ACCOUNTANTS FOR BUSINESS

Innovations in access to finance for SMEs

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This paper reviews a broad range of innovations in business financing and highlights examples of good practice in developed and emerging economies.

The paper is a contribution by the ACCA Global Forum for SMEs to the current debate about improving SMEs' access to finance around the world. The Forum is grateful for the assistance and insights of Andy Davis, associate editor and investment columnist at Prospect magazine.

ABOUT ACCA'S GLOBAL FORUMS

To further its work, ACCA developed an innovative programme of global forums which brings together respected thinkers from the wider profession and academia around the world.

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About the ACCA Global Forum for SMEs
The ACCA Global Forum for SMEs provides a unique platform for promoting the role of SMEs in the global economy. Representing over 15 countries and a wide range of professional backgrounds – from finance institutions, academics and professional advisers to entrepreneurs themselves – the Forum represents the sector's needs at a global level and facilitates the sharing of best practice.

For more information contact
Emmanouil Schizas
Senior Economic Analyst, ACCA
emmanouil.schizas@accaglobal.com

1. Introduction

In the years since the 2007–8 financial crisis, the issue of access to finance for small and medium-sized enterprises (SMEs) has taken on a new prominence, having been formally recognised as an issue of pressing importance at the G20 summit in Pittsburgh in September 2009.[1]

Of course, one of the key reasons for the increased attention that this subject now receives is the well-documented problems of the banking system in many parts of the world following the 'credit crunch' of 2008–9. This dimension of the financial crisis – and the policy and regulatory measures subsequently put in place – has had a notable effect on the ability and willingness of the conventional banking system to fund SMEs in some parts of the world, and has therefore contributed to the emergence of innovative alternative forms of SME finance. In other regions, a general lack of development in commercial banking and other sorts of financial infrastructure has been a more pressing issue.

Even so, other factors beyond the crisis of the developed world's banking system have also contributed to the initiatives that this paper will discuss, notably technological developments and increasing access to online services; electronic data from a growing variety of sources; and innovative financial instruments and structures that together help to create new ways for savers and borrowers, investors and entrepreneurs, to meet and do business.

This paper provides examples of a range of important innovations in SME finance and discusses some of the lessons we can draw from them. Although the definition of an SME varies widely across different markets, for the purposes of this report a small enterprise is considered to be a company with 50 or fewer workers and a medium-sized enterprise is any business with 51 to 249 workers. In common with other definitions of SMEs, this excludes companies in extractive industries, utilities and financial services.

1. 'Leaders' Statement', *The Pittsburgh Summit,* G20, September 2009.

2. The range of innovations in SME finance

Although by no means exhaustive, this section offers an overview of some of the most significant innovations and developments in access to finance for SMEs that have emerged in recent years, under four headings:

- New lending and equity funding initiatives
- Innovative financing structures and instruments
- New proxies for credit information
- Legal and regulatory infrastructure.

NEW LENDING AND EQUITY FUNDING INITIATIVES

The most obvious way to increase access to finance for SMEs is for more new organisations within or outside the banking system to start lending to them, and in many parts of the world this has happened.

In June 2010 the giant Chinese e-commerce platform Alibaba launched a micro-credit company, Alipay Financial, based in the city of Hangzhou, to offer loans from its own cash resources to existing SME users of its e-commerce services. Initially it offered 30-day working capital advances of up to RMB500,000 ($82,000) to fund sales of goods via its Taobao online marketplace. Subsequently, the business expanded geographically and began offering a wider range of loan products. Larger loans could be secured by groups of three SMEs standing as guarantors for each other. Reports suggest that the Alipay Financial loans business later began originating loans among users of Taobao on behalf of China Construction Bank and the Industrial and Commercial Bank (ICBC) of China, among other mainstream financial institutions, to expand its lending capacity. Writing in *Global Times* in February this year, Lu Zhengwai, chief economist at ICBC, said that from its establishment through to the first half of 2012, Alipay Financial had made loans worth some RMB13bn ($2.09bn).

