterprises, with the large majority falling into the latter category. Even the largest businesses employ no more than a few hundred people, with economic activity overwhelmingly undertaken by SMEs and informal businesses.

Extensive analytical work preceding secured transactions reforms indicated that SME and microenterprise access to formal finance has been extremely limited. Financial institutions have been unwilling to lend unless borrowers were able to provide fixed property (land and buildings) as collateral. Since the vast majority of land in the Pacific region is communally owned, and therefore unavailable to be pledged as security for loans, SMEs were effectively shut out of access to finance. This not only reduced their ability to invest and expand, but also weakened incentives to formalize, so that a significant portion of economic activity took place in the informal sector. Further, women were especially disadvantaged because they had no rights to the limited amount of land that was allotted through individual title.

Before reform was implemented, traditional legal support for secured lending in both countries had its roots in legal forms established by either statute or common law derived from English law. Although uncertainties often surrounded land ownership and titles, many lenders considered mortgage

law strong enough to support secured lending. Secured lending was organized around various costly legal forms, some subject to registration and others not. Registries were cumbersome and offered limited information that was often unreliable. Other problems included:

- The secured lender's priority against third parties was not established by registration, but rather by legal formality, which technicality failed to consider all potential competing claims.
- The system was costly for borrowers because they had to pay substantial legal fees associated with loan documents, each of which was unique and had to be drawn up by a lawyer.
- Enforcement was expensive and uncertain.
- Lawyers needed to physically search several registries to determine if an asset had been pledged to another lender.
- The result was very limited access to financing by many businesses, especially smaller and unincorporated entities. Since access to finance is one of the reasons for firms to formalize, informality burgeoned because there was less reason to enter the formal sector.

Description of the Intervention

To achieve reform, extensive analytical work was initially undertaken to highlight the shortcomings and opportunity

13. The Pacific Private Sector Development Initiative (PSDI), a regional technical assistance program to promote private sector development in the Pacific region, implemented these reforms. The Australian Department of Foreign Affairs and Trade (DFAT), the New Zealand Aid Program and the Asian Development Bank fund PSDI.

costs of the existing system, using a combination of economic and legal analyses. This was then used for advocacy with both the private and government sectors to demonstrate the potential advantages of reforming the system. This resulted, in both countries, in formal requests for assistance from the government to the ADB.

A team of technical experts was formed, consisting of lawyers and economists, to help draft the law and undertake economic analysis. An important part of the process was establishing local steering committees to review the draft law. Because of the extensive consultations and seminars that highlighted benefits, opposition to changes did not pose a major challenge to achieving the reforms.

Both countries reformed traditional secured lending laws by establishing simplified “notice filing” registries, which operate electronically and without government registrar intervention.

These registries need the following information:

- Name and address of the secured party (the entity providing the loan or credit).
- Debtor’s name and address (the borrower).
- Collateral description (general or specific), including asset serial numbers (as when a security interest in a motor vehicle is recorded).
- Registrations are paperless, online and instantaneous, eliminating uncertainty about the exact time and date of recording the security interests. The overall cost of the reforms was relatively small, involving technical assistance to change the law and the installation of a registry, amounting to approximately \$300,000 and \$100,000 respectively. Documents submitted for

registrations are not examined, and no certificates are issued to provide evidence of the existence or validity of a security interest. Thus, the registry requires very little input from personnel, which greatly reduces costs.

Registration serves only two purposes:

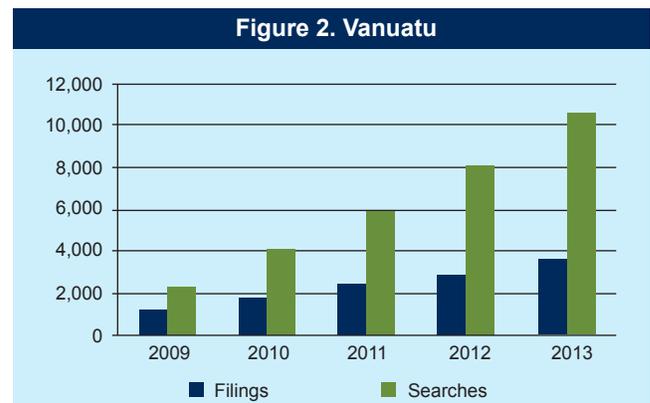
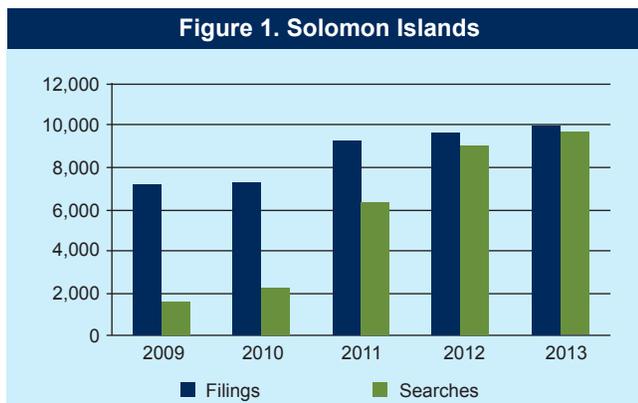
- To provide notice to the public to inquire further before buying or taking a security interest in property of the same nature described in the notice.
- To establish a priority date (the registration date) by which competing claims to collateral can be settled.

Results and Lessons Learned

The new system is inexpensive. In both countries, registration and filing fees for security interests are approximately US\$30, compared with several hundred dollars before the reforms.

Vanuatu has had a steadily increasing level of registrations, while the Solomon Islands have experienced considerable fluctuations. Figures 1 and 2 show the transactions filings and registry searches for both countries through December 2013.

Registrations data indicate that the majority of credit transactions involve borrowers located in the main province of each country, although Solomon Islands has a wider geographic distribution for credit transactions due to more developed centers of economic activity beyond the capital city, Honiara (Table 1). The proportions have remained consistent over 2009–2013, especially for Vanuatu. However, expanding mobile banking, greater awareness of the features of the reform, financial institution acceptance, and greater rural investment means that trends may change. At least



one financial institution in each country has expressed firm interest in expanding loan services in rural areas using nonconventional joint ventures that will undertake supply chain financing using secured transactions to collateralize loans.

Information on Gender of Borrowers: Both countries' registries software was upgraded to collect information on borrower gender, in July 2010 in Vanuatu and in August 2010 in the Solomon Islands. Women are actively using the secured transactions framework either as equal parties or as majority members of a borrower group (Table 2). Although women have registered a much smaller number of security interests than have men, the simplified registry process and the greater certainty introduced by the new framework are clearly encouraging women to take out loans.¹⁴

In both Solomon Islands and Vanuatu, there was wide consensus among financial institutions, lawyers, and central bank staff that: (i) the reforms had strengthened the potential for the financial system to provide financing to SMEs and microbusinesses; and (ii) both the laws and registries are functioning effectively. Procedurally, the registries have operated effectively to enable financial institutions to ensure that they have priority as the secured creditor, while the costs of processing loans have fallen dramatically. Of particular note is that nonbank financial institutions are using the new framework more intensively than commercial banks.

In Solomon Islands, the largest equipment finance company indicated that lending had increased by a factor of six as of end 2013, as a direct result of the reforms. Similarly, in Vanuatu, a large building and equipment wholesaler is beginning to provide financing for purchases, which it secures by the use of the new secured transactions framework. Both the equipment financier and the wholesaler indicated that their nonperforming loan ratios were less than two percent as of end 2013.

It is ironic that commercial banks still rely on lending secured by fixed property, which they say is extremely challenging to manage in the event of default, and on which nonperforming loan ratios exceed 20 percent. Lenders have not had problems seizing assets in the event of default. Their legal right to do so has been tested and upheld by the legal system. In practice, lenders have had little difficulty in repossessing and selling pledged assets without recourse to obtaining court orders.

By contrast, the nonperforming loans secured by moveable property—around 8-15 percent of all bank loans—total less than 4 percent. For finance companies and wholesalers, who are the most active users of the new framework, the nonperforming loan ratio is less than 2 percent. Bank regulators are beginning to ask about lending using the new framework and have shown active interest in its wider adoption.

Table 1. Geographic Distribution of Security Interests—Solomon Islands and Vanuatu

Year	2009	2010	2011	2012	2013
Solomon Islands—Main Province	63.0	90.9	48.8	56.5	61.1
Solomon Islands—Other Provinces	37.0	9.1	51.2	43.5	38.9
Vanuatu—Main Province	84.1	87.1	83.1	88.6	87.2
Vanuatu—Other Provinces	15.9	12.9	16.9	11.4	12.8

Source: Solomon Islands Secured Transactions Filing Office, www.stfosi.com Vanuatu Personal Property Securities Registry; www.ppsr.vu.

