



SME FINANCING: THE ROLE OF ALTERNATIVE INSTRUMENTS

CCAF Annual Conference
Cambridge, 29 June 2018

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Outline

- Recent trends in SME financing
- The role of finance instruments other than straight debt
- Challenges and policy responses for the wider uptake of alternative sources of finance for SMEs



Recent trends in SME financing

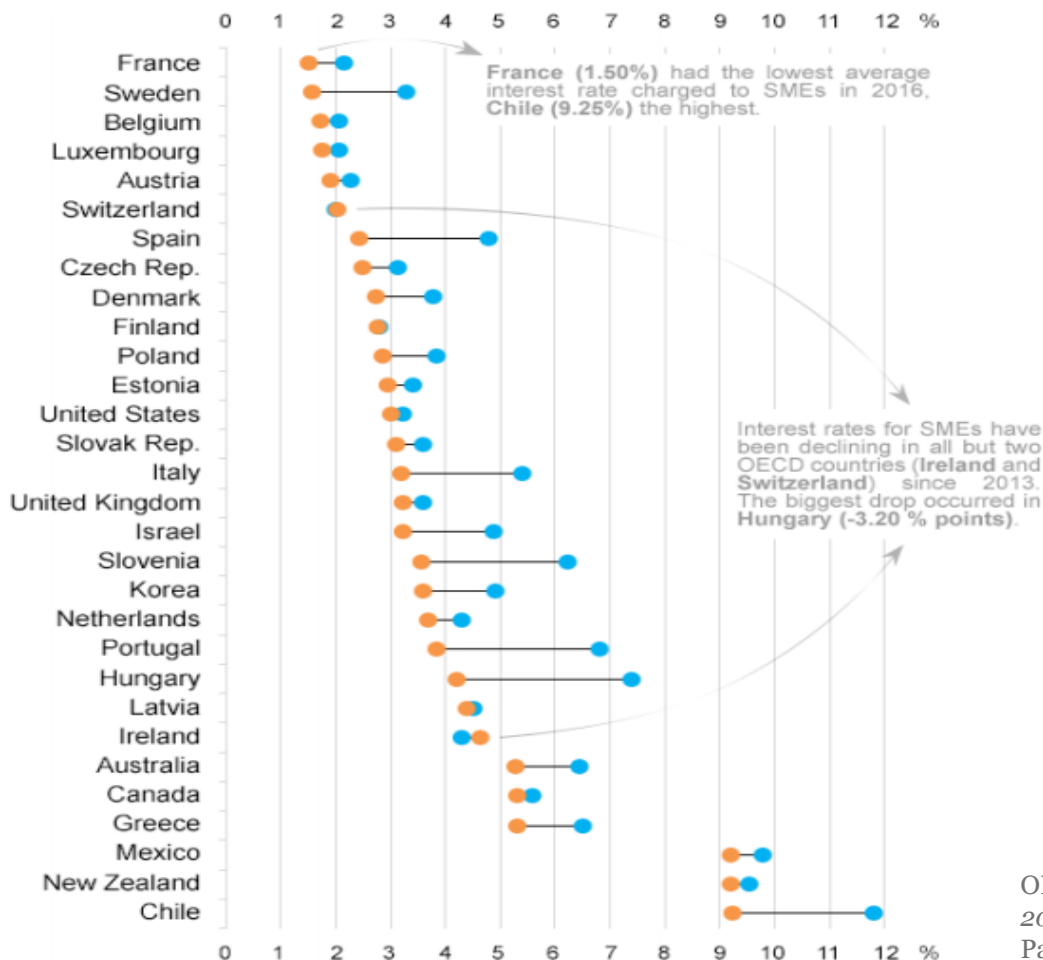


- Annual flagship publication that aims to improve the evidence base on SME finance
- Data on debt, credit costs and conditions, asset-based financing, VC investments, and the financial health of SMEs
- Information on policies and programmes
- 43 participating countries
- Official data from ministries, central banks, statistical offices, sector organisations
- Network of experts



Credit conditions have been improving

Interest rates charged to SMEs 2013 (blue) and 2016 (orange)



Other indicators also point to improvements in credit conditions:

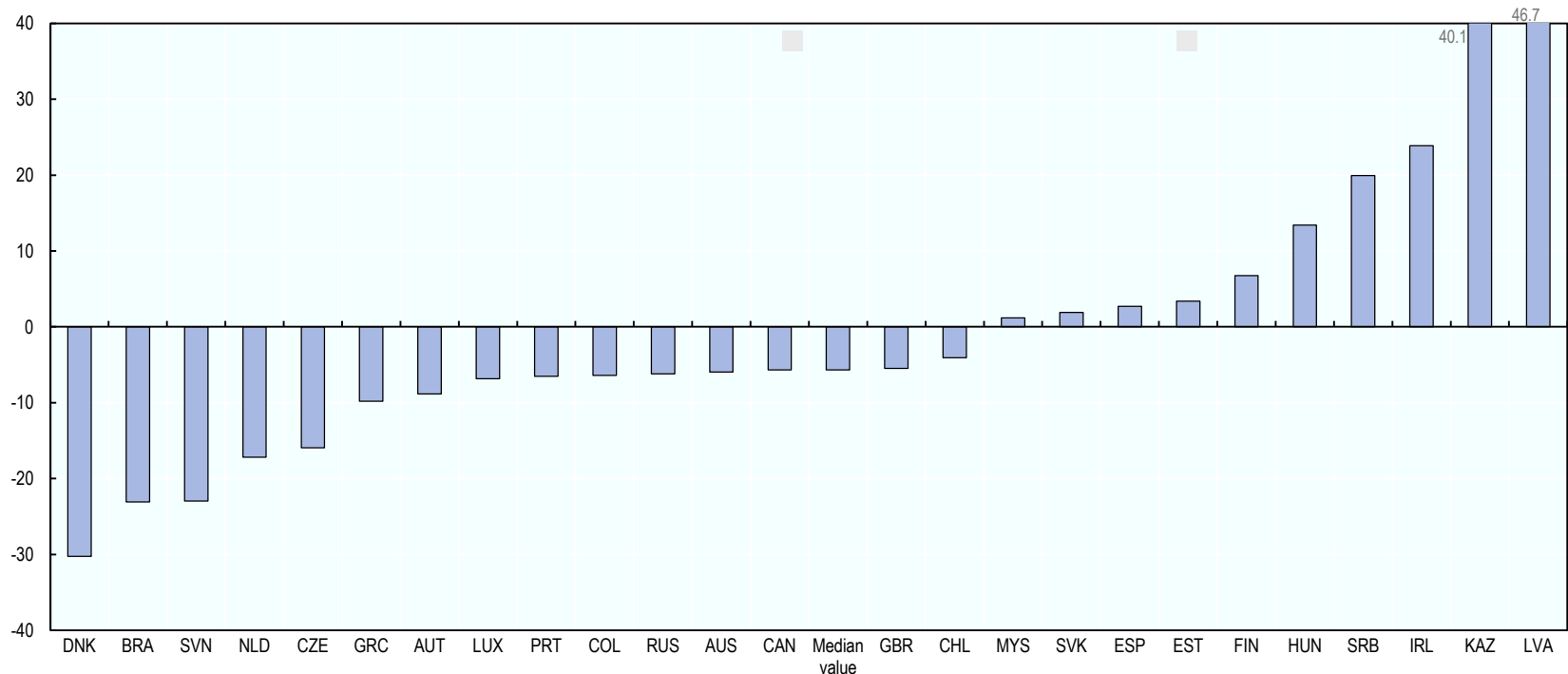
- *Loan rejection data*
- *Demand-side surveys (number of SMEs stating access to finance as a major problem)*
- *Supply-side surveys (with senior loan officials)*



Yet new loans to SMEs have declined in many countries

New loans to SMEs

year-on-year growth rate (%) between 2015 and 2016, adjusted for inflation



Source: OECD (2018), *Financing SMEs and Entrepreneurs 2018: An OECD Scoreboard*, OECD Publishing, Paris, http://dx.doi.org/10.1787/fin_sme_ent-2018-en.

