SCOPING AND ASSESSMENT REPORT - MSME ACCESS TO FINANCE ECOSYSTEM IN AFRICA

SURVEY REPORT

CONTENTS

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Shopping in a local market. Nigeria. (Photo by i_am_zews/Shutterstock)

INTRODUCTION

Micro, small and medium-sized enterprises (MSMEs)[1] are generally accepted as the most important engines of innovation, growth, job creation and social cohesion in most emerging economies. In these economies, MSMEs contribute on average more than 50 percent of employment and 40 percent of GDP and contribute significantly to poverty reduction.[2] In addition, women account for a third of the formal registered MSMEs in Africa.[3] However, MSMEs can only reach their full potential if they operate in an environment where they have access to the finance necessary to start, sustain and grow their business.

MSMEs face multiple hurdles in the effort to establish and grow sustainable enterprises, with the lack of appropriate forms of finance often ranked as the most serious constraint. In developing countries, credit to the private sector is well below the average than in high-income countries, as a share of GDP and the lack of a well-developed financial infrastructure[4] pose challenges for both credit providers and the enterprises using the credit. The situation in Africa is particularly challenging, in that the MSME finance gap (% of formal MSMEs that cannot or can only partially access credit) for sub-Saharan Africa is the highest in the developing world (51 percent in 2017) according to the IFC's *Closing Africa's MSME Finance Gap*.[5] The informal sector (where access to credit is typically severely restricted) contributes an estimated 38 percent of sub-Saharan Africa GDP (from the same report), with the implication that the overall finance gap is probably higher. The situation in MENA is somewhat less challenging, but there are still significant hurdles for MSME access to credit.

Women-owned MSMEs already have limited access to formal credit and other financial services and are at greater risk of being further left behind and marginalized. These MSMEs face specific challenges, such as the lack of collateral, low financial literacy, the sociocultural environment, entrepreneurship skills and lack of customized banking products.[6] Many of policy responses and interventions are gender agnostic and there is a lack of differentiated financial inclusion policies for women-MSMEs. The AFI framework will address these issues.

In light of these realities, AFI is developing a policy framework to enable members to enhance the MSME financing ecosystem in Africa. The framework will guide members to develop MSME financing policies and to identify best practices. The objective of this document is to provide a scope of what has to be addressed in such a framework and to assess what the most important elements are. In doing so, lessons from the global development community are taken into consideration to incorporate into the framework for Africa. This document and the Policy Framework are best read together for a better understanding.

Globally, SME access to finance remains a high priority in terms of government policy responses and interventions.[7] These policies span a wide range of elements, addressing increasing the reach of the credit provider market (extending credit guarantee systems, increasing public support for equity finance instruments and supporting digital forms of access to credit), supporting the development of tools for increased efficiency of MSMEs (implementing online tools, dealing with payment delays to MSMEs) and increasing non-financial support (increasing financial literacy and business skills).

1 In the context of this document and the ensuing policy framework, the term MSME is used in the same context as in AFI Guidance Note 36 SME Finance Guideline Note. The term refers to formal enterprises that have been registered by a recognized authority or agency. The definition of these enterprises varies from country to country, so the survey relies on each country's definition, preferably one set out by law or a particular set of regulations.

2 G20/OECD (2015), G20/OECD High-level Principles on SME Financing

3 WEF (2018), Why women hold the keys to Africa's future

4 Financial infrastructure refers to the framework and institutions for financial services provided by regulated service providers, and includes elements such as payment systems, credit information platforms and collateral registries.

5 IFC (2018), Closing Africa's MSME Finance Gap

6 AFI (2017), Survey Report on SME Finance Policies for Micro, Small and Medium Enterprises (MSMEs) Owned by Women and Women Entrepreneurs

7 OECD (2020), Financing SMEs and Entrepreneurs 2020 An OECD Scoreboard

There are also a number of threats that MSMEs are facing because of the impact of climate change, e.g. prolonged droughts in southern Africa affecting both water supply and hydro-electric power. Access to finance would help build the resilience of these affected MSMEs to the deal with the impact of climate change.

Job creation is one of the major challenges facing Africa in the coming years. An estimated 450 million young Africans will be joining the labour market by 2050, presenting a real challenge for the continent.[8] For Africa to accommodate these job entrants and to achieve its human capital potential, a vibrant private sector is required. Countries on the continent can build on the already substantial contribution of MSMEs in the private sector by active support and further developing the enabling ecosystem for MSMEs, with access to finance ecosystem as a key component. While there has been significant progress in the last decade to establish and enhance this ecosystem, much still needs to be done to enable MSMEs in Africa to drive the required economic progress.

PRINCIPLES FOR AND ELEMENTS OF MSME ACCESS TO FINANCE ECOSYSTEMS

Creating an enabling environment for the growth of MSMEs has been a major focus of international development agencies and groups for well over a decade. The G20's GPFI work has consistently focused on SME finance; the OECD has published extensively on most aspects of MSME development; and the World Bank Group, including the IFC, have made significant contributions to describe the framework and enabling ecosystems for MSMEs, including access to finance.

The GPFI/IFC document *SME Finance Policy Guide*[9] proposed a framework and highlighted some specific elements within this framework. It has served as the G20's guideline for SME access to finance, with further development over time. The framework is as follows:

- Regulatory and Supervisory Frameworks
- Financial Infrastructure
- Public Sector Interventions
- Women and SME Finance
- Agri-finance for SMEs

Some of the aspects highlighted in the framework included enabling alternative forms of finance, the importance of the payment system for SMEs and focusing on improving SME capacity.

The G20/OECD *High-level Principles for SME Financing*[10] expands this framework. The G20 Finance Ministers and Central Banks Governors requested the OECD, together with other relevant international organisations, to develop voluntary high-level principles on SME financing to provide a framework for government action on SME finance.

8 Proparco (2019), SME Finance in Africa - What's New;
9 IFC (2011), SME Finance Policy Guide
10 G20/OECD (2015), G20/OECD High-level Principles for SME Financing

PRINCIPLES ENCOMPASS THE FOLLOWING FACTORS:

IDENTIFY
SME financing needs and gaps and improve the evidence base.

STRENGTHEN
SME access to traditional bank financing.

ENABLE
SMEs to access diverse non-traditional financing instruments and channels.

PROMOTE
financial inclusion for SMEs and ease access to formal financial services, including for informal firms.

DESIGN
regulation that supports a range of financing instruments for SMEs, while ensuring financial stability and investor protection.

IMPROVE
transparency in SME finance markets.

ENHANCE
SME financial skills and strategic vision.

ADOPT
principles of risk-sharing for publicly-supported SME finance instruments.

ENCOURAGE
timely payments in commercial transactions and public procurement.

DESIGN
public programmes for SME finance, which ensure additionality, cost-effectiveness and user-friendliness.

MONITOR
and evaluate public programmes to enhance SME finance.

AFI utilized the available frameworks to formulate a guideline for AFI member countries, *SME Finance Guideline Note (Guideline Note 36)*.[11] This note outlines a range of options and good practices to facilitate access to finance for small- and medium-sized enterprises. The note is aimed at regulators preparing to plan, assess and implement policy and regulatory measures to support access to finance for SMEs and follows the elements of the framework mentioned above. The note lists recommendations for the various elements, making this a practical guide in terms of regulatory interventions. The note is informed by the global SME landscape, so member countries should customize their use of the note, based on their country context.

Recognizing that women entrepreneurs face specific challenges, the AFI network have expressed commitment towards advancing women's financial inclusion and halve the financial inclusion gender gap across members' jurisdictions by 2021, guided by the 10-point Denarau Action Plan.[12]

AFI has also been one of the pioneers in addressing the effects of climate change and championing green finance, with its effect on sustainability and poverty reduction. This intention is captured in the commitments contained in the Sharm El Sheikh Accord.[13] These commitments center around strengthening the AFI network's knowledge and awareness of the interlinkages between financial inclusion, climate change and green finance.

The AFI publication *Inclusive Green Finance Policies for MSMEs*[14] deals with the emerging fields of:

- the challenges posed by climate change to MSMEs; and
- inclusive green finance policies and regulations for MSMEs.

> View here

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- the challenges posed by climate change to MSMEs; and
- inclusive green finance policies and regulations for MSMEs.

This is done in the context of the AFI green finance framework of promotion, provision, protection and prevention, with the intention of using access to finance to help enable the transition to a sustainable and habitable environment.

11 AFI (2019), SME Finance Guideline Note
12 AFI (2016), Denarau Action Plan
13 AFI (2019), Sharm El Sheihk Accord
14 AFI (2020), Inclusive Green Finance Policies for MSMEs

Kenyan vegetable farmer carrying a crate of spinach on her head. (Photo by boezie/iStock)

2020 SMEFWG – QUESTIONNAIRE TO INFORM THE POLICY FRAMEWORK FOR THE MSME FINANCING ECOSYSTEM IN AFRICA

A survey among AFI SME Finance WG members was conducted to ascertain the policy, regulatory, service provider and user landscapes in the MSME access to finance ecosystems. The survey questionnaire is presented in Annexure 1. The results of the survey confirmed the general points of focus as described in this document, as indicated with references to the survey in some of the Sections of this document. Many of the members who completed the survey indicating well-developed ecosystems. However, there are also some areas where additional focus could prove to be beneficial.

The importance of developing and using an MSME access to finance policy was underscored by the vast majority of respondents (79 percent) indicating that a policy is in place or is in the process being developed. In practically all cases (90 percent), oversight of the policy and its implementation is done within a multi-institutional structure.

30%

The central bank/regulator was the institution carrying primary responsibility for this policy in only 30 percent of cases, indicating that country-specific dynamics and mandates determine the multi-institutional structure for this policy.

Most countries use structured data to assess the access to finance situation in a country to ensure that the design of initiatives and the setting of priorities are done on an informed basis. Countries use supply-side data from credit providers, with 50 percent of countries using demand-side surveys to get to an overall assessment. These surveys are done, or are intended to be done, on a regular basis.

Countries use diverse classes of providers to provide access to finance for MSMEs. In all cases, banks and microfinance institutions are enabled to act as credit providers.

46%

Some countries (46 percent) allow dedicated credit-providers, i.e. non-deposit taking institutions including credit unions, to provide credit to MSMEs.