Table 2. The Gender of Borrowers with Secured Loans—June 2013

Country	Equally Men and Women	Majority Women	Majority Men	Indeterminable
Solomon Islands	51	567	1656	7457
Vanuatu	166	222	919	1719

Sources: Solomon Islands Secured Transactions Filing Office, and Vanuatu Personal Property Securities Registry.

14. Because gender disaggregated data were not available during the transitional filing periods and the first year of operation, it is not possible to ascertain whether larger numbers of women are borrowing compared with the old system. Anecdotal evidence suggests that they are.

Because secured transactions registries do not record the value of loans, data on the value of financing under the new framework are not available. It is also hard to estimate exactly how many SMEs have been assisted. However, interviews with lenders revealed that they were already providing financing to all of the large companies in both countries. They stated that almost all the increase in lending was to smaller businesses. Of the 8,000 new loans made in the two countries since the reforms, bankers and finance companies stated that a significant majority of recipients were either individuals or SMEs.

The most surprising aspect of the reform is the continued conservatism of commercial banks, which are far from fully using the new framework. In some cases they are not even aware that without registration of security interests, their loans have no priority over secured lenders nor that there is significant potential for creating new financial lending products. Banks in the Pacific region are highly profitable because of substantial charges for bank services, especially money transfers. Incentives to lend are therefore weaker than they might be in other regions.

A central lesson learned is the importance of implementation. It is clear that achieving the full potential of secured transactions reforms depends on further publicizing the advantages of the new framework for businesses, many of which are unaware of its potential benefits. Without more substantial effort to increase awareness, the new framework will continue to be under-used, and lending policies in both countries will remain overly cautious and conservative. Chambers of commerce would be natural partners, although they will first require significant training.

Success of the reforms also depends on working with lenders to help them use the framework and develop new financial products.

These measures will lead to more intermediation that uses the substantial liquidity that exists in the financial systems of Pacific island economies. They will deepen the reforms and further open access to credit. Given the positive reception of the reforms, familiarity will increase through the passage of time, with intensive implementation leading to the framework being more fully used.

Even with somewhat limited implementation, lending has expanded significantly. But much remains to be done before the full potential for financial market development from secured transactions reform is realized. Lenders need assistance to develop the far larger range of instruments to finance business activities than are now available. The benefits of secured transactions reform will take time to be realized and for new forms of lending to evolve. It is not realistic to expect an overnight transformation of lending. Full implementation could require up to a decade. However, the evidence from such reforms in New Zealand, Canada, and some countries in Eastern Europe shows that it provides a powerful tool to increase financing to businesses, particularly those that are smaller or unincorporated.

*Submitted by:
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Development initiative*



Pacific Islands: Pacific Private Sector Development Initiative II

Started in 2007

Implementing parties¹⁵: Government of Samoa, Government of the Solomon Islands, Asian Development Bank.

Background and Rationale

The goal of the initiative is to remove the obstacles arising from inadequate and outdated company laws in Samoa and the Solomon Islands for individuals who would like to engage in commercial activity using a company as the legal entity. These obstacles include:

- high costs and delays in setting up a company;
- business and company structures that are overly complicated and inflexible; and
- difficulty in accessing financial services and obtaining credit.

While most of these barriers also apply to men, they particularly disadvantage women who, in many cases, are already discriminated against in engaging in economic activity. The processes were so complicated and almost invariably required costly legal advice and assistance, so that many business owners simply chose to remain in the informal sector, with the associated low productivity and difficulty in accessing finance. Moreover, informality is not conducive to sustainable business success. The company law and registry reforms aim to facilitate a transition to the formal economy.

Before reform was implemented, in both countries, business registration was slow and costly. It was especially difficult in these widely scattered countries because the only way

to register a business was to travel to the capital, where the company registry was located and wait while all the legal processes were completed. Usually it was necessary to hire a lawyer, which involved substantial expense. The requirements for establishing companies also involved many outdated legal forms, such as minimum capital requirements, company seals, and several directors, all of which raised costs without serving any business purpose. In many cases, women were required to obtain signatures of male relatives before they could form companies.

Description of the Intervention

To achieve the reform, extensive analytical work was initially undertaken highlighting the shortcomings and opportunity costs of the existing system, using a combination of economic and legal analysis. This was then used as an advocacy tool with both the private sector and the public sector to demonstrate the potential advantages of reforming the system. This resulted in formal requests for assistance in both countries.

A team of technical experts was formed, consisting of lawyers and economists, to assist with the drafting of the law and undertaking economic analysis on the implications. An important part of the process was the establishment of local steering committees to review the draft law, to ensure that momentum was not lost, and to lobby government officials

15. The Pacific Private Sector Development Initiative (PSDI), a regional technical assistance program to promote private sector development in the Pacific region, implemented these reforms. The Australian Department of Foreign Affairs and Trade (DFAT), the New Zealand Aid Program and the Asian Development Bank fund PSDI.

and politicians. This helped overcome the main challenge of inertia in the political system that could have extended the reform period far beyond what was actually achieved.

The Companies Act reform commenced in Solomon Islands and Samoa in 2010 and 2012, respectively, accompanied by the installation of fully electronic company registries.

The new company laws provide for simplified and automated incorporation processes, which significantly reduce the monetary and time costs of establishing a business. For example, while companies are still free to adopt their own tailored rules on matters such as the appointment, removal, powers of directors, rules for meetings, and shareholder rights, doing so is no longer mandatory under the new Companies Acts.

Companies can simply adopt the model rules already contained in the new acts, eliminating the need for lawyers and reducing costs. The provisions for online application and payment also make company incorporation considerably more convenient. In addition, electronic incorporation processes eliminate discretion (administrative and political), which makes it very difficult for any gender discrimination to occur. Furthermore, the new processes directly identify any reporting and disclosure failures, which keep records up to date and reduce administrative costs.

The new company laws also include innovative company structures, such as the single shareholder company, designed to allow maximum flexibility for entrepreneurs to set up and manage a business without other external ownership influences. For example, this gives women greater control over their business operations and income by removing the need for a second, usually male, owner. In addition, the new Companies Acts provide more flexible regimes of company meetings and resolutions, allowing greater ease of participation.

In the Solomon Islands, a community company structure has also been introduced, which is a more transparent and accountable alternative to informality or to establishing trusts and cooperatives. It has great potential for managing royalties received from resources and payments received from leases of customary land. There were 17 community companies in the Solomon Islands as of Dec. 31, 2013.

Results and Lessons Learned

The new registries are accessible from anywhere with Internet access, 24 hours a day, 7 days a week. The online registry has made it cheaper and faster for new businesses to incorporate by cutting through red tape, such as ministerial approvals for company names, requirements to produce company seals, and eliminating the need to hire a lawyer to travel back and forth to the main centers of Honiara in the Solomon Islands and Apia or Savai'i in Samoa, except to make payments. Cost of incorporation is SBD 1,250 (approximately US\$100) in Solomon Islands and ST 250 (approximately US\$106) in Samoa. Typically, before the reform, the cost of incorporation using a lawyer was US\$1,000–US\$2,000. For someone in the provinces, travel cost would double this amount. The time taken to form a company has been reduced to a maximum of one to two days from six weeks in the Solomon Islands and two to three weeks in Samoa as a result of the reforms.

As Figures 1 and 2 show, registrations in both Samoa and the Solomon Islands have increased substantially after the launch of the electronic registries. There are now on average 271 new companies incorporating each year in the Solomon Islands, more than double the pre-reform registration rate. In Samoa, the number of incorporations following the launch of the online registry doubled the average incorporation rate over the previous five years (2008–2012).