In the US and Europe, where e-commerce operations such as eBay and Amazon dominate, similar but smaller networks of alternative finance have begun to appear. In September 2012, Reuters reported that Amazon had begun offering funding to some of its largest sellers under a programme called Amazon Lending. Although Amazon has released no official details of the programme publicly, industry observers told Reuters that Amazon was offering advances of up to $800,000 to some merchants and charging interest rates that ranged from 1% to 13% a year.

Independent operators are also starting to offer finance to Amazon and eBay sellers. The largest such company, Kabbage, which was founded in 2009 and is based in the US city of Atlanta, obtains borrowers' consent to access real-time data from their e-commerce seller's accounts, PayPal accounts, UPS shipping accounts, as well as from a variety of SME accounting software packages such as QuickBooks, Stripe and Xero. Kabbage offers advances of between $500 and $50,000 at interest rates of between 2% and 7% for a 30-day period. For a six-month advance rates range from 10%–18%. In August 2013 the company announced it had made 80,000 advances in the US, four times more than its nearest competitor. During 2013 it also launched in the UK.

In many parts of Africa, meanwhile, high take-up of mobile phones has enabled the growth of mobile payment services that allow users to send and receive small sums via their phones. The most well-known such service is M-Pesa in East Africa, which now has more than 20 million users. Other similar services are also spreading fast, including Ecocash and Textacash in Southern Africa. More recently, services such as M-shwari have appeared, which add a loan facility to the basic mobile payments service. M-shwari is a joint venture between mobile provider Safaricom and a Kenyan bank, Commercial Bank of Africa (CBA). The service enables users to borrow sums ranging from the equivalent of about $1 up to about $235, although the largest loan advanced to date is less than $100.

The attraction of this service has resulted in a very rapid uptake of bank accounts at CBA, with 2.15 million bank accounts opened in the three months to September 2013, transforming it over that period into the second largest retail bank in Kenya.[2] Over the same period, the overall number of bank accounts in Kenya grew 11.3% to a record 21.5 million.[3] Kenya Commercial Bank, the country's largest by asset value, has introduced M-benki, a similar service to M-shwari.

In the UK and US, particularly, new sources of equity and debt funding for SMEs are opening up via the crowdfunding and peer-to-peer (p2p) movement. Equity crowdfunding platforms wherein investors buy an actual stake in the recipient's business are only one of the crowdfunding options, coexisting with a number of pre-selling, donation-, or rewards-based platforms. The leading US equity platform, Kickstarter, raised $480 million in 2013, while UK-based Crowdcube and Seedrs raised £12.2 million and £1.4 million worth of investment respectively. The platforms

2. *Business Daily*, 27 October, 2013.

3. ibid.

have combined rapid growth with geographical expansion as well as product innovation: Crowdcube, for example, has recently launched its own venture fund, while Seedrs now also funds non-UK companies.

A common feature of such platforms is the ability to turn investor pitches into fundraising campaigns through multimedia content and social media integration. Platforms rely on this 'campaign element' and are built to enable two-way investor communications and 'crowd-based due diligence' (see explanation below). Finally, equity platforms are now typically eligible for the same tax incentives and public subsidies as traditional early-stage investment.

With p2p lending platforms, the key innovation has been the creation of a Web-based marketplace in which individuals or institutions with capital to invest are able to make contact with SMEs that want to borrow, and agree to advance funds to them on standardised terms set out by the platform that facilitates the transaction.

Although they all operate in slightly different ways, lending platforms are less diverse than their equity counterparts and have a number of central features in common that are worth setting out.

Platforms seek to assemble loans from groups of individual lenders, ranging from 30-day working capital advances up to five-year term loans and asset-finance deals. All loans are therefore 'fractionalised' between multiple lenders.

They frequently operate auction-based systems that force lenders to compete to provide funding, either by offering a 'bidding down' in a reverse or Dutch auction, or by racing to offer funding at a fixed rate before the target amount is reached and the loan request closes.

They facilitate lending in a semi-public context in which key documents and financial details that would normally remain private are published to potential lenders to support the loan request.

They enable potential lenders to question borrowers during the auction process. Answers to these questions are usually published for all potential lenders to see – hence the term 'crowd-based due diligence'.

They frequently operate secondary markets in which existing lenders who wish to take back their money can sell their share of any loan to other investors. These markets have so far proved liquid, with loan parts changing hands rapidly and often at a premium.