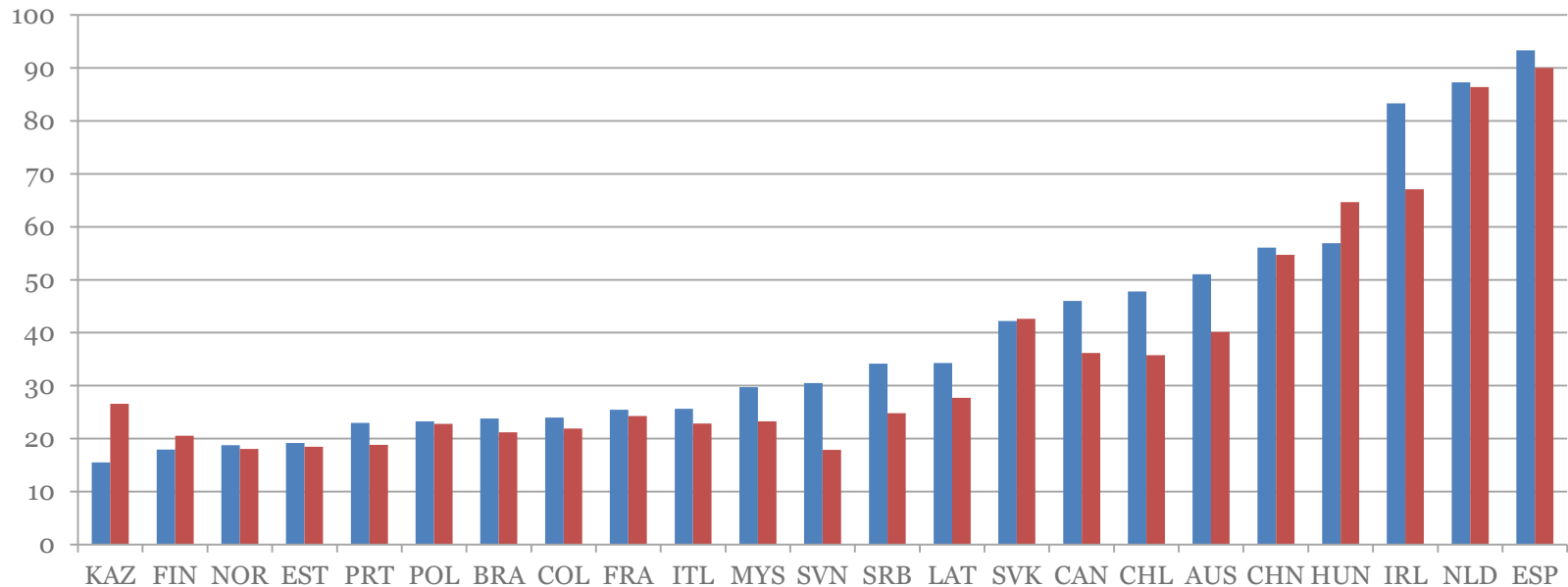


SMEs are reducing their dependence on short-term lending

The share of short-term SME loans as a proportion of all SME loans

As a percentage

■ 2013 ■ 2016



Source: OECD (2018), *Financing SMEs and Entrepreneurs 2018: An OECD Scoreboard*, OECD Publishing, Paris, http://dx.doi.org/10.1787/fin_sme_ent-2018-en.



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There is a broad range of alternative instruments with potential to finance SMEs