Figure 1. New Incorporations Per Year in Samoa

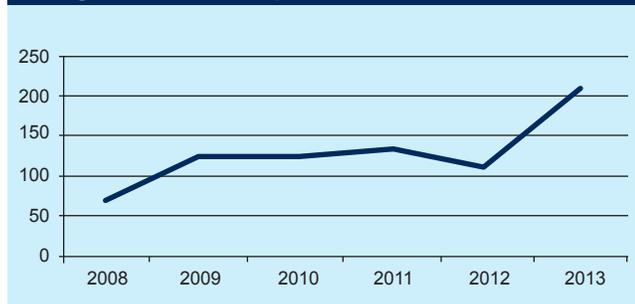


Figure 2. New Incorporations Per Year in Solomon Islands

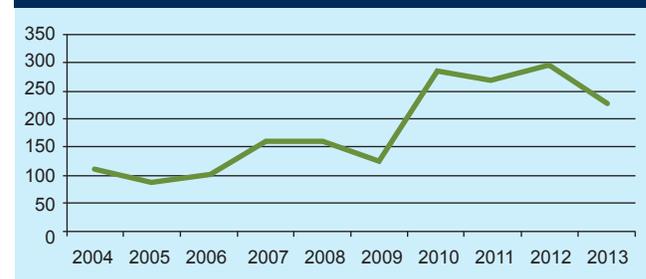


Table 1. Gender of Company Directors and Shareholders in Samoa

Date	Directors					Shareholders				
	Male	% Male	Femal	% Female	Total	Male	% Male	Female	% Female	Total
Feb-13	1,749	68%	810	32%	2,559	1,767	62%	1,088	38%	2,855
Dec-13	1,799	68%	845	32%	2,644	1,877	62%	1,139	38%	3,016

Table 2. Gender of Company Directors and Shareholders in Solomon Islands

Date	Directors					Shareholders				
	Male	% Male	Femal	% Female	Total	Male	% Male	Female	% Female	Total
Dec-10	2,163	77%	663	23%	2,826	1,934	73%	718	27%	2,652
Dec-13	3,658	78%	1044	22%	4,702	2,622	74%	904	26%	3,526

Table 1 and 2 provide information on the gender of company directors and shareholders in both countries. In the Solomon Islands, the number of female company directors increased from 663 to 1,044, while female shareholders increased from 718 to 904 (which represents a slight fall as a percentage of the totals). The number of female company directors and shareholders also increased in Samoa although given how recently the reform occurred, it would be premature to draw any firm conclusions from these data.

A survey of company administrators and business services providers one year after the respective launches found that:

- registering and maintaining companies was significantly easier after the reforms;
- electronically searching the registry for names of directors and shareholders and for examining the articles of incorporation saves substantial amounts of time and money; and
- the ease of access to information has assisted with company administration, accounting, and auditing activities. The company law reforms not only make it easier and more affordable to set up a business, but also provide for simple formal corporate structures, such as single shareholder companies with minimal reporting requirements that are well suited to less developed countries. These are ideal company forms for SMEs.

Banks in both countries are actively using the online registries to search for information on company ownership, directors, signing authority, location, and other basic information that is part of loan decisions. Again, the availability of reliable

essential information removes some of the uncertainty that financial institutions and others have in dealing with SMEs. Furthermore, this information can be obtained at no cost.

The transparency provided by the registries has also been useful for police, tax authorities, and journalists in verifying information for politicians and civil servants, reducing the potential for corruption.

A key element of success of the reform was the extensive pre-reform consultation and the post-reform implementation, which will ensure that the reforms are sustained for the long term. Ongoing engagement with company registries personnel provides the opportunity for feedback and to identify any elements of company law that would benefit from an updating amendment. In Samoa, for example, an amendment is being proposed for an easier company removal process to improve efficiency and compliance. In Samoa, a reporting tool has been developed that substantially improves the capacity to monitor basic indicators and the compliance of companies, including the filing of annual returns.

A key issue identified post-reform is the need to develop online payment systems so that registration fees can be paid electronically. Although work toward solutions is being undertaken in both countries, electronic payment processes are not yet in place.

Submitted by:

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Peru: Credit Bureau Implementation

Started in 1997

Implementing parties: Superintendency of Banking, Insurance and Pension Funds.

Description of the Intervention

In 1997, an important expansion of the Credit Bureau of the Superintendency of Banking, Insurance and Pension Funds of Peru (SBS) went into operation. This change consisted of going from receiving information from debts above US\$5,000 from banks and financial institutions, to receiving information on all the debts in their portfolios from S/.1 (US\$0.35), and including within the scope microfinance regulated institutions, such as Municipal Non-banking Institutions (CMAC), Rural Non-banking Institutions (CRAC) and Micro and Small Enterprise Development Entities (EDPYME).

From 1998 to 2001, several more changes occurred in the design of the formats used to report loan information, to expand the data captured, including risk classification of debtors, payment indicators, write-offs, and loan portfolio sales. Currently, SBS receives through its Debtors Credit Report (Reporte Crediticio de Deudores–RCD) more than 40 items of information per debtor from each reporting institution. These credit records were also made available for private credit bureaus (created by Law 27489 in 2001), which offer this information to the general public, along with additional information from other sources, such as utility and school fees payments and debts in some nonregulated institutions.

The decision to expand the credit bureau was mainly intended to strengthen SBS's credit risk supervision and to improve the ability of supervised institutions to evaluate the risk levels of potential and current clients. Expansion of the credit bureau's coverage carried other benefits as well, because this information was also used to make the financial

market more competitive and transparent. In addition, the possibility of building a credit history made credit accessible to more people. This benefit was enhanced in 2004 when both positive and negative (performing and nonperforming loans) information became available. Before that year, only negative information was revealed.

In the field of supervision, information received through the RCD enables a better evaluation of credit risk levels in each financial institution, as well as regional or sectoral analysis, thanks to the different identification parameters included in the report. In fact, many studies for evaluating the feasibility of new regulations are made based on this information.

For financial institutions, credit risk analysis for small loans is expensive, especially when there is little information available. Since the credit information is publicly available, it may also be useful for third parties as references for business relationships.

To achieve the implementation of the new credit bureau, the SBS had to expand its capacity to process all the information that would be received, which was far more than what was being processed in 1997. Implementation was made possible by modernization and technological changes inside the SBS through various projects and financial support from the Inter-American Development Bank (IDB).

Technology was also a major challenge for financial institutions, especially microfinance institutions, since they had to make their own systems adequate to comply with the periodic information requirements and the quality standards demanded by the supervisory authority.

The detail of information to be revealed to the system was another important issue. SBS requires very detailed information about debtors and current debts for supervision purposes. However, not all of this information can be revealed outside the system, given the need to evaluate the balance between transparency and the protection of information. Today, the information that is revealed through the Consolidated Credit Report (Reporte Crediticio Consolidado–RCC) includes identification of debtors, current, contingent, and total debt to institutions in the financial system, as well as default records and risk classification. Since this is a regulatory obligation imposed by the supervisory authority, participation in the new credit bureau is mandatory for all supervised institutions.

Still, there is a universe of unregulated MFIs (mainly credit unions and nongovernmental organizations) that are outside the scope of these information requirements. Some of these institutions are resistant to sharing their information, especially in an effort to maintain the exclusivity of their clients. However, private credit bureaus have been working in cooperation with microfinance networks¹⁶ in order to make information available at lower costs for MFIs, while also encouraging these same institutions to share their information.

Results and Lessons Learned

The new information managed by the SBS Credit Bureau provided the system with standardized information, both positive and negative, thus reducing the cost of credit evaluation for institutions. Clients who show good credit records benefit from new opportunities for more and better access to financial services, as well as being targeted by

more institutions. By January 2001, there were 1.2 million clients with debt amounts under US\$5,000. By December 2013, that number rose to 4.4 million. This means that prior to the expansion of the scope of the credit bureau system, debts of these clients were not registered, meaning that those clients had no opportunity to show the system their credit records.

A direct benefit of the credit bureau information is that it has allowed the definition and analysis of different types of credit, in particular those granted for business purposes. To assist the supervision of credit risk, the Peruvian regulation uses the information on the debtor's total level of indebtedness in the financial system as an important parameter to define different types of credit granted for businesses purposes.¹⁷ Based on this criterion, microcredit was defined for the first time in 1997 as a special type of credit,¹⁸ different from commercial loans, which applied to larger firms. In 2001, the microcredit definition was adjusted to better match the size characteristics of the demand.¹⁹

Finally, in July 2010, after a careful analysis of the credit bureau information to identify different risk profiles and the characteristics of the debtors, a significant regulatory improvement was made, fine-tuning the definition of microcredit and disaggregating commercial credit. Thus, in addition to microcredit, the following types of credit granted for business purposes were defined: small enterprise credit, medium enterprise credit, large enterprise credit, and corporate credit.²⁰ These definitions allow a more accurate risk evaluation of debtors, recognizing the different market segments and making the estimation of loan loss provisions more consistent with the heterogeneity of the Peruvian credit market.

16. COPEME, an NGO association, in partnership with EQUIFAX, the leading private credit bureau in Peru, has been very active in promoting information sharing among microfinance oriented NGOs.

17. This definition is created for supervision purposes. Other definitions exist, based on number of employees and annual sales, which are provided by the Law N° 28015 "Promotion and Formalization of the Micro and Small Enterprise Law," and mainly used for tax and labor regulation purposes.

18. Regulation issued in 1997 differentiated between two types of business credits: Microenterprise and Commercial. Microenterprise credits were defined as credits granted to physical or legal persons meant to finance production, commercial activities, or services, in enterprises with a level of assets or total indebtedness in the system no bigger than US\$20,000. Commercial loans were any other credit intended for business purposes that did not comply with the previously mentioned conditions.