The use of alternative sources is emerging (e.g. the capital market), with established regulatory oversight of such alternatives or being considered. Leasing and factoring still appear to be in a nascent phase, but the availability of these mechanisms for alternative finance seems to be growing, with 31 percent of respondents indicating that these mechanisms are being offered in their jurisdictions.

The market conduct of credit providers is regulated through some form of a regulatory framework in all the respondents' countries. The structure of these frameworks varies between countries. It includes:

> a general law prescribing market behavior of providers;
> a specific set of requirements in an act relating to credit providers or as part of acts specifying the role and responsibilities of different types of financial service providers;
> the issuing of regulations by the regulator.

The market conduct regulatory framework in many countries is further strengthened by a formal and independent dispute resolution mechanism that allows MSMEs who are aggrieved by the conduct of a credit provider to lodge a complaint with a designated authority.

The credit infrastructure in countries is developing and creating a more enabling environment for sustainable access to credit and increasing the market reach of credit providers. Credit information sharing through credit bureaus, risk-sharing for credit providers through credit guarantee schemes and the extension of collateral through movable asset registries and accompanying legal frameworks are used by the majority of countries. Some respondents also reported the use of credit repositories (in conjunction with the use of credit bureaus), as well as MSME credit rating agencies. Interestingly, no country reported the use of alternative data to inform the credit process for MSMEs.

Business development services are recognized as an essential element in the development and enabling of MSMEs, often in conjunction with access to finance. Such services are being used in most countries, with the state playing a major role in providing these services in more than half of the countries. An appropriate ministry or specifically established state agency often play a key role in business development, in conjunction with other participants in the MSME space.

The importance of addressing the informal MSME market was highlighted by those respondents indicating the relative importance of the informal sector in their countries. Figures of 40 percent - 70 percent of MSMEs were estimated to be informal, with an estimated contribution to GDP of 40 percent - 60 percent by the informal MSMEs.

It is clear from these figures that informality, and the associated difficulty with obtaining financial services and contributing more directly to the economy, is a key element in the AFI network.

Most countries recognized the importance of gender equality and empowering the youth in MSME development, but the importance of responding to climate change and supporting green finance did not feature as strongly in the survey results.

Traditional coffee shop. Ethiopia. (Photo by Stewart Innes/Shutterstock)

OVERVIEW OF RECENT MARKET AND POLICY DEVELOPMENTS IN THE MSME FINANCING ECOSYSTEM

MARKET DEVELOPMENTS

4.1.BANK LENDING REMAINS IMPORTANT, WITH SLOW GROWTH

The lingering consequences of the 2008 global financial crisis are still present in banks' general risk aversion, with banks slowly re-entering the MSME credit market. The MSME demand for access to finance is, therefore, developing into different sources. The OECD's *Financing SMEs and Entrepreneurs 2020 An OECD Scoreboard*[15] shows that SMEs globally are opting for alternative finance instruments to a significant extent, while the growth in straight debt volumes (e.g. bank lending) has been slower. This step towards financial diversification is in line with the *G20/OECD High-Level Principles on SME Financing* mentioned above.

The use of a diverse range of alternative financing instruments by SMEs globally, including asset-based instruments, online alternative finance and venture capital, continued to grow in the reporting period for the *Financing SMEs and Entrepreneurs 2020 An OECD Scoreboard* publication:

- Leasing and factoring volumes were up in a large majority of countries, in line with long-term trends. Growth in factoring accelerated;
- Online alternative finance activities were up by 54 percent;
- Venture capital investments rose by 20.9 percent;
- Public listings on SME stock markets in 2018 were down compared to 2017, but activities remained high from a long-term perspective.

On the other hand, both new lending to SMEs and the outstanding value of SME loans grew only modestly in 2018, with a significant drop in the growth rate of these two indicators. The shift from short-term to long-term SME lending continued, with long maturities outweighing short maturities in most countries. More than half of all new SME loans were of a maturity of more than one year.

Loan guarantees schemes remain the most widespread instrument to address market failure in MSME finance. Loan guarantee volumes continued to rise, with both governments and private institutions involved in promoting the SME providing guarantees.

25% About one-fourth of SMEs globally applied for credit, showing that the majority of SMEs do not seek external financing.

This figure has remained stable over the past four to five years, suggesting that the demand for credit has been relatively constant over the reference period. This seemingly low level of demand is caused by some SMEs not needing or wanting to use external debt, but it is also the result of a lack of access or a belief that credit will not be provided.

The European Investment *Bank's annual study Banking in Africa - financing transformation amid uncertainty*[16] provides an overview of the issues that service providers face in the African market. The study is based on interviews conducted with banking groups of various sizes and market focus across the continent and provides a useful summary of these service providers' perceptions of market conditions.

Overall, banks are planning to extend their loan activities, as could be expected. The manufacturing and agriculture sectors are the top focus areas, with most banks (87 percent) of the respondents placing a high priority to SME financing, although SMEs do not yet constitute a large proportion of bank portfolios in Africa. However, the banking groups identify some specific constraints to lending to SMEs: a shortage of bankable projects, a lack of effective collateral, a lack of managerial capacity, informality and a high default rate amongst SMEs. Most banks regard portfolio (loan) guarantees as important and necessary, but, unfortunately, consider the available schemes as not adequately meeting their needs. In terms of their own operational focus, banks mentioned credit risk management and lending technology.

15 OECD (2020), Financing SMEs and Entrepreneurs 2020 An OECD Scoreboard

16 EIB (2020), Banking in Africa - financing transformation amid uncertainty;

The reasons that banks mentioned that are holding them back from lending more to SMEs are given in figure 1 below.

As can be seen, the major reason given is lack of collateral, followed by managerial capacity and lack of information. The fact that banks did not consider competition to be a constraint (only 2 percent mentioned this) seems to indicate that there is significant scope for banks and other credit providers to expand into the credit market in Africa.

WAYS IN WHICH BANK LENDING TO MSMES CAN BE SUPPORTED

- The lack of collateral suggests that portfolio guarantees could have an important role to play.
- The lack of managerial capacity (and the high default rates) of SMEs suggest that capacity building for SMEs is an important lever to increase access to finance and productive use of such finance.
- The lack of information on SMEs suggests that building the capacity of the credit information industry (credit bureaus and others) could play an important role.

This requires better cooperation between commercial banks and policymakers to enhance the credit reporting systems. This cooperation is also required to establish and grow the use of collateral registries to enable greater levels of SME financial inclusion.

Banks report an increasing focus on establishing and deepening their digital banking services. Digital services reduce the cost of intermediating with smaller clients and provide deposit collection at a lower cost, as well as relieving some pressure on branch networks to fulfil their client servicing mandate. A focus area is the deployment of technology adapted to the context of African countries to lower the cost of and reduce the risks associated with providing loans to MSMEs.

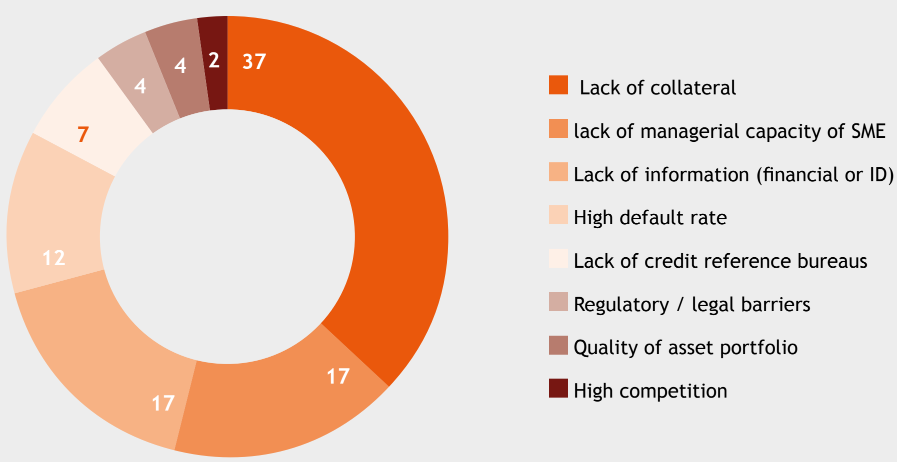
Optimizing the level of competition within Africa’s banking sectors is another challenge, as policymakers must strike a balance between decreasing lending margins (potentially reducing revenue) and ensuring financial stability (requiring higher levels of capital).

4.2. THE DIGITIZATION OF FINANCIAL SERVICES

The trend towards digitization in financial service providers take many forms and is ever-evolving:

- The digitization of delivery and payment channels (mobile and Internet banking, digital payments) is well-established.
- The use of mobile money, where Africa has been the leader for more than a decade.
- The increased digitization of services in banks and other FSPs (e.g. automated processes and digital client support).
- The incorporation of FinTechs in the products and services offered by FSPs.
- FinTechs offering services directly where regulations allow this.

FIGURE 1: MAIN OBSTACLE TO SME LENDING, %



Source: EIB report Banking in Africa - financing transformation amid uncertainty

The EIB report[17] *Banking in Africa - financing transformation amid uncertainty* confirms these trends and acknowledges that these trends are present in the African banking industry and, in some cases, world-leading.

While the long-term effect of the COVID-19 pandemic is still busy plying out, it is clear that the virtual universal response by banks and other FSPs to the pandemic has been an increased focus on digital financial services (DFS). In some cases, the additional take-up of these services has been well above expectations. In all likelihood, the pandemic has given the growth of DFS a permanent boost and an increased focus on the development of DFS is likely to follow.

The section *Digitization in Africa: Channeling Funding to SMEs* by Matthew Gamser from the IFC in the publication *SME Finance in Africa – What's New*[18] emphasizes that the digitization is not restricted to retail clients and payments, but that it actively extends into MSME access to finance as well. There are numerous examples in east and west Africa of such initiatives, and these are likely to grow significantly, for example, digital credit providers in Kenya and Tanzania.

Lessons and insights these developments are described in the CGAP/FSD Kenya publication *A Digital Credit Revolution Insights from Borrowers in Kenya and Tanzania.*[19] Digital credit in this study refers to loans that are delivered and repaid digitally, typically over a mobile phone. These loans are:

> **Instant.** Digital lenders use digital data, such as airtime top-ups, mobile phone call records, and app-based data (on smartphones), on potential borrowers to make near-instant credit decisions. Disbursement also happens quickly because loans are delivered digitally.