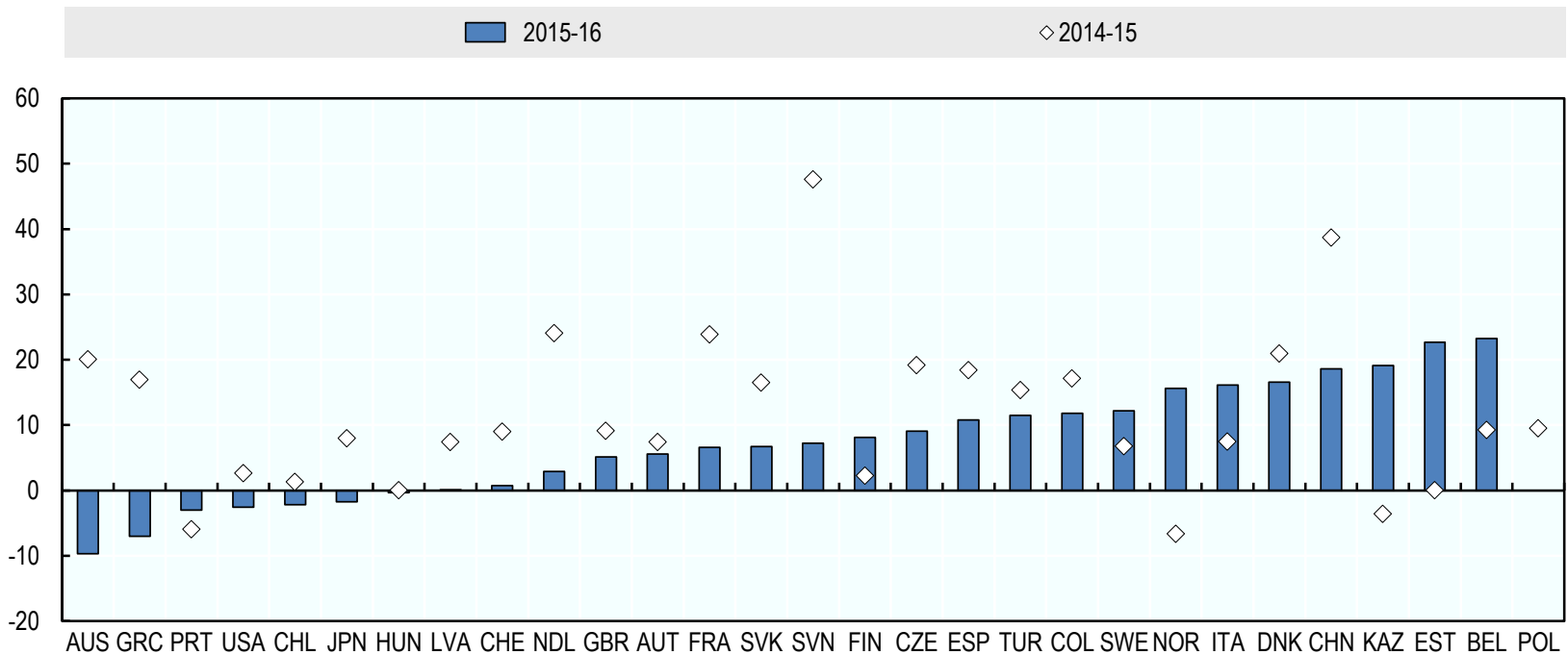
Low Risk/ Return	Low Risk/ Return	Medium Risk/ Return	High Risk/ Return
Asset-Based Finance	Alternative Debt	“Hybrid” Instruments	Equity Instruments
<ul style="list-style-type: none"> • Asset-based lending • Factoring • Purchase Order Finance • Warehouse Receipts • Leasing 	<ul style="list-style-type: none"> • Corporate Bonds • Securitised Debt • Covered Bonds • Private Placements • Crowdfunding (debt) 	<ul style="list-style-type: none"> • Subordinated Loans/Bonds • Silent Participations • Participating Loans • Profit Participation Rights • Convertible Bonds • Bonds with Warrants • Mezzanine Finance 	<ul style="list-style-type: none"> • Private Equity • Venture Capital • Business Angels • Specialised Platforms for Public Listing of SMEs • Crowdfunding (equity)

OECD (2015), *New Approaches to SME and Entrepreneurship Financing: Broadening the Range of Instruments*, OECD Publishing, Paris, <https://doi.org/10.1787/9789264240957-en>.



Sources of finance other than straight debt are becoming more widely used

New production in leasing and hire purchases *year-on-year growth rate (%) adjusted for inflation*



Source: OECD (2018), *Financing SMEs and Entrepreneurs 2018: An OECD Scoreboard*, OECD Publishing, Paris,
http://dx.doi.org/10.1787/fin_sme_ent-2018-en.