19. New regulation increased the limit of total debt in the system to US\$30,000 and excluded asset levels from the definition.

20. Until June 2010, regulations contemplated four credit types: Micro Enterprise, Commercial, Consumer, and Mortgage Loans. From July 2010, eight credit types were defined: Micro Enterprise, Small Enterprise, Medium Enterprise, Large Enterprise, Corporate, Revolving Consumer Credit, Non Revolving Consumer Credit and Mortgage Loans.

Micro and small credit are defined based only on the total indebtedness of the borrower,²¹ both having similar regulatory treatment. Based on the risk proportionality criterion and with the purpose of easing access to credit, the regulation allows lower client documentation requirements at the time of loan origination. Debtor's risk evaluation can be based only on the number of days the loan is overdue. Medium enterprise credit, on the other hand, is defined using annual sales as an additional criterion to total indebtedness and does not have special treatment for micro and small credits. In any case, the information provided by the credit bureau improves the ability of financial institutions to focus on their target market and to better analyze their risks. It also helps funding providers in the selection and monitoring of the MSME sector they want to promote.

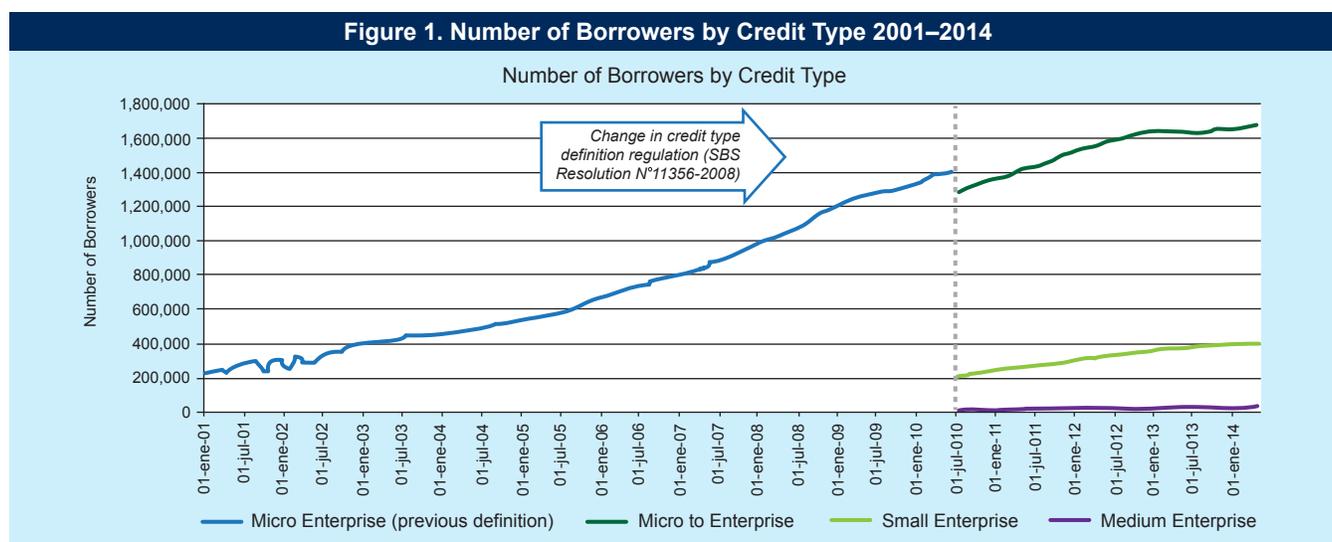
In general, a strong credit report system contributes to reducing the information asymmetries that exist between lenders and borrowers. Lending methodologies for micro and small enterprises especially require loan officers to do mostly field work, establishing close relationships with clients to gather information about their businesses. Once they are incorporated into the financial sector, credit records

allow financial institutions to focus on clients with positive information, making the lending process more efficient. This also has had a strong impact on borrowers themselves, who have become more aware of the benefits of maintaining good credit records, and of serious financing limitations they could face when they do not.

In spite of the many ways in which information from the credit bureau has influenced the development of MSME finance, the specific impact of these cannot be quantified. This is because it was accompanied by many other regulations and actions over time meant to develop a more favorable environment, especially for micro and small-scale finance, in view of the fact that more than 98 percent of firms in Peru are micro and small.

Nevertheless, there is no doubt that credit bureau information has played a key role in the important expansion observed in microfinance, both in terms of the volume of credit provided and the number of debtors participating in the financial sector. Furthermore, as explained above, since 2010 small and medium enterprise finance became more clearly visible, and also performed well. To better interpret Figures 1 and

Figure 1. Number of Borrowers by Credit Type 2001–2014



21. Current definitions for Micro, Small and Medium Enterprises were established by SBS Resolution N° 11356-2008, being:

- Micro Enterprise: Credit granted to physical or legal persons with a total indebtedness in the financial system, not considering house mortgages, no higher than S/.20,000 (approximately US\$7,000) over the last six months, used to finance production, commercial activities or services.
- Small Enterprise: Credit granted to physical or legal persons with a total indebtedness in the financial system, not considering house mortgages, no higher than S/.300,000 (approximately US\$105,000) over the last six months, used to finance production, commercial activities or services.
- Medium Enterprise: Credit granted to legal persons with a total indebtedness in the financial system over S/.300,000, that do not meet conditions to be considered Large or Corporate Credits (for example, sales over US\$7 million in past 2 years, having issued securities, having audited financial statements).

Figure 2, it is important to highlight that the ceiling of debtors’ total indebtedness in the financial system to qualify for a microcredit was substantially reduced in 2010, going from US\$30,000 to around US\$7,000. Hence a portion of what is shown as small enterprise credit was included before in the earlier definition of microcredit.

The impact of credit bureaus on transparency and competition is also well recognized, and this has certainly contributed to the substantial decrease in interest rates observed, especially for microenterprise credit, for which there is a longer period of information.

Finally, information obtained through the credit bureau contributes to a better supervision of credit risk by the SBS. Indeed, the SBS relies heavily on this information to be constantly aware of risk levels in the loan portfolios of each institution, and even in each sector and region, analyzing their evolution and demanding corrective measures, when needed, so that institutions maintain adequate risk profiles. This information is also very important in evaluating over-indebtedness, a critical issue nowadays in most mature microfinance markets. Evaluation of debtors’ credit behavior, number of lenders, and increase in debt are indicators that can help SBS, and the institutions themselves, identify possible problems of over-indebtedness in clients, in order to prevent them.

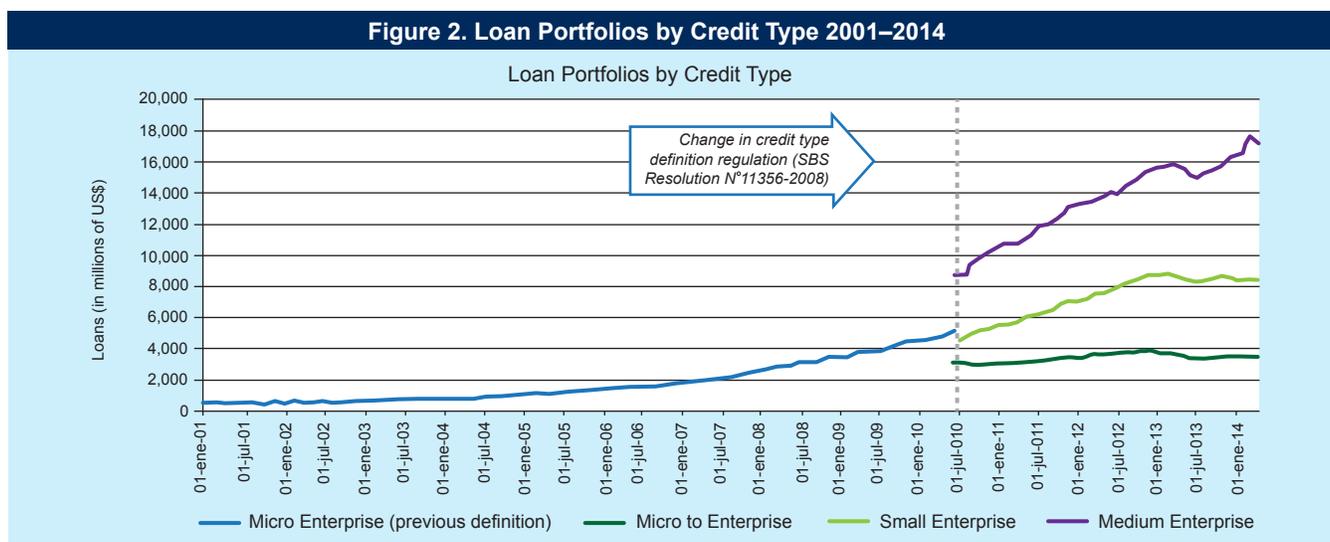
The intense competition observed in the microfinance sector is presenting some new challenges. At the time when the new

credit bureau went into operation, the microfinance sector was already expanding, with new institutions entering the market and with room to grow, and even some restrictions to compete by region.²²

Today, the Peruvian microfinance system has matured. Institutions have no restrictions against competing in the same areas, in urban areas especially, and have experienced increasing competition in recent years. To face these new scenarios, institutions are looking for ways to be more efficient so that they can stay competitive.