They tend to offer more flexible terms than equivalent bank lending, for example on security and early repayment.

Their fee structures make it economical for small investors to build diversified portfolios.

So far this movement remains small, having facilitated about £390 million of loans and invoice discounting transactions to SMEs in the UK by mid-January 2014 via platforms such as Funding Circle, ThinCats, MarketInvoice, Platform Black, Funding Knight, Assetz, Lendinvest and Relendex, among others. The majority of these loans were advanced during 2013 and the leading platforms report that their lending books are doubling in size every six to eight months. In Continental Europe, SME crowdfunding platforms have also started operating, such as Debitos, a German platform that allows companies to auction receivables to raise working capital, and Fakturaborsen, a similar platform in Sweden.

It seems possible that direct lending via these non-bank forms of mediation is poised to become a significant and meaningful alternative source of funding for SMEs in a growing number of countries in the years ahead.

International aid and community organisations

Alongside these more novel examples, development organisations and community-based initiatives continue to play a vital role in promoting access to finance, often via micro-lending institutions that accept borrowers based on the viability of projects rather than the availability of suitable collateral. In Zimbabwe, for example, micro-finance institutions backed by international funds, training and technical assistance are seen as a vital source of funding for marginalised borrowers who struggle to access funds from traditional banks. In Kenya, meanwhile, there has been growing uptake of savings and credit cooperatives (SACCOs) whose members lend to each other in order to access an alternative to expensive bank credit. Kenya has by far the largest number of SACCO members in Africa, with 18% of adult Kenyans using them. A report by their regulator, the SACCO Societies Regulatory Authority, says that total lending increased at an annualised rate of 61% in the first eight months of 2013 compared with the previous year.

INNOVATIVE FINANCING STRUCTURES AND INSTRUMENTS

Probably the most debated development in this area is supply chain finance (SCF). This involves a relationship between a finance provider and a large company under which the financier agrees to advance short-term funding against invoices issued by the large company's suppliers once these have been formally approved for payment. This arrangement provides the following advantages to supplier, customer and financier.

The supplier is able to raise finance against 'approved payables', which in turn are backed by the credit rating of the company at the head of the supply chain – therefore enabling smaller companies to benefit from a cheaper cost of working capital thanks to the superior creditworthiness of their large customers.

The customer is able to optimise its own working capital position by extending its payment terms to 90 days and beyond without putting undue financial pressure on its SME supplier base.

The finance provider is able to manage its credit risk effectively since credit information on large corporates, particularly those based in developed markets, is readily available. This is particularly important when advancing finance to SME suppliers based in developing markets where credit information is scarce or non-existent.

In spite of these apparent advantages, SCF remains a very small part of the overall receivables finance market, accounting for less than 4% of global market value (based on figures from the International Factors Group covering 65 countries) but about 12% by value on average in those countries where it is practised at all – although this average is likely to be heavily influenced by a few larger markets such as Spain, where it is widely used.

Nonetheless, SCF is now a rapidly growing part of the trade finance product range offered by large, international banks. According to recent research by Demica, a UK-based provider of the electronic invoicing systems that connect the large corporate customers and the suppliers that join its SCF programme, leading banks are reporting current growth rates of 30%–40% per year in SCF volumes. These rates are expected to moderate to 20%–30% a year by 2015 and 10% a year by 2020. Eastern Europe, India and China are reported to be the regions with the greatest growth potential for SCF providers.

A number of large, international companies are now operating SCF programmes with their major suppliers but multilateral and state-backed institutions have made the most concerted efforts to harness the potential of discounting receivables to improve cashflow for SME suppliers in developing markets . These programmes tend to offer 'reverse factoring', by which SMEs that supply large companies can raise short-term funding against invoices that have already been approved for payment by their larger customers.

Probably the best example of reverse factoring's potential to increase access to working capital for SMEs in the developing world is the Cadenas Productivas programme in Mexico. This project, backed by the state-run development bank Nacional Financiera (Nafin), created an online marketplace in which SMEs that are accredited suppliers to 'Big Buyers' – large, established companies – can offer their invoices for sale to a panel of financial buyers in return for immediate access to working capital. Nafin's aim in launching Cadenas Productivas was to greatly enhance access to finance for the country's SMEs, 80% of which received no bank credit, according to a 2004 study by Banco de Mexico. Between its establishment in September 2001 and mid-2009, the most recent date for which information is readily available, Nafin's SCF programme had attracted 455 'big buyers' and more than 80,000 of their suppliers, and had advanced more than $60bn to Mexican SMEs. About 20 Mexican banks and financial institutions lend via the Nafin platform.

