



WORLD BANK GROUP



International  
Finance Corporation  
WORLD BANK GROUP



## Financing MSMEs in Emerging Markets

Jinchang Lai

Principal Operations Officer, and Lead for Financial Infrastructure,  
East Asia & Pacific, Finance & Markets, World Bank Group

Asia-Pacific Financial Forum, Shenzhen, August 1, 2016

## The Many Faces of Finance

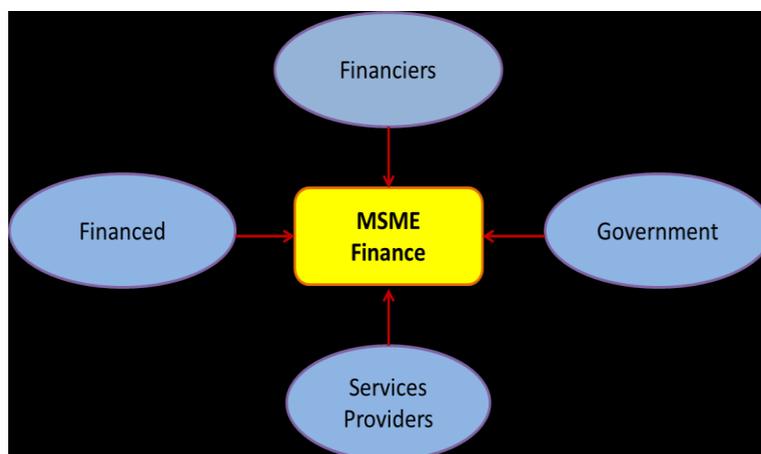
- MSME finance topic is about external finance
- Where can a MSME obtain finance from outside the business? Potential sources:
  - ✓ Friends and relatives
  - ✓ Informal lenders
  - ✓ Trade creditors
  - ✓ Equity investors (*angels, equity investment institutions, government funds, etc.*)
  - ✓ Financial leasing companies
  - ✓ Debt financiers: **banks**, non-deposit-taking lenders (NDTL), non-recurrent buyers of debt, mutual finance schemes, etc.
  - ✓ Capital market investors via issuance of debt instruments
  - ✓ Government support programs via loans, grants, risk sharing, or interest subsidies, etc.
  - ✓ Risk financiers (*insurers, mutual insurance schemes, government risk compensation, etc.*)
  - ✓ Crowd-funders

## How Does a Good Market Look Like?

- The objective of an economy should be to develop an effective, efficient and inclusive **market** for MSME finance, with the following main characteristics:
  - ✓ The demand side has convenient access to a diversified range of affordable finance timely
  - ✓ The supply side can underwrite efficiently and able to structure incentives for the financed, with manageable transaction cost
  - ✓ Various finance players are allowed to operate based on commercial principles with clear and relatively low entry requirements, e.g., NDTLs
  - ✓ Different forms of finance compete fairly on an equal footing following *inter alia* the market "price for risk" signals
  - ✓ The demand side has adequate knowledge in managing financing relationships, with necessary protection and redress mechanisms in place; and financiers and the financed can exit in an orderly manner when needed