> **Automated.** From registration to application, disbursement, and repayment, lender decisions and actions are automated, based on pre-set parameters.

> **Remote.** Loan applications, disbursements, and repayments are managed and con¬ducted remotely, generally eliminating human interaction from the loan process.

Some of the important insights are:

> **Household and business needs dominate reasons for borrowing.** Digital borrowers report primarily taking out loans for ordinary house¬hold needs (35 percent in Kenya, 37 percent in Tanzania) or for busi¬ness purposes (37 percent in Kenya, 31 percent in Tanzania).

> **About half of borrowers reported having repaid a digital loan late, and a significant proportion re¬port having defaulted.** Fifty-six percent of borrowers in Tanzania and 47 percent in Kenya have repaid a digital loan late; 31 percent in Tan¬zania and 12 percent in Kenya report having defaulted.

> The survey findings suggest that digital credit is **not widely used by the most vul¬nerable groups** characterized by irregu¬lar cash flows, such as those primarily receiving income through farming and casual work.

> The results also indicate that **better transparency and consumer protection requirements are needed**, and regula¬tors will need tools to monitor com¬pliance and consumer outcomes in this market.

The G20 document[20] *Digital Innovation Can Improve Financial Access for SMEs* stresses the growing importance of DFS in MSME access to finance. Process automation, innovation in technology use and the sharing of data (from DFS) are identified as key issues. The potential contribution of digital services to improve efficiencies (thereby reducing cost) and making access to such services far more widespread (thereby increasing reach) requires on-going support from all stakeholders, including regulatory authorities.

The IFC in the publication *Digital Access: The Future of Financial Inclusion in Africa*[21] arrives at very similar conclusions. It highlights the use of alternative data to develop new credit products and the potential of DFS to provide banking services to small-scale farmers and digitizing the specific agricultural value chain in the process. The digitization of the cocoa value in Côte d'Ivoire is described, showing that DFS could serve as an entry point for broader financial inclusion of the farming community.

17 EIB (2020), Banking in Africa - financing transformation amid uncertainty
18 Proparco (2019), SME Finance in Africa – What's New
19 CGAP/FSD Kenya (2018), A Digital Credit Revolution Insights from Borrowers in Kenya and Tanzania;
20 G20 (2019), Digital Innovation Can Improve Financial Access for SMEs
21 IFC (2018), Digital Access: The future of Financial Inclusion in Africa;

POLICY DEVELOPMENTS

4.3.NATIONAL COORDINATION OF MSME DEVELOPMENT, INCLUDING ACCESS TO CREDIT

MSME ecosystems are complex, with different components falling under different governmental domains and regulatory frameworks. Overarching MSME policies, therefore, require active coordination among the major stakeholders. In the absence of such a coordinating effort, component-based policy initiatives run the risk of not achieving the desired impact, because of factors outside the scope of such individual policies. Many countries have established such coordinating structures, with the central bank and other key members of financial services regulators of such structures.

The survey conducted amongst AFI SME Finance WG members (refer Section 4 of this document) confirmed that an overall MSME policy either exists or is in the process of being formulated. In most cases, the Ministry of Trade/Commerce/Industry or similar holds the primary responsibility or the policy, but in a few cases, it is the central bank (e.g. Morocco) or a coordinating financial inclusion structure (e.g. Mexico with the National Council for Financial Inclusion). Some countries do include gender-specific issues in this policy (e.g. Zimbabwe), which makes it easier to implement the policies in a gender-sensitive matter.

The OECD document *Improving the business environment for SMEs through effective regulation*[22] makes the point that it is key for MSME development to make the interaction of MSMEs with the various regulatory requirements as efficient and as simple as possible. It has become best practice to set up a single facility that enables MSMEs to register with all applicable authorities and agencies as a one-stop-shop. This type of approach is the outcome of a coordinated approach and is in the interest of all stakeholders.

Regulatory authorities are using the coordinating approach to extend the scope of their efforts to improve the MSME access to finance ecosystem. The Central Bank of Egypt is an example of this, in that, their Nile Pioneers[23] initiative involves the Nile University, the Financial Regulatory Authority and the Egyptian Banking Institute. This initiative has evolved, aiming to enable SME lenders to understand the SME landscape and to assist the lenders to engage in improving the capacity of MSMEs through business development centers, supported in part by the expertise from the University and the capacity of the Financial Regulatory Authority. This constitutes a virtuous circle in the ecosystem, in that, improved capability within lenders will lead to improved capacity in MSMEs, resulting in business growth for both.

4.4. THE USE OF DATA TO ENHANCE THE MSME ACCESS TO CREDIT ECOSYSTEM

The availability and use of data are essential to inform MSME access to finance policy and strategy, improve the effectiveness of the credit risk reporting infrastructure and inform the design of the credit products and service models offered by credit providers. The more complete, accurate and relevant the data sets are, the better the ecosystem operates and develops.

22 OECD (2018), Improving the business environment for SMEs through effective regulation;

23 Oxford Business Group (2019), New lending initiatives increase access to finance for Egypt's SMEs;

Baker in shop selling traditional puffed and round bread on street of Cairo, Egypt. (Photo by Juan Alberto Casado/iStock)

It is important to collect and provide data that enables gender-specific and youth-specific insights, as such insights are necessary to effectively include these segments.

The G20/OECD *High-level Principles for SME Financing*[24] are explicit on the use of informed evidence to guide policies and strategies. As a first step in developing a strategy for enhancing MSME access to finance, governments should assess the extent to which SMEs' financing needs are met and where gaps exist. This should be done in cooperation with relevant stakeholders, including central banks and financial supervisory authorities, financial services and research institutions and SME representatives. Efforts should be placed on improving statistical information about SME financing, particularly in developing economies, as a lack of reliable evidence constrains policy design, implementation and assessment. The use of standardized data and measurement indicators, within and across countries, facilitate international benchmarking and regulatory coordination, and can shed light on outstanding financing gaps and issues. In this regard, the AFI *SME Financial Inclusion Indicators Base Set*[25] should be populated and used, as this represents the consensus of AFI members on what the most important indicators are and the sources of the data to populate those indicators.

The supply-side of MSME finance is being addressed by credit providers and regulatory authorities with information regularly updated by the credit providers. Credit registries (see Section 3.8 below) are also beginning to play a significant role in informing authorities of the take-up and portfolio quality of MSME lending. To get a complete view of the state of use/non-use of MSME access to finance, demand-side information is also necessary. This typically requires a survey to be undertaken. Some demand-side surveys exist and are being used, like the FinMark Trust FinScope MSME surveys,[26] used by a number of countries in Africa. The survey undertaken among AFI Finance Working Group members (see Section 4 below), indicated that an estimated 50 percent of AFI member countries use demand-side surveys, including countries such as Eswatini, Namibia, Zimbabwe, and Egypt. Such surveys provide a perspective from the MSME sector and highlight constraints and realities that could be targeted by policy and regulatory interventions. For example, Namibia used the demand-survey to formulate the MSME access to finance policy, based on the needs of the MSMEs as determined in the survey. This has led to the focus on business services for the development of MSMEs and the strengthening of the dispute resolution mechanisms in the country. In the case of Eswatini, the realization that micro and informal businesses are not being served by financial services providers (as indicated by the survey) led to the establishment of business clinics – regular focus group discussions with such enterprises to keep track of their needs and to what extent these are being met.

The WBG's Enterprise Surveys[27] covers most countries and provides a ready-made basis for assessment and cross-country comparison. These surveys are firm-level surveys of a representative sample of an economy's private sector. The surveys cover a broad range of business environment topics, including access to finance, corruption, infrastructure, crime, competition, and performance measures. The survey results are in the public domain. The European Bank for Reconstruction and Development (EBRD) recently launched an initiative[28] to conduct MSME surveys, similar and compatible to the WBG's enterprise surveys, in 40 countries in central Europe, Russia, Central Asia, the Balkans, parts of the Middle East and North Africa. Topics included in the questionnaire – such as productivity, the adoption of technology and innovation, competition, the qualification of the workforce, informality, access to financial services, infrastructure and the impact of government regulations – will be comparable on a global scale. The survey will also include a module on the green economy.

The AFI *SME Finance Guideline Note*[29] similarly stresses the importance of data in the SME finance system, referencing the AFI SME Financial Inclusion Indicators Base Set. It also makes the connection between such data and the business advisory services to respond to the needs of SMEs.

> View here

24 GPFI (2015), G20/OECD High-level Principles for SME Financing

25 AFI (2015), Guideline Note 16: SME Financial Inclusion Indicators Base Set;

26 http://finmark.org.za/_programme/data-for-financial-markets/finscope/finscope-msme/

27 https://www.enterprisesurveys.org/en/about-us

28 https://www.ebrd.com/news/2018/ebrd-eib-and-wbg-launch-new-enterprise-survey-in-over-40-countries.html

29 AFI (2019), SME Finance Guideline Note

4.5. REGULATORY FRAMEWORKS

Regulatory frameworks are the essential maps to the MSME access to finance landscapes. The frameworks define the classes of credit providers that can operate in a market, under what conditions and under what prudential requirements. It is therefore essential to ensure that such frameworks enable a sufficiently broad range of classes of credit providers to meet the needs of the market in a stable and sustainable manner.

Commercial banks typically have limited reach with their branch networks skewed towards urban areas. It is, therefore, necessary to enable other classes of financial service providers, i.e. non-bank financial service providers or NBFIs to establish a presence in the more rural areas. This is especially necessary to serve rural areas and farming communities. Most countries have established a microfinance regulatory framework with this in mind, with appropriate levels of capital adequacy and regulatory compliance to allow for lower operational costs. In some countries, e.g. Ghana, this approach has been successfully refined by establishing second- (microfinance institutions) and third-tier (microcredit institutions) to serve the entire MSME (and individual) markets in Ghana.