In this context, information from the credit bureau is being used not only as an instrument for risk management, but also increasingly as a tool to target good clients. This benefits clients who show good credit records, since they will likely be offered more financing and better conditions by competitors in the market. Institutions may also benefit, since they reduce their evaluation costs for potential clients.

Nonetheless, some worries have risen in relation to those institutions that introduce unbanked clients to the system. Evaluation of an unbanked client is more costly, since this has to be deeper given a lack of previous credit records. However, institutions may not find enough incentives to make this extra investment if clients are not likely to remain with them long enough. Another outstanding issue is that, despite the development of the microfinance sector, there are still many areas, mainly rural, that lack access to financial services.



22. Until 2002, Municipal Non-Banking Institutions (CMAC) could only operate in their own regions, or any other region where there was no other CMAC operating.

Therefore, the SBS is continuously evaluating actions that can promote the expansion of the financial system, especially to reach those who have limited or no access to financial services. In this area, new methodologies are being explored, such as psychometric models, that may contribute to bringing access to those clients that are new to the system and have no credit records to show, by making client evaluation more cost efficient for institutions.

Credit Bureau by Operation
(*Central de Riesgos por Operaciones – CRO*)

The public credit bureau today shows balances per debtor, not per operation. In spite of the amount of detail in that information, it has some limitations, mainly associated with the fact that movements in individual operations cannot be identified (such as the interest rate on the loan, terms, and payments).

In accordance with the needs of modern supervision, the Credit Report by Operations (Reporte Crediticio de Operaciones - RCO), provides more detailed information. This report is being required only from institutions with at least 25 percent of their portfolios allocated to nonretail loans and for credit operations classified as “nonretail.”

It is expected that in the longer term, all operations will be included in the RCO, although this means that the SBS and other institutions must continue enhancing their capacity to

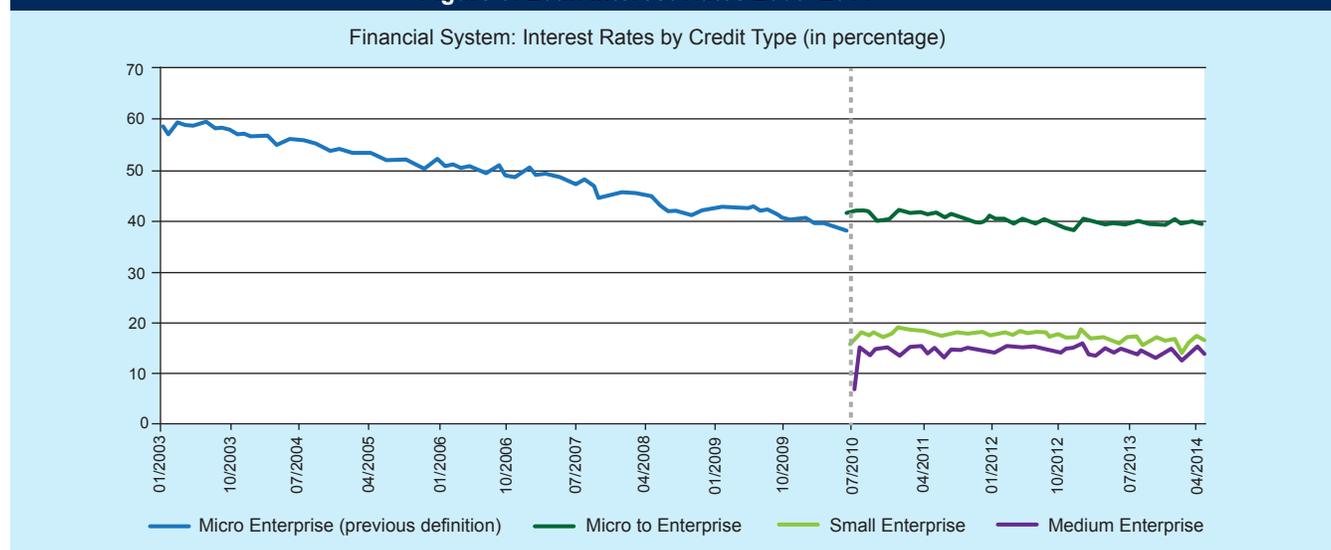
receive or produce all that information. Nonetheless, having such detailed information from every operation would strengthen supervision, especially of MFIs, whose loans show more dynamic behavior than any other type of credit.

Regulated institutions have 15 days to send their RCD to the SBS. Once received, the SBS runs several validations and revisions to ensure the quality of the information received, asking for corrections if they are needed. Later, information is consolidated so it can be made available to the system through the Consolidated Debtors Report. This process results in a delay in information of about a month, and can be more days for private bureaus that run their own processes to consolidate other sources of information.

The dynamic behavior of the microfinance sector means such delays have a greater opportunity cost every day, given the speed at which clients can take on new debt, show arrears, or otherwise change their risk condition since the last report of information. However, it is difficult to reduce this time without reducing the quality of the information.

Some non-regulated institutions are currently sharing information with some private bureaus, but the availability of this information is not standardized or centralized, like that provided by regulated institutions. An evaluation of the costs and benefits of sharing information for those institutions is needed. When sharing information, institutions also obtain additional information that allows them to improve their

Figure 3. Loan Interest Rates 2003–2014



credit risk management and, at the same time, decrease the risk of over-indebtedness for those clients who are evaluated based only on public records. However, competition in the sector may discourage information sharing in institutions that are not legally required to do so (such as credit unions or NGOs), since most of their clients are still exclusive and would probably stop being so once other institutions target them.

Another interesting aspect is a proposed law for the incorporation of credit unions under the direct supervision of the SBS. Among other issues, this would mean that those institutions would be under obligation to report information

on their debtors, which would then include in public records an important amount of information that is not currently public. Credit unions would face some challenges in the adequacy of their information systems to comply with the requirements of supervised institutions.

Submitted by:

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Republic of Korea: Improving Women's Access to Finance Through Family-Friendly Companies

Started in 2008



Implementing parties: Ministry of Gender Equality and Family.

Background and Rationale

This is a certification program with an evaluation system to certify companies that run family-friendly management systems. Such management systems include flexible work hours, support programs for childbirth, childcare and education, support for dependent family members, and support for employees.

In response to changes in social trends including lower birth rates, an aging society, and an increase in the female workforce in economic activities, certification of family-friendly companies aims to build a more family-friendly society that enables workforce balance between work and life.

The program was introduced in 2008, and the Act on the Promotion of Creation of Family-friendly Social Environment has been amended to make a basis for implementation. For 2014, the Korean government budgeted US\$1.1 million to “Projects for Building Family-friendly Social Environment,” for promotion and screening, an increase of 73.3 percent from US\$0.6 million in 2013. This budget will be used for the payment of certification fees, consulting fees for certification of SMEs, organizing forums and promotion.

The Ministry of Gender Equality and Family is in charge of certification. Organizations as diverse as companies, public agencies, and local governments are eligible to apply. As of 2013, 522 companies and agencies have been certified, with 183 of them being SMEs and making up 35.1 percent.

Description of the Intervention

Applicants scoring above 60 out of 100 are certified as family-friendly companies. Evaluation criteria include:

- meeting key requirements for operation;
- progress in implementing a family-friendly system; and
- satisfactory level of family-friendly management.

A detailed description of the evaluation criteria and the scoring method is provided in Box 1.

Each applicant receives certification through document screening and auditing by the relevant authority (Korea Management Association Registrations & Assessments Inc.) and review for Certification by the Family-Friendly Companies Committee (Ministry of Gender Equality and Family).

As many as 26 entities, including central government agencies, local governments, and private businesses are offering 77 incentives for certified companies. Financial incentives are provided as described below.