## Four Main Players in a Market

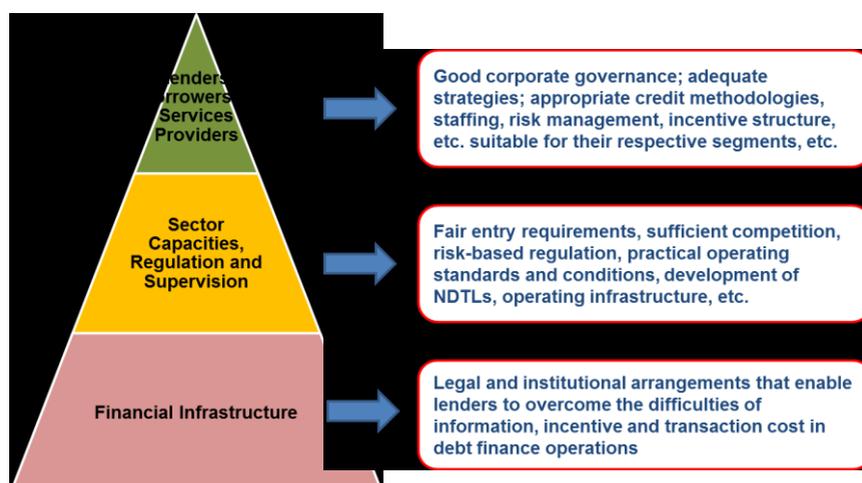


## Key Elements in Market Development

- Each MSME finance sub-market has its own requirements to make the market "tick"
- Using **lending industry (credit market) as an example**, three layers of different requirements (see graph)
- In emerging markets, reforms in this space have generally not been easy as most of the contents involve government agencies which often do not understand (e.g., *Ministry of Justice*), may not be committed, or face resource and capacity constraints
- The job of APEC-ABAC in this area should be to work on the 1st and 2<sup>nd</sup> layers
- What does it mean? See a simplified case



## Foundations for a Credit Market

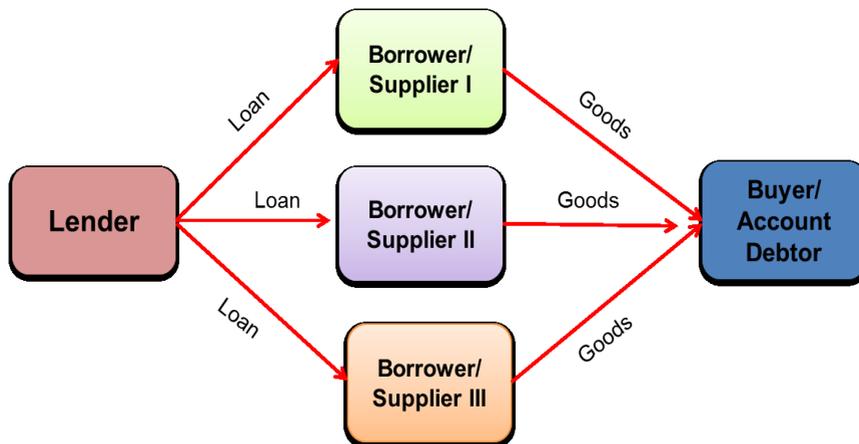


## Case: What Infrastructure is Needed for AR Finance?

- A simplified case of accounts receivable (AR) lending:
  - ✓ Buyer A is a medium-sized enterprise in APEC Economy Charlie, which source from three smaller size suppliers; the usual payment term is three months upon the satisfactory receipt of goods
  - ✓ Suppliers I, II and III all need to borrow; otherwise, they will not have funds to start the next cycle of operations
  - ✓ They apply for loans from Bank Beta to be secured by their changing receivables due from Buyer A (*the account debtor, or "customer"*)
  - ✓ Will Bank Beta lend to these three suppliers (*the "client"*)?
  - ✓ Supposed all three are bankable clients, why and why not?
- This is an enabling environment matter, i.e. the 1<sup>st</sup> and 2<sup>nd</sup> layer issues



## Case: What Infrastructure is Needed for AR Finance?



## Case: What Infrastructure is Needed for AR Finance?

- Lenders will have to consider:
  - ✓ Can ARs be taken as collateral in Economy Charlie?
  - ✓ How will lender Beta get information on the "customer"?
  - ✓ Will lender Beta be able to perfect its security interest on ARs and establish priority against third parties?
  - ✓ Is lender Beta empowered to collect (enforce) directly from customer (account debtor) in case of need?
  - ✓ In the event of client bankruptcy, what will be the position of lender Beta vis-a-vis other creditors? In the event of customer bankruptcy, what will be the position of lender Beta?
  - ✓ And, .... so on
- These concern **secured transactions** system, **credit reporting** system and **insolvency** framework
- Without answers to most of these questions, do not expect that you will have good MSME finance in your economy