The use of technology enables different types of credit providers and different mechanisms for MSME access to finance. The IFC publication *Regulating Alternative Finance: Results from a Global Regulator Survey*[30] mentions peer-to-peer/marketplace lending and equity crowdfunding as two such developments with significant potential. Whilst such developments hold many promises, each also brings particular risks and regulatory challenges and should be included in the regulatory frameworks of countries.

4.6. INCREASED FOCUS IN ALTERNATIVE MECHANISMS FOR CREDIT ACCESS

The continued slower than required growth in lending from banks and similar types of credit providers to the MSME sector, due to mismatches in what banks can offer and what MSMEs require, has led to the increased use of alternative mechanisms for MSME financing, as mentioned in section 3.1 above.

The OECD publication *New Approaches to SME and Entrepreneurship Financing: Broadening the Range of Instruments*[31] provides an overview of these alternative mechanisms and has been used in international forums discussing the issue of alternative financing:

> **Asset-based finance** is a widespread form of finance for SMEs, used to monetize the value of specific assets and access working capital under more flexible terms than they could from conventional lending channels. As firms obtain funding based on the value of specific assets, including accounts receivables, inventory, machinery, equipment and real estate, rather than on their own credit standing, asset-based finance can serve the financing needs of start-up and small firms that have difficulties in accessing traditional lending. In the forms of factoring and leasing, asset-based finance is widely used in many countries.

30 IFC (2019), Regulating Alternative Finance: Results from a Global Regulator Survey;

31 OECD (2015), New Approaches to SME and Entrepreneurship Financing: Broadening the Range of Instruments;

Vendors in a fresh food and grain market. Tamale, Ghana. (Photo by fivepointsix/Shutterstock)

> **Factoring** is defined as a type of supplier financing, in which enterprises (sellers) sell their creditworthy accounts receivable at a discount (generally equal to interest plus service fees) and receive immediate cash from a specialized institution, or factor. In other words, the factor buys the right to collect an enterprise's invoices from its customers, by paying the firm the face value of these invoices, less a discount.

The degree of regulation governing factoring varies between countries. There are four main regulatory approaches:

- countries with complete supervision, regulation and licensing of all factoring products and services (China);
- countries that require factoring service providers to obtain a banking license and hence, compliance of capital adequacy regulations (e.g. Mexico);
- countries that require registration by the factor as a financial institution, but do not regulate capital adequacy (e.g. Turkey);
- countries with no official regulation or governmental supervision, but in which membership to international factoring associations is well-established (e.g. Russia).

The survey conducted among AFI SME Finance WG members confirmed the use of factoring FI members' countries, e.g. in Mexico, Eswatini, Costa Rica, Bangladesh and Zimbabwe.

The Mexican *DFI Nacional Financiera (NAFIN)* has enabled the successful implementation of factoring. NAFIN's program, in essence, links small and more risky suppliers with larger, creditworthy firms that buy from them. Small firms can then use the receivables from their larger clients to secure loans. Participating SMEs must be registered with NAFIN and have an account with a bank that has a relationship with the buying enterprise. Following a factoring transaction, funds are transferred directly to the MSME's bank account and the factor service provider (i.e. the bank) becomes the creditor. NAFIN requires that all factoring services are offered without additional collateral or service fees, at a maximum rate that is below commercial bank rates. The sale of receivables and the transfer of funds are done electronically. Through this arrangement, around 7000 MSMEs per annum have benefitted from the scheme.

> **Leasing** is a three-party arrangement, where one party, the lessor, buys an asset from the supplier upon request of the lessee (e.g. the MSME) and leases this asset to the lessee for a certain period in exchange for leasing payments. The total value of leasing payments may or may not amortize the cost of the leased asset.

Leasing typically requires initial down payments from the MSMEs. Research shows that companies without an established credit profile use leasing more often than well-established companies because leasing allows them to reduce their financing costs relative to other options.[32] The main reason for this is that the lessor retains ownership of the asset, thereby reducing the risk to the lessor.

From a public policy perspective, leasing incentivizes formality in economies, where widespread informality exists. Informal SMEs have limited access to formal sources of finance, such as banks. Once a business starts operating with leasing, it begins to establish a credit profile that becomes part of the formal credit information system. This information then becomes available to financial institutions, enabling MSMEs to access additional financial services.[33]

Leasing is used extensively in developed and larger economies, but its use is evolving in emerging economies as well, with Brazil, Colombia and South Africa having active leasing markets. The survey referred to earlier confirmed the use of leasing in many AFI members' countries, with use more widespread than for factoring.

> **Debt securitization** and covered bonds are instruments for the refinancing of banks and their portfolio risk management. In essence, banks would package and sell a portion of their loan book to raise finance for further business activity. This market has developed significantly, although the global financial crisis slowed this development for a while. These are important instruments to foster SME lending, as the process of securitization draws in other funders that are not necessarily engaged in the MSME market.

> **Crowdfunding** has grown rapidly since the mid of the 2000s, but it still represents a minor share of business financing. While the pace of technological developments has enabled a rapid diffusion of crowdfunding, the regulatory environment has limited a broader adoption, especially for securities-based crowdfunding (equity crowd-funding). With proper regulatory oversight and market development, there is no reason why this cannot become a more significant mechanism for MSME access to finance.

32 Sharpe and Nguyen (1995), Capital Market Imperfections and the Incentive to Lease

33 Al Sugheyer and others, IFC (2009), Leasing in development. Guidelines for emerging economies.

> **Hybrid instruments** combine debt and equity features into a single financing vehicle. These techniques represent an appealing form of finance for enterprises that are approaching a turning point in their life cycle. When the risks and opportunities of the business are increasing, a capital injection is needed, but these enterprises have limited or no access to debt financing or equity, e.g. young high-growth companies. Governments can use one of the mechanisms that have been deployed in a country (see Section 3.7 below) to participate in these instruments, typically by establishing a fund or funds for a specific purpose, e.g. innovation funds.

> **Equity finance** comprises all financial resources that are provided to the firms in return for an ownership interest. These include including public instruments, i.e. equity shares traded in some form of a stock exchange, and private equity tools, which are relevant for the unlisted companies' market. Equity investors do not receive any security from the investee company and their return is entirely determined by the success of the entrepreneurial venture. Equity financing is especially relevant for companies that have a high risk-return profile, such as new, innovative and high growth firms. Seed and early stage equity finance can boost firm creation and development.

For decades, private market participants and authorities have been encouraging the establishment of public SME equity markets. However, many SME exchanges have failed to attract sufficient companies for listing or achieved sufficient trading to maintain active markets. A key challenge is to achieve the right balance between greater flexibility and lower costs for SMEs wanting to use this form of financing and due diligence requirements to preserve market integrity and transparency and attract investors. India's NSE Emerge[34] is one of the more successful SME equity initiatives. It is part of the National Stock Exchange (NSE), aimed at SMEs and start-up companies. These companies can get listed on NSE Emerge without an Initial Public Offering (IPO) and with simplified requirements. Over 200 companies have listed and about a dozen have moved to the main board of the NSE.

> **Venture capital and angel investing** (private equity) are typically targeting a small pool of high-growth potential companies, with the capacity for high returns in a short timeframe. The two forms are similar in some respects but are characterized by different motivations, stage of investment, scale and operating models. Business angels invest their own money, rather than collecting funds from a variety of investors, focus mainly on the seed and early stage, contrarily to venture capitalists' increasing focus on later stages, bring into the venture their own entrepreneurial skills and expertise, with a more hands-on role in the company than venture capitalists.

34 https://www1.nseindia.com/emerge/index_sme.htm

Market trader swiping a credit card on a pos machine. Nigeria. (Photo by i_am_zews/Shutterstock)

4.7. CONTINUED SUPPORT FROM DIRECT STATE PARTICIPATION

Some form of direct state support is one of the cornerstones for improving the MSME access to finance ecosystem. The IFC's *SME Finance Policy Guide*[35] provides an overview of the mechanisms in use and gives some guidelines for the use of these mechanisms:

> State Banks

For state-owned banks to play a positive and complementary role in the provision of credit to SMEs, the following are advisable:

- Legislation must specify clear mandates, relating to identified gaps in MSME financing;
- Sound governance structures with independent boards;
- Clear performance criteria, preferably with a defined exit if the objective has been met;
- The obligation to price loans according to risk, and to generate a positive return;
- The ability to recruit and retain qualified staff.

There are many examples of successful state banks, with Morocco's *Crédit Populaire du Maroc* (CPM) being one such example. It has succeeded in serving SMEs due to its proximity to clients and an effective governance structure. It is one of the largest Moroccan banks, accounting for one-fourth of the country's banking assets. SME finance has been a significant source of profits due to good credit quality, effective pricing, and an inexpensive funding base. A specific law lays out the foundations for effective governance by clearly defining the CPM's mandate and establishing checks and balances between the head office and its cooperative members.

> Apexes and Other Wholesale Funding Facilities

Second-tier funding facilities, or apexes, can be set up to manage and on-lend funds to financial institutions, and to accelerate the growth of sound SME retail capacity to expand access to finance. Guidelines include:

- Define the apex mission and objectives clearly with a focus on sustainable and responsible financial institutions and SMEs;
- Focus on putting in place good governance and professional management, with the instruments on offer by the facility geared to market context;
- Manage an apex portfolio based on performance, which includes sufficient data to enable complete reviews of financial institution portfolios and be willing to act in the case of poor performance;
- Encourage apexes to crowd in commercial local funding by having this as one of their objectives.

> Public Credit Guarantee Schemes

Credit guarantee schemes are an essential component of the credit infrastructure (see Section 3.8 below). State intervention is often required to establish such a scheme and to ensure that it is adequately capitalized to meet its commitments. This involvement does not have to preclude co-investment and co-ownership by other interested parties, e.g. commercial banks. Governments can also directly guarantee loans, especially in times of crises, as happened in a few countries in the current COVID-19 pandemic. Such measures should only be applicable for a short period and for a particular unforeseen event.

> Government Procurement from SMEs

The public sector can be a major buyer of goods and services from SMEs. In some countries, government entities are encouraged to procure a percentage of their required goods and services from MSMEs, with some of these targets allocated to women-led MSMEs. This procurement from MSMEs can more effectively link these enterprises to supply chain finance and to factoring through the contractual and payment relationship.

This procurement and development of the MSME access to finance ecosystem is a key growth lever for the MSMEs to extend their market reach and improve their operational maturity and sustainability.