Factoring volumes, VC investments and online alternative finance instruments were also up in 2016



Private equity and debt markets are expanding, including in Europe

Private equity (USD billion)

	2010	2011	2012	2013	2014	2015	2016
North America	80	87	95	176	189	168	199
Europe	40	44	64	86	77	70	116
Asia	36	54	42	37	58	37	40
Rest of world	16	17	18	12	15	12	9
Total	172	202	219	311	339	287	364
Global un-invested capital ("dry powder")	622	601	565	666	695	752	869

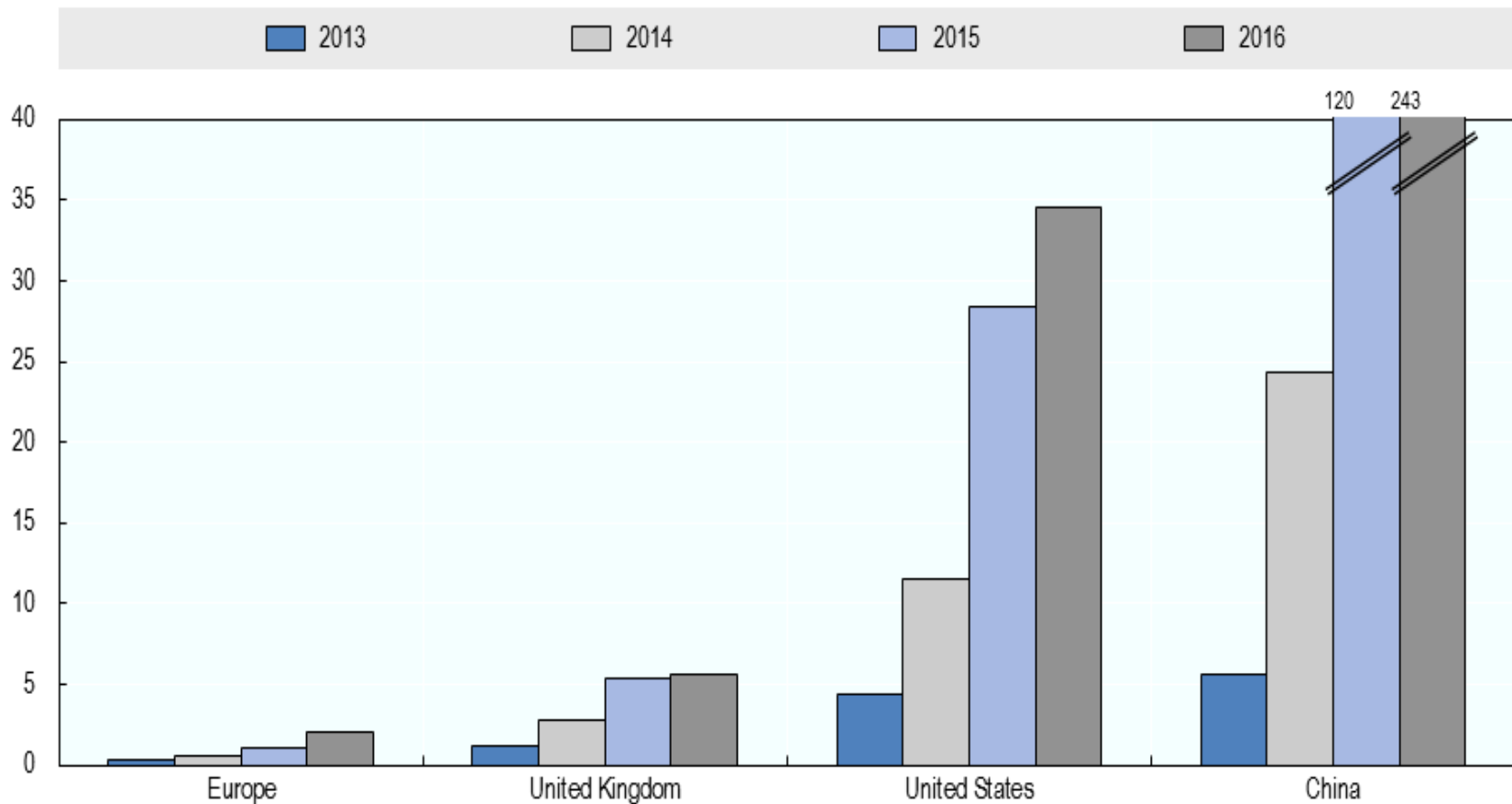
Private debt (USD billion)

	2011	2012	2013	2014	2015
North America	31	36	37	47	54
<i>Percent of World Total</i>	66	58	66	64	59
Europe	13	18	18	23	31
<i>Percent of World Total</i>	28	29	32	31	34
Asia	3	8	1	3	6
<i>Percent of World Total</i>	7	13	1	4	7
Total	47	62	56	73	90