## Role of APEC-ABAC

- Annex I reflects the state of play for SME finance and Annex II for micro business finance in selected APEC economies
- Access to finance is among the top business obstacles for the developing APEC economies (*Enterprise Surveys, World Bank Group*)
- The APEC **Financial Infrastructure Development Network (FIDN)** has been working on the 1<sup>st</sup> and 2<sup>nd</sup> layer reforms, in collaboration with **IFC**, industry associations (*e.g., FCI, Thai Bankers Association, Vietnam Banks Association*), private sector supporters, and government agencies (*e.g., Philippines DOF, China PBOC*), etc.
- Measurable progresses have been made in some economies (*e.g., Vietnam, China, Philippines*)



## Role of APEC-ABAC

- Continuous efforts in MSME finance will be required in the foreseeable future; and, going forward, more advocacies to and pressures on governments will be useful and, also, greater efforts are required in insolvency reforms and the development of a professional debt collection industry
- A good way to think about all these in one term: ***how could a market be created? how can a market grow? how will a market function better?***
- With such a broader market perspective, public sector reforms, industry collective efforts, and private sector solutions can all fit together
- This should be the very essence of ***"public-private collaboration to develop APEC Financial Markets"***



Thank You !

The views and judgments  
herein should not be  
management and  
not rendering any  
who relies on this



## Annex I: Access to Finance by Firms in Selected APEC Economies

Economy	% of firms with a bank loan/line of credit	% of investments financed by banks	% of investments financed by supplier credit	% of investments financed by equity/stock	% of firms identifying access to finance as a major constraint
China	25.3	4.5	1.9	3.2	2.9
Indonesia	27.4	19.3	5.3	1.4	16.5
Korea	N.A	20.0	0.1	8.1	12.1
Malaysia	31.0	15.6	5.2	9.5	12.1
Mexico	32.0	8.8	15.6	8.5	29.6
Peru	66.8	34.7	10.9	5.4	8.5
PNG	45.7	26.5	0.0	0.0	3.2
Philippines	29.9	10.0	2.6	5.7	10.7
Thailand	15.5	9.9	3.8	0.8	2.4
Vietnam	41.1	16.4	3.5	8.5	10.9
<b>East Asia &amp; Pacific</b>	<b>27.9</b>	<b>10.1</b>	<b>3.4</b>	<b>3.5</b>	<b>12.2</b>
<b>High Income OECD</b>	<b>50.7</b>	<b>20.3</b>	<b>4.2</b>	<b>2.4</b>	<b>11.6</b>

Source: Compiled from Enterprise Surveys data, World Bank Group.  
Note: The above does not show % of finance available from non-bank lenders.



## Annex II: Access to Finance by Adults in Selected APEC Economies

Economy	Borrowed Any money	Borrowed from a financial institution	Borrowed from family/friends	Borrowed from a private informal lender	Borrowed for a farm or business
Australia	43.2	23.4	16.9	0.8	3.1
China	36.3	9.6	25.1	1.1	7.0
Indonesia	56.6	13.1	41.5	2.9	11.7
Japan	23.1	7.9	6.0	0.3	1.1
Korea	39.4	18.2	17.1	0.7	4.6
Malaysia	56.1	19.5	39.0	0.8	6.1
Mexico	50.8	10.4	26.0	9.9	9.5
Peru	27.5	11.2	10.4	2.3	6.8
Philippines	69.7	11.8	48.7	13.5	13.6
Thailand	50.3	15.4	31.1	9.1	12.8
Vietnam	46.8	18.4	29.9	1.8	7.1
US	51.4	23.3	19.8	1.4	2.5
<b>High Income OECD</b>	<b>39.8</b>	<b>18.4</b>	<b>14.9</b>	<b>0.9</b>	<b>2.6</b>

Source: Compiled from Global Findex, World Bank Group.