MSMEs in some countries are often quite critical of the promptness of payments from the public sector. Failure to pay on time increases the cost of doing business and could put the MSME in financial distress. It is therefore critical that the public sector institutions pay SMEs promptly. This should also set the benchmark for business-to-business payments, as delays in such payments are equally problematic for MSMEs.

> SME Capacity and Business Skills

Business skills and management capacity are typically areas in which MSMEs require support. The EIB study referred to earlier identified these as major constraints faced by banks in Africa in the process of providing access to finance.

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35 IFC (2011), SME Finance Policy Guide

Recommendations for public sector-supported initiatives to improve MSME capacity and business include:

- Structure the interventions in such a manner that standardized content is optimized, but not at the expense of required segment-specific content.
- Follow a "train the trainer" approach, so that the intervention can easily be scaled.
- Coordinate the activities and roles of public and private organizations in the capacity building interventions.
- Benchmarking and program evaluation are not simple, yet ongoing monitoring and evaluation is critical to the effective use of interventions.

> Other Areas of State Involvement

The OECD's *Financing SMEs and Entrepreneurs 2020 An OECD Scoreboard*[36] identifies a number of specific areas (some already mentioned in this section) that are and will continue to benefit from public sector involvement:

- Extending the reach and use of credit guarantee volumes;
- Public support for equity finance instruments;
- Regulatory approaches and targeted policies to support FinTech developments are becoming more widespread;
- Initiatives to foster "open banking," whereby financial institutions are obliged to share their data with third-party financial service providers, are emerging;
- Governments are implementing online tools for SMEs and entrepreneurs to find the appropriate financial and business support.

It is common amongst MSMEs, particularly micro-enterprises, not to be aware of the services, finance mechanisms and skills training that are available to them. This is detrimental to the financial well-being of the MSMEs and the potential contribution to the economy that such enterprises can make. A program of outreach and awareness, aimed at getting the information to the whole MSME segment, including informal MSMEs, is therefore required. This campaign should focus on segments with specific needs, e.g. women- and youth-led enterprises and should be structured in such a manner that it is easily understood by all MSMEs.

4.8.FURTHER DEVELOPMENT OF THE CREDIT INFRASTRUCTURE

The credit infrastructure in a country is a key component in the MSME access to finance ecosystem. The extent to which this infrastructure is developed plays a major role in making access possible, driving efficiencies and sustaining the viability of MSME finance.

Credit guarantee schemes and credit information systems are the two most used and required parts of the infrastructural ecosystem. The WBG document *SME Finance*[37] highlights the use of credit guarantee schemes (CGS). A CGS provides partial guarantees on loans to borrowers by covering a share of the default risk of the loan in exchange for a fee. It is widely used in most developed and developing countries, particularly to alleviate financing constraints of MSMEs.

36 OECD (2020), Financing SMEs and Entrepreneurs 2020 An OECD Scoreboard

37 WBG (2017), SME Finance

Local SMEs around the FCE train (Fianarantsoa - East Coast) during a stop in a railway station. Madagascar. (Photo by pierivb/iStock)

As mentioned earlier in this report, banks view guarantee schemes as the most common and effective government program to support SME financing in developed and developing countries, ahead of directed state involvement or subsidies.

In terms of financial sustainability, the performance of public credit guarantee schemes has been mixed at best. Studies show that Chile's scheme covers all its costs through fees and interest income, but studies of other schemes show that some CGSs require additional government support to be sustainable.

While CGSs can be useful mechanisms for increasing access to SMEs, it is a challenge to design and manage these initiatives sustainably.

Some credit guarantee schemes target the agricultural sector and incorporate elements of green finance, such as NIRSAL (Nigerian Incentive-Based Risk Sharing Initiative for Agricultural Lending) and NIRSAL, a similar institution in Ghana.

GUIDELINES FOR EFFECTIVE CREDIT GUARANTEE SCHEMES

- **Eligibility criteria:** Guarantee schemes should target SMEs through ceilings on turnover, number of employees, and/or size of the loan.
- **Approval rules and procedures:** Final approval or rejection of an application should occur within two weeks.
- **Coverage ratios:** Coverage ratios should ensure sufficient protection against default risk, while maintaining strong incentives for effective loan origination and monitoring.
- **Fees:** Fees should be risk-based and contribute to the financial sustainability of the scheme.
- **Payment rules and procedures:** Payment rules should take into account the effectiveness of the collateral and insolvency regimes. Schemes in LDCs should base payments on default events, while ensuring incentives for effective debt collection.
- **Supervision:** Oversight is a key element to ensuring the soundness of operations.
- **Risk weighting for banks' prudential requirements:** A well-designed and financially robust guarantee scheme should allow regulators to assign a lower risk weight to exposures covered by the guarantee.

A popular form of a private CGS is a mutual guarantee association. MSMEs are the members of such a scheme, with each member depositing money into a fund that in effect, guarantees loans of members at financial institutions, based on a contractual agreement between the members.

An example of a successful CGS is FOGAPE, a scheme operated by Banco Estado, a state-owned bank in Chile. It provides partial guarantees on SME loans extended by commercial banks and counter-guarantees to mutual guarantee associations. FOGAPE targets SMEs who lack collateral or need longer maturities. It operates like a traditional guarantee scheme by sharing the risk of default on eligible loans and charging a guarantee premium. However, it also conducts a number of auctions every year, where banks submit bids indicating the amount of guarantee it wants to receive and the minimum coverage ratio it is willing to accept. Coverage ratios fluctuate around 70 percent. Banks pay a premium that depends on their historical default and claims performance, and that typically varies between 1 and 2 percent of the outstanding balance. Banks with high default rates can be excluded from the scheme. FOGAPE has been financially sustainable, due to the auctioning of coverage ratios, the risk-related fees, and an average net loss ratio of 1.5 percent of guarantees.

A key question related to the impact of CGSs is whether they lead to additionality, that is, whether they generate additional loans for targeted firms and allow them to borrow at better terms. Most empirical studies find evidence of financial additionality. One such study[38] analyzed Chile's credit guarantee scheme for bank loans to SMEs. Their statistical analysis finds that credit guarantees have large positive effects on firms' total borrowing without large increases in default rates. They also find that the scheme has a strong amplification effect: firms increase borrowing from other banks in the 18 months following a loan guarantee; firms receiving guarantees build new bank relationships and firms use the credit increase to expand their operations. These results are likely to apply beyond Chile.

38 William Mullins & Patricio Toro (2018), Credit Guarantees and New Bank Relationships, Central Bank of Chile

The WBG study[39] *Improving Access to Finance for SMEs - Opportunities through Credit Reporting, Secured Lending and Insolvency Practices* provides an overview of additional components of the credit infrastructure:

In this study four practices in credit reporting are discussed:

> improving borrower identification when it comes to SMEs;
> identifying and including more sources that report information on SME borrowing;
> facilitating comprehensive delivery of financial information; and
> developing credit reporting products customized for SMEs.

As mentioned, credit reporting systems are essential in any well-functioning MSME access to finance ecosystem and are widely used. This use was confirmed by the AFI survey mentioned, which indicated that most AFI members' countries have such a system in place. It is the most important element in addressing the inherent information asymmetry in the MSME credit market. Apart from the four key practices mentioned above, regulatory oversight to ensure equitable access and maintaining appropriate data ownership is a key requirement.

The use of alternative data to inform the credit process is increasing, as more data becomes available to utilize. This is especially true in the mobile space, where both mobile service use and mobile money use generate data on users that can be incorporated in the credit decision process. This development holds the twin advantage that such data is already available, and it is not dependent on the previous use of credit facilities. As such, it is advantageous to women, as no bias is introduced in the decision process, and to first-time borrowers without a credit history. Such use is already in place in Ghana and Zimbabwe, albeit it on a provider-specific basis. The next step would be to make such information available to all participants in the credit information system.

Secured lending practices are discussed in the context that, in developing economies, almost 80 percent of firms' capital stock consists of movable assets, such as machinery, equipment and receivables. Smaller firms, in particular, are less likely to have access to fixed assets like a plot of land or building. As such, movable assets are the main type of collateral that an SME can offer to secure financing. However, where legal and institutional protections are inadequate, banks are often reluctant to accept movable assets as collateral. Women are especially disadvantaged through a lack of access to traditional forms of collateral here.

For rural women, limited access to land ownership constrains their ability to provide fixed collateral for loans and therefore, limits investment in agricultural inputs and equipment. Enabling and providing a framework to incorporate movable assets are therefore key to empowering women entrepreneurs.

39 WBG (2018), Improving Access to Finance for SMEs - Opportunities through Credit Reporting, Secured Lending and Insolvency Practices

Woman selling peanuts and beans in the street in her village. Zimbabwe. (Photo by Lucian Coman/Shutterstock)

Secured lending practices require a legal framework to determine creditor and debtor rights and to define proceedings to follow, in case of default. Studies confirm that stronger legal protections for creditors translate into greater access to finance for SMEs. One study[40] explores the impact of creditor protection on SMEs' access to bank credit using cross-country firm-level data for 54 countries. It concludes that in countries with limited creditor protections, smaller companies have significantly less access to bank credit compared to larger ones. Creditors are better protected, and hence more inclined to engage in lending, when secured transaction rules define how the rights of creditors in the collateral are established and how collateral priority is determined.[41]

A collateral registry, which lists and records the existence of security interest in movable assets help to protect the rights of creditors in secured lending. Such registries are publicly available databases of interests in or ownership of assets. A comprehensive and integrated secured transactions regime requires a well-functioning collateral registry. This mechanism supports the legal framework of security rights in movable assets by recording claims on the assets and establishing priority, based on the time of registration.

In Africa, Ghana, The Gambia, Liberia, Malawi, Nigeria and Zambia have launched modern collateral registries, i.e. a centralized facility, where any interest in an asset is noted and available as part of online public access to the registry.