Online alternative financing instruments are rising fast, often from a low basis

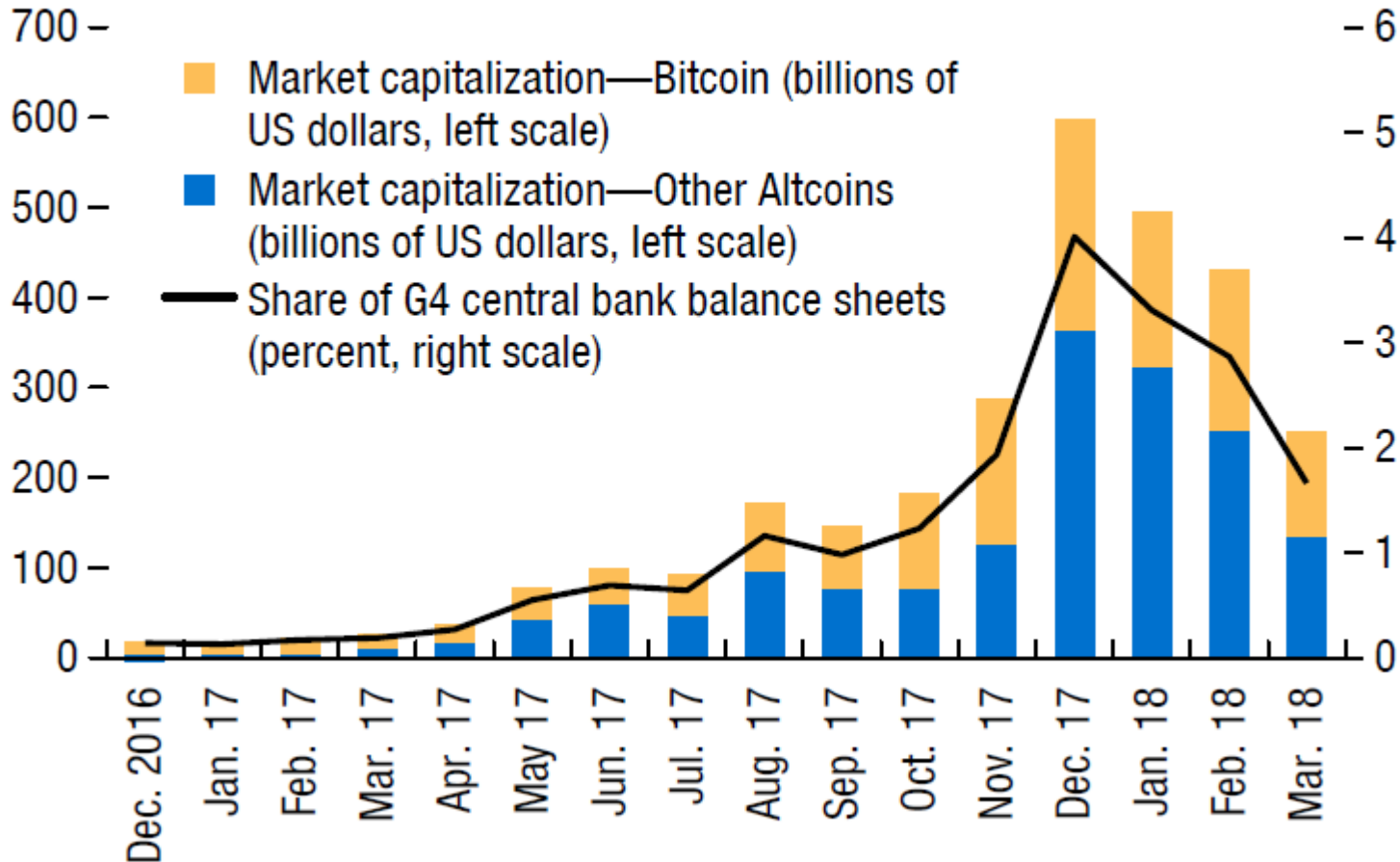
Total volume of alternative finance raised through digital platforms, selected countries and regions, in billion USD





Crypto-assets and ICOs are gaining prominence, but the future is uncertain

**Market Capitalization of Crypto Assets
(Billions of US dollars)**





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Challenges persist to the wider take-up of these instruments by SMEs