A more global version of Nafin's Cadenas Productivas is provided by the International Finance Corporation (IFC – a member of the World Bank Group) through its Global Trade Supplier Finance (GTSF) programme, a $500 million initiative that started in 2010 and is specifically designed to advance working capital finance to SME suppliers based in the developing world that are selling to end-customers in developed markets. As above, the intention is to enable small and poorly collateralised borrowers in the emerging markets to access finance at prices that reflect the credit risk of their much larger end-customers.

In the research it undertook before setting up the GTSF programme, the IFC found that there were about $400bn-worth a year of exports from emerging markets to corporate customers in the US, Western Europe and Japan that could potentially be financeable via SCF, yet only about 5% of such exports were actually financed through SCF. This indicates the huge growth potential for this form of finance.

Reasons for the very low penetration of SCF in emerging markets range from the lack of financial products of this sort offered by local commercial banks to the lack of experience among global banks of working in this way in emerging markets.

At least two private sector companies are now operating that seek to pursue the same business as the IFC's cross-border SCF programme. Aztec Exchange is an online platform launched in May 2013 to enable SMEs in the developing world and credit-constrained developed markets, particularly in Europe, to sell invoices that they have issued to large overseas buyers and those buyers' local subsidiaries and that have been approved for payment. Aztec is based in Dublin, where it has about 30 staff, and currently operates in 38 countries, including 6 in Africa, 11 each in Asia and Europe and 10 in the Americas. The buyers on its platform are mainly hedge funds based in London, New York and Singapore. Invoices sold via Aztec Exchange can be outstanding for anything from 30 to 180 days, although in practice most fall into the 60–90 day range. Discount rates on the platform have tended to range from 0.9% to 2% per 30-day period, with advances as high as 85% of the invoice value.

Advance Global Capital (AGC) differs from Aztec in that it is both an investor in trade receivables and the operator of an electronic platform on which these receivables can be offered for sale. AGC began operating in Kosovo in September 2013 in partnership with two large supermarket groups and is offering SCF to a pilot group of their farm and food processing suppliers, with plans to expand the project significantly as more suppliers are taken through the education and onboarding process in coming months. AGC is also operating in Macedonia and will shortly launch in Peru in partnership with a local factoring company.

The Bank Payment Obligation (BPO)

In international trade, there has been a steady move away from Letters of Credit (LoCs) between issuing and confirming banks as the preferred method of financing cross-border transactions, and towards Open Account trading. It is estimated that about 85% of world trade is now undertaken on Open Account terms. Generally speaking, companies in developed markets are less willing to arrange LoCs and commercial banks in emerging markets are normally reluctant to extend credit to local exporters in the absence of an LoC. This has made cross-border trade more difficult to finance via traditional trade finance instruments in some cases and has led to a rapid increase in cross-border factoring volumes.

In the second quarter of 2013, however, the Society for Worldwide Interbank Financial Telecommunication (Swift) and the International Chamber of Commerce issued new technological and legal standards for the BPO, which they hope will underpin greater adoption of SCF. Swift defines the BPO as 'an irrevocable undertaking given on the part of one bank to pay another bank provided that a number of predetermined conditions have been satisfied through the electronic matching of data within the Swift Trade Services Utility, a data matching and workflow engine which enables banks to establish a common view of supply chain transaction data and to monitor events from inception to completion'.

This enables the banks serving both parties in a cross-border transaction to use a standard framework for confirming export transactions and supplying finance. In effect, use of the BPO enables banks in the markets where suppliers (often SMEs) are based to 'onboard' those companies so that they can be included in SCF programmes put in place by large corporates and their banks located elsewhere in the world. Previously, developed-world banks had often struggled to engage with supplier companies based in emerging markets, in part owing to the difficulty of carrying out adequate 'Know Your Customer' procedures, as required by their domestic banking regulators. BPOs effectively enable local banks to onboard these suppliers and so make cross-border SCF transactions easier to undertake for banks.