4.9. INFORMAL MSMEs[42] AND THE MOVE TO FORMALITY

Many businesses in the developing world are informal, in the sense that they are not formally constituted and registered as business entities. The situation in Africa, particularly sub-Saharan Africa, is typical of this situation. Moving from a situation of substantial informality to greater formality is a complex process and require careful planning. Many enterprises are established because there are no alternatives to maintain livelihoods, i.e. the so-called "survivalist" enterprises. The societal impact of these enterprises will be improved by enabling them to acquire and use financial services, including access to credit, to allow the enterprises to become more resilient and sustainable. Once this is achieved, then the move towards formality becomes more realistic and beneficial.

Typically, credit providers will view informal enterprises as individuals and will deal with them as such. The study *Financing the growth of SMEs in Africa: What are the constraints to SME financing within ECOWAS?*[43] finds that formality strongly influences MSME access to credit in the West Africa region. The recommendation that there should be a strong move to formality and SMEs forming groups to improve access to finance, are not without significant practical challenges.

The GPFI report, *Use of Alternative Data to Enhance Credit Reporting to Enable Access to Digital Financial Services by Individuals and SMEs operating in the Informal Economy,*[44] proposes a different approach and advocates the use of alternative data to bring informal or un-served enterprises into mainstream financing. The report acknowledges that the use of such data poses an additional risk in the access to the credit ecosystem, primarily related to business practice, data privacy and consumer protection issues. The report lists 21 detailed recommendations to deal with these issues.

According to the World Bank Enterprise Surveys, the main reasons that MSMEs state for not registering their business, are the lack of information on how to register an enterprise, the time to complete the registration process, taxes that registered businesses would need to pay, and the lack of perceived benefits from formalization.[45] Interventions in South Asia and Latin America show that simplifying business registration channels, reducing registration costs, and providing greater information on the benefits of registering a business have proven to have had little effect to increase the formalization of firms. In Zimbabwe, the government has adopted an inclusive approach and is working with the Zimbabwe Revenue Authority, local authorities and MSME associations to promote the formalization of the informal sector and come up with an appropriate tax and accounting regime for MSMEs.

40 Chong, Alberto, Arturo Galindo and Alejandro Micco (2004), Creditor Protection and SME Finance

41 Berger, Allen N., and Gregory F. Udell (2006), A More Complete Conceptual Framework for SME Finance

42 "Informal MSMEs" in this context refers to enterprises operating without a business license or registration, i.e. these enterprises are not recognised by any authority.

43 Peter Quarteya, Ebo Turksona, Joshua Y. Aborb, Abdul Malik Iddrisua (2017), Financing the growth of SMEs in Africa: What are the constraints to SME financing within ECOWAS?

44 GPFI (2018), Use of Alternative Data to Enhance Credit Reporting to Enable Access to Digital Financial Services by Individuals and SMEs operating in the Informal Economy

45 IFC (2013), Closing the Credit Gap for Formal and Informal Micro, Small, and Medium Enterprises

In South Africa the focus has been on simplifying the tax obligations for small and micro-enterprises, through two mechanisms:[46]

> small business corporation tax, which includes favorable and graduated tax rates and allows accelerated depreciation;
> turn-over tax, aimed at micro-enterprises and only uses turnover for tax purposes and eliminating the need for detailed records of expenses to be kept.

There are some indications that these measures have been adopted by MSMEs (about 18 percent of all business tax returns utilized one of these mechanisms), but it is still uncertain to what extent this has decreased informality.[47]

Section 3 above confirms the incidence and the importance of informal MSMEs in the AFI network. Suffice to note, that in some cases the contribution of informal MSMEs is estimated to be up to 50 percent of all enterprises (in terms of total turnover). This underscores the importance of addressing the informal sector of MSMEs and structuring avenues to formality.

4.10. LEGAL STRUCTURES DEALING WITH DEBT REVIEW AND INSOLVENCY PROCEEDINGS

The legal and regulatory framework dealing with enterprises in financial distress is a key element in the MSME access to finance ecosystem. Certainty around the rights of creditors and debtors are a prerequisite for the market entry and participation of credit providers, and other access to finance participants, as well as for MSMEs to utilize the finance provided.

Availability and transparency of processes to enable financially distressed enterprises to regain financial viability again or, if this is not possible, to optimize and fairly distribute assets to creditors, are therefore regarded as basic building blocks in the access to finance ecosystem.

This framework has three components that are of particular interest to MSMEs:

> Debt review (with possible debt restructuring) without involving a legal process;
> Entering into a legal process to restructure the enterprise, if feasible (pre-insolvency proceedings);
> Simplified (or specialized) insolvency proceedings to allow quick, efficient and fair market exit for failed MSMEs.

The WBG document *Improving Access to Finance for SMEs*[48] provides an overview of these components, referring to countries that have adopted specific approaches.

46 Rajendra Rajaram (2019), The Effectiveness of Tax Relief Initiatives on SMEs in South Africa
47 Deloitte (2019), The tax compliance burden for small and medium enterprises (SMEs)
48 WBG (2018), Improving Access to Finance for SMEs Opportunities through Credit Reporting, Secured Lending and Insolvency Practices

Five workers in a carpentry workshop, portrait. South Africa. (Photo by Monkey Business Images/Shutterstock)

Debt Review and Out-of-Court Workouts (OCWs)

Bankruptcies are viewed as a last resort to preserve viable firms in financial distress. However, when dealing with insolvency or financial distress, SMEs face different legal, regulatory and financial constraints than large corporations. OCWs can meet the needs of SMEs by reducing the expenses associated with litigation, cutting the time required to ease corporate distress and easing the uncertainty surrounding adverse outcomes. OCWs refer to debt restructuring that involves a multilateral agreement with creditors to change a debtor's composition of assets and liabilities without the intervention of a court. OCWs are used to ensure rapid recovery for distressed companies through a voluntary agreement (compromise) between the distressed company and its creditors. An OCW may involve debt rescheduling, reduction of interest rates, total or partial write-off of debt, or even new loans. The most common features of OCWs are a standstill period when creditors cannot enforce their claims and a good faith negotiation requirement (i.e. negotiating towards a solution).

As an example of a successful debt review process, the government of Malaysia established a Corporate Debt Restructuring Committee (CDRC) to provide a platform for corporate borrowers and their creditors to work out feasible debt resolutions without having to resort to legal proceedings. The aim of the CDRC is to help sustain economic activity and employment in Malaysia by expediting debt restructuring of viable enterprises. The operations of CDRC are governed by a code of conduct.[49]

Out-of-court processes are regularly used in the following countries: Australia, Belgium, Colombia, France, Greece, Guatemala, Italy, Japan, Latvia, Malaysia (as mentioned), the Philippines, the Republic of Korea, South Africa (where it is known as Business Rescue) and the United Kingdom.

Pre-Insolvency Proceedings

Pre-insolvency proceedings aim to restructure firms before they become formally insolvent. They are typically governed by insolvency laws and regulations, and involve an administrative or judicial authority, the latter is typically the court dealing with insolvencies. Indeed, sanctioning by a court (or an administrative authority) is one of the main features of pre-insolvency proceedings. With pre-insolvency proceedings, the debtor has the ability to initiate the proceedings, as opposed to regular insolvency proceedings that can be initiated by the creditor as well.

Pre-insolvency proceedings can be viewed as collective proceedings under the supervision of a court or an administrative authority, which give a debtor in financial difficulties the opportunity to restructure at a pre-insolvency stage and to avoid the commencement of formal insolvency proceedings in the traditional sense. A restructuring moratorium forms part of pre-insolvency proceedings in certain legal systems. The purpose of the moratorium is to temporarily suspend certain creditors rights, such as the right to enforce security.

49 CDRC Corporate Debt Restructuring Program; https://www.cdrc.my/

A malagasy femal SME pollinates a vanilla flower. Sambava, Madagascar. (Photo by pierivb/iStock)

Pre-insolvency proceedings are available in some countries, for example, Honduras, Vietnam, the Dominican Republic, Chile, Peru, Croatia, Spain, Oman, Lebanon and in 17 member states of the Organization for the Harmonization of Business Law in Africa (the OHADA[50] countries), although it is rarely used in these latter countries.

Specialized Insolvency Proceedings

In-court corporate insolvency procedures are of paramount importance for economic growth and market stability. They allow viable businesses to be successfully preserved or efficiently closed while helping creditors achieve maximum value of their assets. However, insolvency procedures can be complicated, time-consuming, costly and with very rigid structures. A recent insolvency reform trend is the establishment of specialized insolvency proceedings that may reduce the risk of firm disappearance by enabling targeted, expedited and simplified judicial debt restructuring or liquidation procedures. These proceedings, also called simplified proceedings, offer procedural advantages and cost advantages and are typically accessible by smaller enterprises only.

The specialized proceedings mechanisms are balanced, with incentives for both debtors and creditors. Incentives for debtors can include the availability of a moratorium—so that creditors cannot enforce their claims outside of the insolvency process—and allowing the debtor to remain in control of business operations. Incentives for creditors can include flexibility in negotiating a settlement (reorganization plan) and achieving a better return by preserving the debtor's business (which in regular insolvency procedures might have ceased operations).

Countries that have implemented reforms in this area have adopted one of two approaches. The first is to rely on the general insolvency framework, with exceptions, and the second is to adopt a new insolvency regime explicitly tailored to the needs of MSMEs. Japan and Korea opted for specialized SME-based approach. Others (Germany, Argentina and Greece) have adopted exceptions to their general insolvency legislation to assist SMEs. The OHADA economies implemented a unified insolvency regime that introduced a simplified reorganization proceeding for small companies.

Simplified liquidation procedures are common in Argentina, Greece, Japan, the Netherlands, Niger, Poland and Uruguay. Some countries, e.g. Brazil, Cameroon, Canada, Greece, Italy and Lithuania, have simplified in-court reorganization procedures. In OHADA economies, the Uniform Act stipulates that simplified liquidation is available to small companies with no real estate assets, while simplified reorganization is available to all small companies.

4.11. FINANCING AGRICULTURE AND AGRICULTURAL VALUE CHAINS

As is the case in many emerging economies, agriculture is a major area of activity in most African economies, with many of the MSMEs engaged in some form within the agricultural value chain.

> The establishment of sustainable and beneficial access to finance mechanisms have been traditionally very difficult in agriculture because of a high degree of informality and the inherent uncertainty of agriculture in many cases.

Additional focus, with state intervention where needed, is required to expand the access to finance ecosystem.