POLICY OBSTACLE	MAIN AREA OF CONSTRAINTS	POTENTIAL POLICY ACTION	STRUCTURAL MEASURES
Demand-side	Lack of awareness, negative perceptions and inability to access alternatives to bank finance	<ul style="list-style-type: none"> Consider a national strategy to foster financial literacy, ideally with a specific focus on SMEs Develop financial education programmes for entrepreneurs and would-be entrepreneurs, including through incubators Develop investor-readiness programmes 	<ul style="list-style-type: none"> Address the fragmentation of SME financial markets Improve the liquidity and scale of markets (thin markets problem) Help to develop an SME finance ecosystem Create links and matchmaking services between (potential) investors, entrepreneurs and large companies Monitor and evaluate public policies in this area
	Lack of financial skills and vision	<ul style="list-style-type: none"> Enhance SME financial skills and strategic vision by offering advisory services to improve accounting, financial management and overall business development Complement the provision of financial support to SMEs with non-financial elements such as counselling and monitoring 	
	Disadvantageous tax treatment of equity instruments	<ul style="list-style-type: none"> Encourage tax neutral regulation Support a range of financing instruments for SMEs, e.g. via tax deductibility for innovative start-ups that participate in entrepreneurship trainings or in incubator programmes 	
Supply-side	Opacity of the SME market	<ul style="list-style-type: none"> Improve transparency and provide targeted information, e.g. by credit registries or bureaus for SMEs and rating services going beyond collateral and historical financial information Identify SME financing needs and gaps and improve the evidence base 	
	Regulatory ambiguity or barriers to entry in the SME market	<ul style="list-style-type: none"> Design regulation that supports a range of financing instruments for SMEs, while ensuring financial stability and investor protection 	
	Limited exit options	<ul style="list-style-type: none"> Lower the costs of IPOs Introduce measures that reduce the length of time between investing and exiting Considering the needs of equity investors when designing regulation 	



G20/OECD High-Level Principles on SME Financing

1. Identify SME financing needs and gaps and improve the evidence base.
2. Strengthen SME access to traditional bank financing.
3. **Enable SMEs to access diverse non-traditional financing instruments and channels.**
4. Promote financial inclusion for SMEs and ease access to formal financial services, including for informal firms.
5. Design regulation that supports a range of financing instruments for SMEs, while ensuring financial stability and investor protection.
6. Improve transparency in SME finance markets.
7. Enhance SME financial skills and strategic vision.
8. Adopt principles of risk sharing for publicly supported SME finance instruments.
9. Encourage timely payments in commercial transactions and public procurement.
10. Design public programmes for SME finance which ensure additionality, cost effectiveness and user-friendliness.
11. Monitor and evaluate public programmes to enhance SME finance.



Policy approaches to enable SMEs to access non-traditional financing instruments

Common and other approaches

- Tax incentives to encourage investments in SMEs – large variations in the level of the tax incentive and in eligibility criteria
- Information programmes to increase SME awareness and understanding of various financing options, through seminars and/or brochures/websites
- Promotion of factoring of electronically recorded monetary claims and supply-chain finance electronic platforms
- Accelerators or incubators to improve SMEs' investor-readiness
- Adapted requirements for issuing debt or listing
- Provision of equity funding either directly through public financial institutions or indirectly through funds (private equity or venture capital funds, business angels)
- Framework in place mostly for *equity* crowdfunding, with limitations for both the issuer and the investor

Innovative approaches

- Services matching SMEs with finance providers and investors



Regulatory issues influence the development of online alternative finance instruments

How to balance consumer/investor protection and financial stability with financial innovation?

- Development of dedicated regulatory framework more suitable to (equity) crowdfunding activities, with adapted due diligence and information requirements, restrictions, prospectus and registration exemptions
- Regulatory sandboxes to regulate and supervise Fintech activities



The regulatory landscape on ICOs is fragmented





Areas for further research

- More harmonised data and evidence on trends in alternative instruments, also in combination with traditional instruments
- Classification and a clear terminology on crypto-assets
- The potential of these instruments to address SME finance gaps
- The drivers and determinants of take-up of different financial instruments by SMEs
- Options for regulatory and supervisory approaches
- Innovative policy options to stimulate these markets



THANK YOU!

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