Other advantages of the BPO, according to Swift, are that the two banks involved in any transaction are exposed to each other, rather than to each other's customers, that the companies involved in a transaction are each able to work with a bank they know, and that putting in place the BPO allows finance to be advanced to the supplier much earlier in the life of a transaction, from the time the order is placed rather than when an invoice is eventually approved for payment.

Figures from Swift show that so far seven, mainly Asian, banking groups have gone live since the BPO payment method was launched in April 2013, although some were already live under the previous BPO rules. According to Andre Casterman, global head of Corporate and Supply Chain Markets at Swift, the banks that operate BPO are supporting 25 live corporate clients, including SMEs in China. 'We see approximately 70 new BPO transactions – usually one per purchase order – per month in total,' he says. 'These are very early days and it takes time to materialise given the heavy work on the legal side, for example corporates re-negotiating trade flows to move from Letters of Credit and Open Account to BPOs, and banks setting up new services. But we expect those figures to double in 2014 as we witness global and regional banks implementing the BPO.'

NEW PROXIES FOR CREDIT INFORMATION

Alibaba in China has overcome the lack of reliable third-party credit information on SME borrowers by relying on the transaction and payment data that Alipay, its proprietary payments system, collects. This has allowed it to build a predictive model for assessing credit risk among its pool of potential borrowers. Similar strategies are being pursued in the US and elsewhere by lenders that harvest user data from sources such as eBay, Amazon, PayPal and UPS in order to build similarly predictive models.

In addition, other approaches to using alternative data sources are beginning to appear. For example, in the US, debt crowdfunding platforms assess credit risk by using a range of alternative measures, such as buyer ratings on trading platforms such as eBay or Amazon, shipping information collected from DHL and utility consumption (to verify whether a business is operating as claimed). They also check the business owners' online social reputation via sources such as their Klout Score, which assesses an individual's online presence, number of social networking connections and how close those connections are geographically. This helps to indicate whether a business that seeks to raise money via a crowdfunding site will be successful in fundraising from its own friends and family networks. In addition, platform owners say that the more tightknit a business's network is in geographical terms the greater will be the social pressure on borrowers to repay their loans.

The online merchant lender Kabbage (see 'New lending and equity funding initiatives' above) also has a partnership with Yelp, an online customer reviews service, which allows it to incorporate into its underwriting process data on how positive or negative a business's consumer feedback is.

As online information sources multiply and the cost of mining and manipulating this data continues to fall, we can expect to see many more sources of data added to credit underwriting processes as well as much greater use of 'real time' data rather than historic credit information that is sometimes overtaken by events.

LEGAL AND REGULATORY INFRASTRUCTURE

Frequently, the really effective innovations in a particular sector are not new ideas. Nonetheless, their introduction can provide the legal and/or regulatory certainty necessary to underpin trust on both sides of a transaction. It is the absence of trust that tends to make the costs of doing business prohibitive. In the absence of trust, finance providers rely disproportionately on collateral; small businesses can rarely provide collateral and when they can its quality can easily come into question. The creation of moveable asset registries is a good example of policies to address this failure and is being pursued in a number of countries: a recent review by the World Bank found that such policies tend to improve SME access to bank loans, especially among smaller businesses.[4]

Perhaps the most ambitious case to date has been the establishment of the rules and infrastructure necessary to set up the National Asset Registries in China. In October 2007, the People's Bank of China (PBoC) launched its online asset registry for accounts receivable, enabling short-term loans secured against specific receivables (known as moveable assets) to be registered centrally and publicly. This greatly reduces the risk of fraud for the lender and therefore dramatically increases trust among lenders that their money is properly secured and that their interest in the assets that are backing their loans can be enforced if needs be.

The results of this initiative have been spectacular. According to the August 2013 IFC/Global Partnership for Financial Iinclusion (GPFI) progress report, the number of SMEs obtaining finance from China's 'Big Five Banks' went from a compound annual growth rate (CAGR) of –1% during 2006–8 to a CAGR of 11% in 2008–10. The shift among China's 'Large Commercial Banks' was even more marked, from a CAGR of 17% in 2006–8 to a CAGR of 44% in 2008–10. As regards the change in the value of lending, borrowing by SME clients of the Big Five grew at 2% a year in 2006–8 and 25% a year in 2008–10, while borrowing by SME clients of the Large Commercial Banks grew at 20% a year in 2006 –8 and 45% a year in 2008–10.