The agricultural segment is not homogenous, involves different types of participants, have different needs depending on the agricultural activity and is notoriously unpredictable. Overall national coordination to sustainably develop the agricultural sector will, therefore, be advantageous for market participants and should provide clarity of roles. Financial regulators should play a role in the formulation of such a policy.

Traditional credit providers are typically not well-equipped to deal with the diverse needs of the different types of farmers, farming cooperatives and buyers of framing produce. This requires regulatory support to:

- Enable the establishment of different classes of service providers to meet the needs of the agricultural sector (refer Section 4.5);
- Act as a catalyst to develop the capabilities of all credit providers to the agricultural sector to offer appropriate products, e.g. taking into account the revenue patterns of specific crops, and to assess the actual needs of the type and size of farming that is undertaken. In this context, the particular needs of women in the agricultural ecosystem should be determined and incorporated. This development of capabilities is best undertaken in conjunction with another unit, e.g. the Ministry of Agriculture.

50 Benin, Burkina Faso, Cameroon, Central African Republic, Comoros, Congo, Côte d'Ivoire, Chad, Democratic Republic of the Congo, Equatorial Guinea, Gabon, Guinea, Guinea Bissau, Mali, Niger, Senegal, Togo

Agricultural value chains (AVC) present an opportunity to advance the access to finance ecosystem for agriculture. The African Development Bank study[51] *Agricultural Value Chain Financing (AVCF) and Development for Enhanced Export Competitiveness* describes the importance of AVCs in the African context and also the characteristics of AVCs that are pertinent to the financing of these chains.

A typical AVC comprises of producers, traders or aggregators, processing/packaging, and marketing. Each AVC actor has distinct characteristics and financing requirements. Three of these characteristics are particularly important for the discussion of AVC financing:

> **Firstly,** there is the growing integration and concentration of supply chains, giving some chain-linked partners the ability to provide some of the financing towards enhancing the overall health of the supply chain;

> **Secondly,** the value chain raises the creditworthiness of the various participants. Therefore, financial organizations can look beyond the past performance and balance sheets of individual participants for assessing loans and providing financial services. More importantly, such providers of outside-the value chain financing must now consider themselves as part of the team with the chain-linked partners;

> **Thirdly,** despite the value chain, some risks of lending within the chain will remain, as agricultural finance has always involved higher levels of risk and high costs associated with lending than many other business activities. For this reason, the application of risk mitigation measures is even more important in AVC financing.

An innovative example of using the value chain to extend access to finance for the smallholder farmers in an AVC can be found in Tanzania. TechnoServe, a market facilitator helped establish Kilicafe, an organization owned by 9 000 smallholder farmers. This organization works with local and international financial institutions to design financial products that serve those in the value chain. These products range from short-term input credit and pre-financing sales to multi-year loans used by farmers to invest in centralized processing facilities. Credit is guaranteed through a variety of innovative ways, including private guarantee funds, warehouse receipts and forward sales to specialty coffee buyers.

Climate change is expected to make agricultural development in Africa more challenging. Weather patterns are becoming less favorable in many instances, increasing the volatility of crop and livestock yields.

It is expected that southern Africa and the Mediterranean region of North Africa will be especially impacted, although these are current predictions. It is paramount that the ability to deal with these changes and building resilience is developed amongst agricultural MSMEs and farmers, with access to finance being a key enabler.[52]

51 AfDB (2013), Agricultural Value Chain Financing (AVCF) and Development for Enhanced Export Competitiveness;

52 McKinsey (2020), How will African farmers adjust to changing patterns of precipitation?

A worker is sorting through the harvested coffee beans as they dry. Tanzania. (Photo by BruceBlock/iStock)

REGULATORY AND MARKET ISSUE TO CONSIDER IN AFRICA

The preceding sections gave an overview of some of the recent and current developments in the global MSME access to finance ecosystem. The position in Africa has been discussed in some of the sections as well. This section deals with some of the issues in the MSME access to finance ecosystem in Africa that would be important to address, in current and future policy development.

It is worth recalling that the EIB study on banking in Africa highlighted issues of a shortage of bankable projects, a lack of effective collateral, a lack of managerial capacity, informality and a high default rate amongst SMEs. There was also concern expressed that credit guarantee schemes, although very important for MSME access to finance, largely do not meet the requirements of the credit providers. Although policy interventions should not only be based on the concerns of banking groups, there is sufficient evidence to put the following forward, as areas requiring regulatory attention.

Focus on developing the credit infrastructure, particularly effective CGS and efficient and inclusive credit reporting systems. Most countries have the basic building blocks in place, so it is a matter of engaging with stakeholders, determining what is required in the country context and structuring an implementation plan to "close the gaps". In this process the establishment of a credit registry, if it does not exist already, could be helpful. Secured transactions, with a modern movable credit registry, should equally be on the agenda, where these do not exist.

Consider developing, in conjunction with other relevant authorities, a debt review and insolvency regime that addresses the needs of the MSME segment. In particular, this should include guidelines for out-of-court workouts and simplified restructuring and liquidation proceedings.

In many respects, Africa is a leader in digitization, especially in the use of mobile technology. Countries could consider ways in which this could be taken to the next level by enabling DFS to address the needs of MSMEs, consider the sharing of digital data (with due regard to privacy concerns) to enrich and broaden the credit information systems and to consider the use of digital information and technology to assist in regulatory oversight. The business and financial capability of enterprises require on-going upskilling and support. Continued and coordinated support for business development services, taking gender-specific requirements into account, would be helpful in order to address these issues.

Where this has not been done, a path from informality to greater formality for informal MSMEs would be useful. It is probably not advisable to attempt to get all informal enterprises to full formality but structuring the path so that it is an advantageous step for a significant number of MSMEs would be in the interest of both the MSMEs and the broader economy.

Climate change and the effects it will have on many countries and industries are real, with opportunities existing to engage in green markets and to support the move away from fossil fuel and the reliance on those industries. With some exceptions, there appear to be few policy interventions in Africa to link the access to finance ecosystem into these imperatives to deal with the effect of climate change and to support industries (MSMEs) that can take advantage of the opportunities present in the move to greener economies. This requires additional focus, as Africa is expected to be severely affected by climate change; something that is already becoming apparent.

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ANNEXURE: 2020 SMEFWG – QUESTIONNAIRE TO INFORM THE POLICY FRAMEWORK FOR THE MSME FINANCING ECOSYSTEM IN AFRICA

The survey questionnaire that was used in the survey among the AFI SME Finance Working Group members is given below.

INTRODUCTION

Micro, small and medium enterprises (MSMEs) play a major role in most economies, particularly in developing countries. MSMEs constitute approximately 90 percent of businesses and provide more than 50 percent of employment worldwide, contributing 35 percent to global gross domestic product (GDP). MSMEs act as export enablers for developing countries and provide real economic inclusivity for women, with 30 percent of MSMEs run by women. A large number of MSMEs in developing countries often have limited access to finance and face challenges in accessing traditional financial service providers, such as banks. This is especially true for start-up businesses, due to their lack of income and lack of collateral assets.

In view of these constraints faced by MSMEs, AFI is developing a policy framework to enable members to enhance the MSME financing ecosystem in Africa. The framework will guide members to develop MSME financing policies and to identify best practices. These can then be used to provide recommendations on ways of bridging the MSME credit gaps in countries, thereby unlocking the potential of MSMEs to further contribute to growth in the African region.

The objective of this questionnaire is to collect information on the policies and current state of the MSME access to finance landscape in all AFI member institution countries. Policy initiatives that have been particularly successful will be identified, with a view to determine best practice. Information on enabling women and youth-led MSMEs and initiatives to promote green financing will also be collected, given the importance of these segments to ensure inclusivity and sustainability.

This information from this survey will be used to construct the basic policy framework for the MSME financing ecosystem, which will then be enhanced by further engagement with AFI members from the Africa region before publication.

In the context of this survey and the ensuing policy framework, the term MSME is used in the same context as in AFI Guidance Note 36 SME Finance Guideline Note. The term refers to formal enterprises that have been registered by a recognized authority or agency. The definition of these enterprises varies from country to country, so the survey relies on each country's definition, preferably one set out by law or a particular set of regulations.

Some of the questions in the survey refer to informal enterprises as well, but in all cases these are denoted as such. These questions are aimed at getting insight into the size of the informal segment and what member countries are doing to address informality.

The terms used in the questionnaire are consistent with the use of terms in previous AFI publications. Please refer to the attached Annex if necessary.

GENERAL INFORMATION

Name:

Institution:

Email Address:

SECTION 1 - MSME ACCESS TO FINANCE POLICY

Q1.1 Is there a specific approved policy relating to MSME access to finance in your country?

☐ Yes

☐ In the process of drafting / enactment

☐ No

☐ Do not know

Q1.2 Please specify which institution has the primary responsibility for this policy.

Q1.3 Are there multi-institutional structures or working groups involved in the oversight of the policy?

☐ Yes

☐ In the process of setting up

☐ No

☐ Do not know

Q1.4 Is the effect of the policy being monitored in a quantitative manner?

☐ Yes

☐ No

☐ Do not know

Kindly specify which institution is monitoring the effect of the policy in a quantitative manner.

SECTION 2 - LEGAL AND REGULATORY STRUCTURES

The following questions pertain to institutions that are allowed to provide credit to MSMEs.

Q2.1 Which of the following type of institutions are allowed to provide credit to MSMEs? Please select all that are applicable.

☐ Banks

☐ Microfinance Institution

☐ Dedicated Credit Providers

☐ Others. Please specify: _________________

BANKS

The following questions pertain to Banks who are allowed to provide credit to MSMEs.

Q2.2a Kindly indicate the level of capital adequacy (CA), e.g. Basel levels

Q2.2b Is the CA level for MSMEs adjusted to enhance access?

☐ Yes

☐ No

Q2.2c Kindly indicate the total value of MSME credit take-up

MICROFINANCE INSTITUTION

The following questions pertain to Microfinance Institutions who are allowed to provide credit to MSMEs.

Q2.3a Kindly indicate the level of capital adequacy (CA), e.g. Basel levels

Q2.3b Is the CA level for MSMEs adjusted to enhance access?