- Ministry of Employment and Labor: priority in receiving subsidized loans for industrial accident prevention facility (maximum of US\$0.3 million for each, with a special rate of 3 percent) and subsidy provided for procurement of equipment (maximum of US\$0.02 million for each).
- Small & Medium Business Administration: special offer of policy-related loans to SMEs (US\$4.1 million for

Box 1. Evaluation Criteria for Certifying Family-Friendly Companies

I. Major Requirement (30 points)

Leadership (12): attention and commitment of top management

Management system (8): teams and human resources allocated to projects to promote family-friendliness (2); budget allocated to projects to promote family-friendliness (2); regulations related to family-friendliness (4).

Family-friendly culture (10 points): education program to promote family-friendliness (6); accessibility to family friendliness system (4).

II. Progress in Implementing Family-Friendly System (60 points)

Basic elements (30): health management and support according to life cycle of employees (10), support for childbirth of employees and their spouses (10), childcare support and support for educational costs for children of employees (10).

Specialized elements¹⁷(30): flexible work hours (10), flexibility in working environment (10), health management support for family members (10), support for leisure time activities (10), support for weddings and funerals (10), social contribution to promote family-friendliness (10).

III. Satisfaction Level of Family-Friendly Management(10): overall satisfaction level of employees (10)

* An applicant chooses three out of the six specialized elements for evaluation.

SMEs based in the Seoul metropolitan area, and US\$4.5 million for SMEs based in non-Seoul metropolitan areas and within 150 percent of sales revenue).

- Financial Services Commission: 0.1 percent discount for the guarantee fee for the technical evaluation by the Korea Technology Finance Corp.
- Korea Credit Guarantee Fund: expansion guarantee limit for SME up to US\$2.7 million in the process of guarantee examination.¹⁷
- Woori Bank, KB (commercial banks): lower interest rate by 1-1.5 percent.

Results and Lessons Learned

Certification for family-friendly companies is expected to promote family-friendly management and thus create a family-friendly corporate culture. In addition, it should improve the quality of life for employees and their families.

According to a comparative analysis by the Korean Women's Development Institute of companies with certification as family-friendly companies (159) and companies that are uncertified, it has been shown that certified companies have achieved improvements in profitability, stability, and growth. In particular, the indices of certified companies, including the ratio of operating profit to net sales, the ratio of net income to net sales, and the return on equity have shown remarkable improvements, while debt ratios and capital adequacy ratios are improving as well. Specifically, certified companies show increases in productivity rates higher than those of non-certified companies by 0.22- 1.95 percent.

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17. Korea Credit Guarantee Fund aims to provide assistance for small and medium-sized businesses with limited guarantee capacity in sourcing funds by guaranteeing their liabilities. Businesses certified for family-friendliness are offered guarantees with an expanded limit.

Republic of Korea: Win-Win Loan Package

Started in 2010



Implementing parties: Hana Bank, Ministry of Gender Equality and Family.

Background and Rationale

The Win-Win Package Loan was first introduced in 2010 to support small and medium-sized subcontractors in light of the demand for shared growth between large-sized corporations and SMEs that are under a business partnership.

Loans are offered under its program for small-sized subcontractors, as well as contractors, based on the credit of the large-sized corporations. It has been designed to ensure liquidity for SMEs that are partnering with large-sized corporation to supply products to them. By making full use of supply chains based on win-win partnerships, SMEs have access to finance with relatively cheaper borrowing cost than when they source finance directly with their own credit.

Large-sized corporations take charge of fundraising and commission financial institutions to offer loans for partnering companies at low interest rates.

Description of the Intervention

Win-Win Package Loans are offered as follows:

- Win-Win Accounts Receivables Secured Loan, a financial service based on the credit of large-sized corporations for contracting SMEs.
- Win-Win Vendor Loans offered by supporting subcontractors throughout the settlement process by using accounts receivable bonds that contractors normally receive.

Note that large-sized corporations refer to a purchasing company, a contractor to a selling company, and sub-contractor to a vendor.

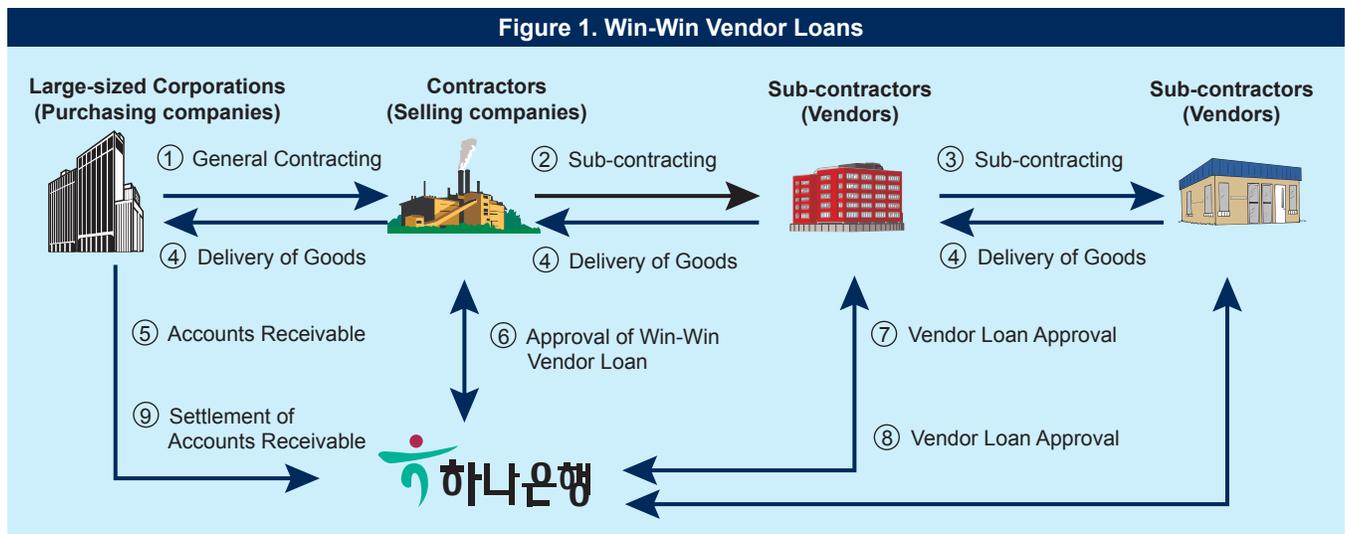
- Win-Win Accounts Receivables Secured Loan: with accounts receivable of a purchasing company (large-sized corporation) as security, a contracting partner finances itself by executing the loan.
- Win-Win Vendor Loan: a contractor takes an accounts receivable bond from a purchasing company as security to support subcontractors in receiving payment for delivered goods.

The Win-Win Vendor Purchasing Loan enables sub-contractors to receive financial assistance under identical conditions as accounts receivables that contractors have acquired from purchasing companies, once large-sized corporations, contractors, and sub-contractors agree to form a package (these companies sign an agreement in advance).

Results and Lessons Learned

As of 2013, the amount of loans reached US\$0.32 billion, with 355 large-sized corporations signing agreements with their partnering SMEs (note: large-sized corporations and partnering SMEs need to create a package before applying for a Win-Win Package Loan).

The following are the expected results for purchasing companies (large-sized corporations), selling companies (contractors) and vendors (sub-contractors).



- **Purchasing companies:** can improve their corporate image through credit offered to sub-contractors, as well as contractors.
- **Selling companies:** based on the offering of credit and the credit rating of purchasing companies, payment of delivered goods can be made earlier at relatively lower cost or payment of delivered goods from vendors can be made with a receivable as a security. The companies can thus see improvement in the flow of funds.

- **Vendors:** with Win-Win Vendor Loans based on credit offered by purchasing companies, payment for delivered goods can be made to enable the withdrawal of payment before the due date. Furthermore, vendors will see improvement in the reliability of purchasing companies and contractors. In particular, sub-contractors benefit from SME financing through relatively low interest rates based on the credit rating of the purchasing companies, as well as early payments for delivered goods.

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Republic of Korea: Intellectual Property for Secured Loans

Started in 2011



Implementing parties: Korea Development Bank.

Background and Rationale

IP Secured Loan and IP Fund are part of financial assistance policy based on intellectual property possessed by SMEs to foster ventures and start-ups. In this case, intellectual property rights refer to property rights recognized by relevant legislation, which includes patent rights, trademark rights, design rights, and copyright.

As part of “creative finance” derived from “creative economy” pursued by president Park Geun-hye, these programs are significant in providing SMEs with opportunities for financing by developing new financial markets with intellectual property rights as a medium for diversifying the market that has conventionally been centered on traditional loan guarantees.