This process received a further significant boost in July 2009 when the PBoC opened its asset registry for leases, enabling a functioning market in fixed asset finance to develop, where the lender's title to the asset can be centrally registered and made properly enforceable in law.

4. Love, I., Martinez Peria, M. S. and Sing, S., *Collateral Registries for Movable Assets – Does their Introduction Spur Firms' Access to Bank Finance?*, World Bank Policy Research Working Paper no. 6477, 2013.

3 The major trends driving innovation

NEW PAYMENT SYSTEMS CREATE NEW SOURCES OF FINANCIAL INFORMATION

Many of the most striking new ways of channelling finance to SMEs are emerging as a result of the growth of new electronic payments systems. This is true of Alibaba's lending operations in China, where its dominance of e-commerce in China enables its payment system, Alipay, to generate huge volumes of transaction and payment data from the companies and individuals that use it. By mining this proprietary data, Alipay Financial has a means of assessing the risk and creditworthiness of would-be borrowers and therefore of pricing its loans to them. This in turn allows it to overcome one of the most important barriers that prevent SMEs gaining greater access to finance – the lack of reliable credit information on potential SME borrowers in many parts of the world. The same applies to the mobile payments systems that are expanding rapidly in Africa.

GROWING AGGREGATION OF ONLINE DATA SOURCES

Alongside this growth in data from electronic payments systems comes the growing use of aggregated data from multiple online sources, as described in the preceding section. This allows technology-based intermediaries to draw upon a wide range of online sources in order to build up richer information on potential borrowers, frequently by using real-time information rather than historical data. The vast increase in data that becomes available when more of an SME's activity moves online provides a major opportunity for activities such as financial intermediation, which depend on access to sufficient data in order to operate.

GROWING MARKET ACCEPTANCE OF ONLINE MEDIATION

The role of the internet as a sales channel for financial products is already well established in many markets. For example, in the UK direct online sales of car insurance accounted for 67% of the market in 2012, up from 58% in 2008, while the share of traditional brokers fell by the same amount over that period. This trend is also gradually extending to the main SME funding markets, particularly thanks to the growth of p2p and crowdfunding platforms. In particular, smaller-value loans and working-capital facilities are much more likely to be profitable for the providers if mediated online, since the overheads associated with a large branch network make small-scale lending to SMEs barely profitable for many banks unless the borrower can also be sold other products such as insurance or interest rate swaps.

Electronic platforms have also proved enormously beneficial in other areas, for example, the Cadenas Productivas SCF programme operated by Nafin in Mexico. Here, according to a World Bank research report: 'Over 98% of all services are provided electronically, which reduces time and labour costs. The electronic platform also allows all commercial banks to participate in the programme, which gives national reach via the internet to regional banks.' Technology can allow great economies of scale – Nafin grew from a 2% share of the Mexican factoring market in 2001 to 60% of that market in 2004.

CHANGING REGULATION OF BANKS

The great re-regulation of the developed world's banking system since the 2007–8 financial crisis, and in particular the continuing implementation of the Basel II rules and the introduction of the Basel III regime, is having a range of important effects. In particular, incentives have increased for banks to cut their exposure to assets that carry relatively high risk weightings and that are relatively illiquid, such as SME loans and overdrafts. By contrast, initiatives such as Alibaba's illustrate a major advantage that new non-bank lenders enjoy over the conventional banking sector: they are not obliged to hold regulatory capital against the risk that borrowers may default. In the case of loans to SMEs, where regulatory risk weightings tend to be high, this represents an important cost advantage.

In addition, the prospect of higher risk weightings on trade finance instruments such as Letters of Credit under the Basel III regime have made banks less willing to provide this form of trade finance – which is often the most readily accepted in emerging markets. The effect is to encourage the emergence of alternative ways of financing cross-border trade flows, such as BPO under supply-chain finance and international factoring arrangements.