☐ Yes

☐ No

Q2.3c Kindly indicate the total value of MSME credit take-up

DEDICATED CREDIT PROVIDERS (ONLY CREDIT)

The following questions pertain to Dedicated Credit Providers providing credit to MSMEs

Q2.4a Kindly indicate the level of capital adequacy (CA), e.g. Basel levels

Q2.4b Is the CA level for MSMEs adjusted to enhance access?

☐ Yes

☐ No

Q2.4c Kindly indicate the total value of MSME credit take-up

Others. Please specify:_________

You have selected “Others” in Q2.1 previously. The following questions pertain to the other institutions you have identified, who are allowed to provide credit to MSMEs.

Q2.5a Kindly indicate the level of capital adequacy (CA), e.g. Basel levels

Q2.5b Is the CA level for MSMEs adjusted to enhance access?

☐ Yes

☐ No

Q2.5c Kindly indicate the total value of MSME credit take-up

Q2.6 Are there other forms of access to capital actively used in the country?

☐ Do not know

☐ No

☐ Yes. Please specify: _________________

Q2.6a What is the oversight structure for these enterprises? Briefly describe in the comment box below.

Q2.7 Which of the following tools are used to promote the MSME market with regulated credit providers? Select all that apply.

☐ No specific action - relying on market forces

☐ Persuasion (moral suasion)

☐ Agreed targets that stipulate what proportion of lending or what total take-up will be allocated to the MSME market

☐ Regulations that specify what proportion of lending should be allocated to the MSME market

☐ Others. Please specify:___________

Q2.8 Are there Interest rate caps applicable to finance for MSMEs?

☐ Yes, and it is applicable to all MSME lending

☐ It is only applicable to certain MSME lending cases

☐ No

Q2.9 How is the status of MSME access to finance measured?

☐ Supply-side information from credit providers, e.g. information supplied to the regulator

☐ Demand-side information, e.g. market surveys

☐ Others. Please specify: _________

If MSME access to finance is measured using demand-side information, kindly indicate the intervals of data collection.

Q2.10 How is market conduct regulated (i.e. how is the oversight established) in the credit provider space? Please select all that is applicable.

☐ General act relating to market behavior of service providers

☐ Specific act relating to credit providers

☐ Part of the act relating to service provider types, e.g. Banks Act or similar

☐ Through regulations/guidelines

☐ Others. Please specify. __________________

Q2.11 Is there a formal and independent dispute resolution mechanism in place (e.g. an Ombuds system) for MSMEs?

☐ Yes

☐ In the process of setting up

☐ No

☐ Do not know

Q2.12 Which of the following instruments are allowed in the market? Please select all that are applicable

☐ Leasing

☐ Factoring

☐ Discounting

Q2.12a Kindly specify the value/size of MSME take-up

☐ Leasing

☐ Factoring

☐ Discounting

Q2.13 Is there a specific policy dealing with informal credit providers?

☐ Yes

☐ In the process of drafting / enactment

☐ No

☐ Do not know

Q2.14 What are the major regulatory steps taken to control / mature the informal market? Briefly describe in the comment box below.

Q2.15 What is the estimated MSME take-up of the informal credit, as a percentage of the total regulated MSME credit take-up?

SECTION 3 - FINANCIAL MARKET INFRASTRUCTURE

Q3. Which of the following infrastructural elements are actively being used in the MSME credit market? Please select all that apply.

☐ Credit repository, i.e. the reporting of all agreements in a central place/system

☐ Credit bureaus, i.e. the use of information on the servicing of credit agreements

☐ Credit rating agencies, i.e. the use of the financial and sectoral position of enterprises to determine credit worthiness

☐ The use of alternative data to determine credit worthiness, e.g. the use of digital payment turnover

☐ Credit guarantee schemes, including partial credit guarantee schemes

☐ Export finance guarantees

☐ Movable asset registries and system, i.e. secured transaction framework

☐ Others. Please specify: ____________

Q3.1 Who is the provider of most used credit guarantee scheme?

☐ State

☐ Private

Q3.2 Are there mutual credit guarantee associations?

☐ Yes

☐ No

☐ Do not know

SECTION 4 - ECOSYSTEM ISSUES

Q4.1 Are there Development Finance Institutions (DFIs) that actively participate in the MSME finance space?

☐ Yes

☐ No

☐ Do not know

Briefly describe the role and involvement of DFIs in the MSME Finance space.

Q4.2 Is there direct state monetary intervention in the MSME market?

☐ Yes

☐ No

☐ Do not know

Q4.2a What are the types of major interventions? Briefly describe in the comment box below.

Q4.2b What is the estimated value of state support to the MSME access to finance needs, as a percentage of the total regulated MSME credit take-up?

Q4.3 Is there a business development services (BDS) sector?

☐ Yes

☐ No

☐ Do not know

Q4.3a Is there an institution that coordinates the DBS sector? Kindly indicate the institution(s) who is/are responsible.

Q4.3b Do any of the credit providers or other actors provide BDS services?

☐ Yes

☐ No

☐ Do not know

Q4.3c Are there any international development agencies (e.g. World Bank) involved in the BDS segment?

☐ Yes

☐ No

☐ Do not know

Q4.4 Are there special legal/regulatory guidelines or structures dealing with MSME debt resolution?

☐ Yes

☐ No

☐ Do not know

Q4.4a If yes, which of the following are incorporated? Please select all that apply.

☐ Credit counselling

☐ Agreed mechanisms to determine seniority of debt (who gets paid first)

☐ Agreed mechanisms to determine loss to debtors (haircuts)

☐ Refinancing programs

☐ Direct debt relief, e.g. subsidized interest rates

☐ Others. Please specify:_________________

Q4.5a What approximate percentage of MSMEs are informal (not registered as businesses)?

☐ 0% to 10%

☐ 11% to 20%

☐ 21% to 30%

☐ 31% to 50%

☐ 41% to 50%

☐ 51% to 60%

☐ 61% to 70%

☐ 71% to 80%

☐ 81% to 90%

☐ 91% to 100%

Q4.5b What approximate percentage of the total market value (in terms of total turnover) do the informal businesses represent?

☐ 0% to 10%

☐ 11% to 20%

☐ 21% to 30%

☐ 31% to 50%

☐ 41% to 50%

☐ 51% to 60%

☐ 61% to 70%

☐ 71% to 80%

☐ 81% to 90%

☐ 91% to 100%

Q4.6 Is there a differential between the cost of credit for MSMEs and larger corporates?

☐ No, there is no differential

☐ Yes. Kindly stipulate the average differential between MSMEs and larger corporations

SECTION 5 - FOCUS AREAS

Women- and youth-led MSMEs and green finance are key segments in the MSME space. In the following comment box, kindly summarize the policy and regulatory measures that have been taken in these segments.

5.1a Women

Q5.1b Youth

Q5.1c Green Finance

The agricultural sector is typically a major sector in many developing countries, given the importance to employment, food security and exporting. Many countries focus on enabling the different elements of the value chain, to enable the sector to reach its potential.

Q5.2a Are there specific agri-finance policies?

☐ Yes

☐ No

☐ Do not know

Q5.2b What are the objective of these policies? Briefly describe in the comment box below.

Q5.2c Are these initiatives to improve access to finance for specific elements in the agri-value chain?

☐ Yes

☐ No

Q5.2d What other services are provided (e.g. digitization of export process) to stimulate the agri-sector, in conjunction with access to finance? Briefly describe in the comment box below.

SECTION 6 - SUCCESSES AND MAJOR FOCUS AREAS

Q6.1 Interventions or regulatory structures that have been particularly successful in the MSME space in the last few years.

Kindly summarize any successes of the interventions or regulatory structures. Reference to published materials would be very useful (if available).

Q6.2 Apart from dealing with the effects of COVID-19, what are the most important areas that you will focus on to improve MSME access to and use of finance in the next 12 months and why? Briefly describe in the comment box below.

Q6.3 In terms of the response to the COVID-19 pandemic, are there any specific regulatory responses that focus on the MSME space?

Kindly narrate the specific regulatory response. References would be very useful (if available).

ANNEX - GLOSSARY AND EXPLANATORY NOTES

CREDIT GUARANTEE SCHEME

A credit guarantee scheme (CGS) is an arrangement where a third party, often but not necessarily the state, provides partial credit risk cover to lenders. This arrangement involves the third-party receiving a fee to provide this risk mitigation service, with pre-defined conditions as to how much will be covered in case of default by the lender, under what circumstances the cover will be provided and what the responsibilities of the lender are.

A popular form of private CGS is a mutual guarantee association. MSMEs are the members of such a scheme, each member deposits money into a fund that in effect guarantees loans of members at financial institutions.

BUSINESS DEVELOPMENT SERVICES (BDS)

The International Finance Corporation IFC defines Business development services defined as those non-financial services and products offered to entrepreneurs at various stages of their business needs to improve business skills and equip entrepreneurs to run their businesses more effectively. These services are primarily aimed at skills transfer or business advice and are sometimes offered in conjunction with credit and other financial services. Business development services can act as an enhancer of access to finance. These services include financial literacy and capability training, basic business skills (e.g. bookkeeping and accounting), access to market skills training and general business planning and expansion.

DEVELOPMENT FINANCE INSTITUTIONS (DFIS)

DFIs typically provide credit and a wide range of capacity-building programs to households, SMEs, and even larger private corporations, whose financial needs are not sufficiently served by private banks or local capital markets. Historically, DFIs have been created by governments around the world to promote economic growth and support social development. In doing so, they seek to promote strategic sectors of the economy, such as agriculture, international trade, housing, tourism, infrastructure, and green industries, among other sectors.

CAPITAL ADEQUACY REQUIREMENTS

The capital adequacy requirement (also known as regulatory capital or just capital requirement) is the amount of capital a bank or other financial institution has to have, as required by its financial regulator. This is usually expressed as a ratio of equity (capital) as a percentage of risk-weighted assets. The purpose is to establish that banks have enough capital on reserve to handle a certain amount of losses, before being at risk for becoming insolvent.

Basel norms for capital adequacy (Basel I, II and II) are international guidelines published by the Basel Committee on Banking Supervision, part of the Bank for International Settlement. These norms are an effort to coordinate banking regulations globally, with the goal of strengthening the international banking system.

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