Description of the Intervention

The Korea Development Bank (KDB) offers financial instruments related to IP according to the stages of growth that businesses go through:

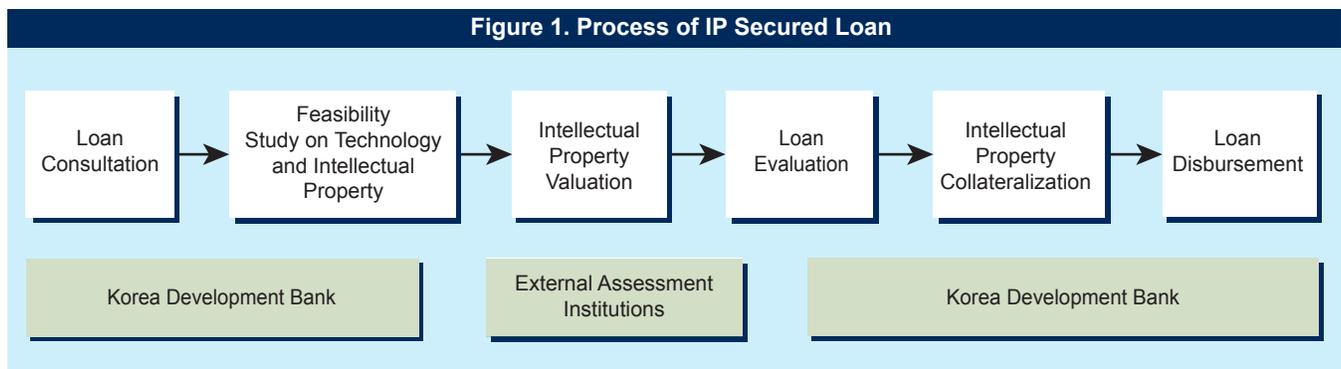
- For start-up companies, loans are offered for purchasing IP.
- For venture companies and MSMEs, IP loan guarantees are offered for diversifying sources of financing by recognizing intangible assets, IP, as security.
- For SMEs in their mature stage, IP funding is offered for providing a comprehensive financing program (i. e., assistance for investment activities and loan programs, which include loans, investments, and securitization of IP).

IP Secured Loan was first introduced in September 2013. It provides funding for SMEs to boost IP finance by offering guaranteed loans via an evaluation of the IP and forming an organization to facilitate the collection of IP Secured Loans.

The IP Secured Loan program is categorized into loans and collections.

- Loans: IP is valued by external assessment institutions and, based on the results, it is recognized as a security.

Figure 1. Process of IP Secured Loan



The valuation process is based on a valuation model developed with support from the Korean Intellectual Property Office.

- Collections: For nonperforming loans, either a company or a fund intervenes to purchase the secured IP, thus providing relevant assistance in collecting loans.

To crystallize such ideas and efforts, a fund has been raised in collaboration with the KDB under an agreement made with the Korea Patent Office (KPO) for cooperation to boost IP finance. KPO contributed more than 50 percent of the fund, and KDB more than 20 percent, to raise approximately US\$18 million. The fund seeks to invest in well-performing businesses possessing IP, as well as purchasing and selling secured IP of businesses that are incapable of paying off their debts. Further, Intellectual Discovery Inc., the largest company with expertise in IP, established in 2010, will purchase secured IP to set up a basis for proactively responding to patent-related lawsuits filed by foreign companies and thereby boosting IP businesses.

The IP Fund raised US\$90 million in 2013 with a maturity of seven years. The fund aims to support SMEs with IP as a guarantee medium by recognizing IP as an asset that independently generates profit.

IP Fund can act in various forms such as Sales & License Back, IP securitization and IP Pool. In Korea, the fund is currently managed as a form of Sales & License Back,

whereby a business sells its IP to investors (funds) to secure finance and then pays a license fee to the investors.

Results and Lessons Learned

As of 2013, 15 companies benefitted from loans with a total amount outstanding of US\$15.4 million.

As of April 2014, 10 companies have benefitted from IP Fund investments amounting to US\$46 million. A Korean retail company, Codes Combine, stands out as the first case in Korea where the IP fund invested in the trademark rights of businesses. The company so far has attracted investments of up to US\$0.9 million with its 88 trademark rights.

IP Fund and IP Secured Loan programs have the momentum to transform IP holders into successful businesses by offering financial assistance to companies with outstanding IP, yet lacking tangible assets for guarantees. The funds are anticipated to promote growth and enhance SME value by diversifying sources of financing through IP. However, the IP Secured Loan program for patent rights faces challenges in valuing intellectual property rights. A high priority is the development of a valuation model and promotion of a market for the collection of IP secured loans.

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The Philippines: Policies to Implement Microfinance Plus

Started in 2011

Implementing parties: Bangko Sentral ng Pilipinas (BSP).

Background and Rationale

Considered the country's economic backbone, MSMEs comprise 99.6 percent of total business enterprises (944,897 as of 2012). As of 2012, these sectors collectively employed 61.2 percent of the workforce, and accounted for 35.7 percent of value added (Department of Trade and Industry). MSMEs can be central for the country's overall economic growth, job creation and productivity, and they are a central part of the Philippines government's inclusive growth strategy.

MSMEs, however, face many barriers to firm expansion including shortages of working capital to finance their business activities and difficulties in obtaining credit from formal financial institutions. Apart from credit, MSMEs require other financial products, which they likewise have difficulty accessing, such as savings accounts, insurance, remittance, and payment facilities. Moreover, MSMEs generally lack access to economic safety nets and are thus more prone to shocks.

In recognition of this vulnerability, especially the large base of microenterprises, there is a need to lift these institutions into larger and generally more resilient entities, and to push for greater access to financial services for them. This gap in the financing pool serves as an opportunity for financial institutions to support enterprises that are considered large for microcredit but small for traditional bank borrowing. Moreover, it is in the government's interest to cultivate a financial and investment climate that can support existing microenterprises to grow and engage in activities that are on a larger scale.

Description of the Intervention

The Bangko Sentral ng Pilipinas (BSP), the Philippines' central monetary authority, is mandated to support a climate conducive to inclusive finance. It has put forward several policy issuances and undertaken initiatives on microfinance and most recently on financial inclusion in general. Building on the success in microfinance, the BSP in December 2011 issued a circular that adjusts microfinance regulations to serve the needs of microenterprises growing into SMEs.

However, more than two years after the regulation's implementation, these larger loans comprise only a small percentage compared to the traditional microfinance loan portfolio of the banking system, and few formal financial institutions have actually provided these newly permitted loans. The BSP is thus still faced with the fundamental question of how to address the credit requirements of microenterprises that will foster their growth and ultimately allow them to graduate to small or medium entities.

I. Microfinance Landscape of the Philippines

The Philippine General Banking Law of 2000 in its Sections 40, 43, and 44 effectively recognizes the importance of the banking sector as a vehicle to provide access to microfinancial services to the public. Mention of microfinance in the law indicates the importance of the poor's access to appropriate financial services and suggests that microfinance can be an effective tool for poverty alleviation and should be viably integrated into the business of financial institutions.

To implement the provision of the law, the BSP issued Circular 272 on Jan. 30, 2001, which put forward the

definition of microfinance and highlighted microfinance loans as small loans granted to basic sectors that shall not exceed PhP150,000.

With the effectivity of Circular 272 and its implementing regulations, 119 banks engaged in microfinance, lending some PhP2.6B to 390,635 borrowers in 2002. By end of 2013, a significant growth in microfinance was evident with 182 banks reaching over a million clients and providing them with PhP8.7B in loans. The various policies and issuances¹ crafted by the BSP had mobilized the Philippine banking system to deepen its reach to the low-income sectors of the society.

The importance of delivering a variety of financial services to underserved areas through microfinance is now at the forefront of BSP work in financial inclusion, broadening the scope of microfinance to include deposits, insurance and remittances, among others, that are appropriately designed and priced to cater to the needs and capacity of this market.

In particular, the BSP issued Circular 694 Oct. 14, 2010, that expanded the range of microfinance products as well as increased the threshold amount for loans from up to PhP150,000, as originally defined in Circular 272, to certain microfinance loans that can be up to PhP300,000. In recognition that there are still many unbanked areas in the country, the BSP also liberalized the establishment of microbanking offices (MBOs). Less costly to put up than a regular bank branch, and authorized to provide financial services such as deposits, loans, payments, and microinsurance, among others, MBOs are a way of allowing banks to set up office in areas that remain underserved.

The loan product Microfinance Plus, covering loans of PhP150,001 to PhP300,000 was introduced by BSP Circular 744, crafted in recognition of the needs of growing microenterprises that might become SMEs. In the same vein, the average daily balance for microdeposits, initially set at PhP15,000, was adjusted to PhP40,000.

The government has also focused on policies and initiatives that can foster the growth and development of SMEs, as well as micros. In 2008, the Magna Carta for MSMEs (Republic Act 9501, 2008) was amended to further support the sector. In this law, microenterprises were redefined as entities with “total assets, inclusive of those arising from loans but exclusive of the land on which the particular business entity’s office, plant and equipment are situated, must have value...of not more than PhP 3 Million.”

Data on microfinance activities reported by banks tells of a positive turnout and progress. The advance in these activities suggests that microfinance is a tool that addresses the financial requirements of clients, while providing viable business for banks. Improvements in policies to expand the range of microfinance services and products are thus well anchored and can be expected to continue.

II. Introduction of Microfinance Plus

The microfinance credit technology has been successful due to its incremental nature (i.e., loan amounts increase after each cycle of good repayment) of the loan where the credit discipline of the borrower is built over time. Equally important, the microfinance regulatory framework provided space for banks willing to incorporate microfinance in their business models to viably serve the microenterprise sector. While there seemed to be adequate facilities, at one level, for microenterprises with relatively small credit needs and, at the other, for well-established enterprises that could access traditional windows of banks, businesses that were in transition—requiring larger loans but not yet fully compliant with traditional bank requirements—were left without adequate financial services. Some literature calls this the “missing middle,” essentially characterized by its position between large numbers of microenterprises, on one hand, a few large firms, on the other, and small and medium enterprises mostly lacking access to credit and other financial services.

The BSP, through its group dedicated to financial inclusion, that is, the Inclusive Financial Advocacy Staff (IFAS), reviewed the threshold amount of loans to microenterprises as a response to their growing businesses. Data from 2005-2010 showed that, while the average loan size was still around PhP7,400, there were a growing number of clients requiring significantly larger loans. In addition to analyzing time series data, banks with microfinance operations with a relatively large pool of clients in this segment were interviewed to understand the credit assessment of these clients. It was evident that a good repayment record of the client was the main basis for increasing the loan size, in addition to a cash flow analysis of the growing business. A report to the Monetary Board, the highest decision-making body of the BSP, showed that there was a growing demand for loans in the PhP100,000 to PhP150,000 range (with PhP150,000 the maximum then allowed for microfinance loans). The report also suggests that microenterprises may have greater financial requirements than what microfinance-engaged banks are allowed to lend to them, but smaller than what other banks are willing to provide.

In response to this, under BSP Circular 744 dated Dec. 28, 2011, Microenterprise Loans Plus or Microfinance Plus was added to the types of loans available. Microfinance Plus is essentially the same as microfinance loans as defined in Circular 272, but with additional features to respond to the increased risk brought by the higher loan ceiling. Circular 744 defines Microfinance Plus as “loans granted to the basic sectors, on the basis of the borrower’s cash flow, for their growing microenterprises and small businesses. These loans are from PhP150,001 to PhP300,000. The borrowers that will qualify as recipients of Microfinance Plus shall have a track record of at least two microfinance loan cycles in the PhP50,000 to PhP150,000 range demonstrating the success of the business, its increasing credit demand, and subsequent increased capacity to pay. The borrower must also have a savings account. The delivery of Microfinance Plus will be utilizing microfinance principles and methodologies in accordance with existing BSP regulations.”

Microfinance Plus thus pushes up the threshold of loans that may be lent to microenterprises. It is hoped to boost microfinance lending by allowing the disbursement of larger sums to the micro sector with the hope of bridging the financing needs for microenterprises that are at the threshold of growth to become SMEs.

Results and Lessons Learned

Directly after the issuance of Circular 744, PhP48M was disbursed to 4,024 microenterprises in the form of Microfinance Plus loans. In the subsequent quarters, the amounts fluctuated below the PhP90M mark to some 3,000-4,000 borrowers. At end 2013, growth numbers shifted dramatically shift upward, with PhP111M in total loans to more than 6,000 borrowers.

However, while the loan portfolio shows some growth, movement in Microfinance Plus remains modest. Since its beginning until 2013, Microfinance Plus has only made up some 1 percent of the total microfinance loan portfolio of the banking system, and no more than 20 banks (no more than 10 percent of those engaging in microfinance) have offered this type of loan. This points to low take up, and ultimately raises questions about how to help microenterprises grow.

Low take up of Microfinance Plus may be due to the following reasons:

- For growing microenterprises, growth may not rest only on access to larger amounts of credit. At a certain level, microenterprises may need business development services to manage growth. Offering a product that only increases the amount of credit available without an attendant framework for business development may be insufficient. This suggests that such government programs must be rolled out on a larger scale to reach more such borrowers.
- Microenterprises may be satisfied with the level of their business. Staying as small or informal as possible may actually provide incentives for microenterprises as this can avoid a business environment that proves to be too costly for them to grow (e.g., a progressive income tax scheme). Regulations also tend to be more onerous (e.g., registration, compliance with labor laws, etc.) and be seen as another deterrent to business growth. The process of formalization must therefore be considered in the costs of transition for these microenterprises to SMEs and may thus require some incentive mechanisms.

Lastly, although larger microfinance loans are now made available through the microfinance regulatory framework, microenterprises do not graduate into SMEs because their access to larger loans remains poor. In other words, funds are there for larger loans, but there remains a problem on how to obtain these larger loans. Perhaps not all of the microenterprises that are potentially offered the Microfinance Plus product may be effectively able to access these due to a lack of credit rating information or asymmetric information on the capacity of the firm to repay its loans. Financial institutions, although mandated by the law to set aside 8 percent of their loan portfolios for micro and small enterprises, may remain apprehensive about extending credit to these firms due to their perceived high-risk profile. Ongoing work in the Philippines on the establishment of a comprehensive credit information system and a collateral registry may eventually enable banks to ascertain the creditworthiness of potential SMEs.

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The Russian Federation: Laws and Regulations for Electronic Means of Payment

Started in 2011



Implementing parties: Russian Central Bank, State Duma, and other state bodies.

Background and Rationale

Prior to 2011, in the Russian Federation there was no legal basis for using electronic wallets by companies. Instead, those firms that wanted to receive payments via electronic payment systems had to sign agreements with e-payment operators to channel customer money into their bank accounts.

Introduction of corporate e-wallets could simplify accepting payments from customers for various goods and services.

Description of the Intervention

Federal Law “On National Payment System” was adopted in 2011 and instituted three types of electronic means of payment (EMP): non-personified/personified (for natural persons) and corporate (for companies and entrepreneurs). These three types of electronic means of payment come under different regulatory regimes. For the corporate EMP it is as follows:

- EMP holders should be fully identified as prescribed by Anti-Money Laundering and Combatting the Financing of Terror law.
- Total funds of a corporate EMP should not exceed 100,000 RUB at the end of the operator’s workday (excesses are transferred automatically to the owner’s bank account).
- Transfer of electronic money to the nonpersonified EMPs belonging to natural persons exempted from Customer Due Diligence is prohibited.

Just as for a bank account, corporate EMPs are subject to reporting to the Federal Tax Service, and to the freezing of funds in cases prescribed by federal legislation.

The implementation of the new regulations was supported by the Central Bank of Russia, State Duma, and the private sector.

Results and Lessons Learned

It is still too early to measure results. But the changes in e-money regulations have raised issues that continue to be discussed. Private sector representatives have voiced some concerns that the regulatory regime for the corporate EMPs is not consistent with the risks its usage can imply. For example, the same customer due diligence (CDD) and reporting requirements apply as for a bank account but it also entails certain limits that do not exist for bank accounts. Therefore, corporate EMPs are rather an addition to a bank account rather than a “lighter” substitute.

Another concern of the private sector is a ban on the transfer of electronic money to nonpersonified e-wallets, which is an obstacle for making refunds or implementing cashback programs. This issue is partly addressed in the legal draft adopted in December 2013 and scheduled to enter into force in July 2014.

Implementation of the corporate e-wallets seems to be a case of non-proportionate regulation. Private sector feedback indicates that the value of this service for their business is very little. Legislation does not differentiate between small entrepreneurs and large corporations for the purposes of

opening corporate EMPs. Because of rather low demand for that service, some e-money operators do not even provide it. Beginning around 2011 and afterwards, e-money operators started implementing projects that allow simple and fast connections to the e-money payment system for the businesses. At the same time, natural persons got the opportunity to pay through the e-money payment system even without having e-wallet. That became possible by introducing payment processing capabilities that include not only e-money transactions but also payment cards, mobile commerce, etc., through a single Web form.

However, businesses and entrepreneurs still need to have opened a bank account. Therefore, these projects expand the opportunities for payers rather than payees. Unfortunately, Russian legislation makes it de-facto impossible for any business without opening a “classic” bank account. Hence, any private initiative cannot overcome this obstacle.

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