LOSS OF TRUST IN BANKS

In some markets, the conduct of banks before and during the financial crisis has led to a profound loss of trust in these institutions, both because of doubts over their ethics and because of their apparent reluctance to lend to smaller businesses. This trend has led alternative lenders to position themselves in direct opposition to banks as the 'true supporters' of entrepreneurs and SMEs and it has considerably boosted their appeal.

THE SEARCH FOR YIELD CAUSED BY ULTRA-LOW INTEREST RATES

A final economic trend that cannot be underestimated is the effect of a sustained period of very low or state-controlled interest rates. In the West and in certain countries or places in Asia, the effect of this has been to fuel a 'search for yield' that has encouraged savers and investors to move beyond the traditional sources of income in search of higher returns. This search has taken some of them into new asset classes that were previously unavailable, such as direct lending to SMEs.

INTERNATIONAL COORDINATION

The interest and support of international organisations is frequently vital in highlighting examples of financial innovation that have the capacity to benefit SMEs in many parts of the world and in spreading knowledge of best practice. For example, the World Bank has published several research papers on Mexico's Cadenas Productivas' progress that have raised international awareness of its growth and effectiveness in spreading access to working capital among the country's SMEs. Similarly, the IFC's Global Trade Supplier Finance programme is helping to spread awareness of reverse factoring around the world. The work undertaken by the G20 and others since the financial crisis has drawn attention to a wide variety of barriers to finance that affect SMEs around the world and has set in train international efforts to remove them.

4. Barriers to greater adoption of innovations in SME finance and recommendations

Major barriers remain to the wider take-up by SMEs of the innovative funding options that are becoming available in different parts of the world. These barriers can be briefly summarised as: lack of financial education among SMEs; limited financial infrastructure; and legal, regulatory and accounting uncertainties.

LACK OF FINANCIAL EDUCATION AMONG SMES

Undoubtedly the greatest challenge facing any financial innovator seeking to target the SME market is the generally low level of financial awareness among those running small businesses. This encompasses both a lack of awareness of the range of options available and a lack of understanding of how those options work in practice, even after the business becomes aware of them. Often today, it falls to development banks and other public sector institutions to provide the necessary technical assistance and financial education. Although great efforts have been made in many countries to improve financial literacy among the business community, success to date has been very limited. ACCA's work in this area suggests that policymakers need to reconsider their approach to financial literacy, focusing on a 'business plan first' strategy where qualified finance professionals talk entrepreneurs through their plans for the business and provide 'just-in-time' training and mentoring for the specific types of finance that might be most effective and explain where to find them.

LIMITED FINANCIAL INFRASTRUCTURE

Both innovative and traditional approaches to providing finance to SMEs depend on access to effective financial infrastructure – from credit databases to payment systems. The experience of China after the PBoC's introduction of asset registries for receivables and leases shows very clearly how vital these developments have been. Equally, the record of financial innovators in developing new sources of data to aid in assessing credit risk where traditional public credit databases are not available demonstrates the key role that basic financial infrastructure plays in enabling the flow of funds to SMEs. A keener focus by policymakers on ensuring improved access to financial information and encouraging the creation of basic infrastructure such as asset registries, credit bureaux or credit risk databases, such as the International Chamber of Commerce (ICC) Trade Register, is vital in enabling credit to flow.

LEGAL, REGULATORY AND ACCOUNTING UNCERTAINTIES

There are numerous instances where 'grey areas' of law and regulation can create barriers to innovation in financial services and obstruct the flow of funding to SMEs.

Examples include:

- weak protection of minority shareholder rights in some jurisdictions, which discourages equity investment
- uncertainty over the classification of receivables under accounting rules where payment terms are extended, for example in multi-lender platforms of SCF programmes; also, some large companies have expressed concerns that these liabilities might need to be reclassified as loans rather than trade payables, which would affect key financial ratios
- uncertainty in some jurisdictions as to the status of factored receivables in bankruptcy, depending on whether the transaction is viewed by regulators as borrowing or the sale and repurchase of an asset
- the need for clarification of the regulatory risk weightings to be applied to bank payment obligations
- doubts over the regulatory status of new entrants, which can make it difficult for them to operate.

These issues all require detailed efforts by policymakers, regulators and interested parties, including ACCA, to ensure that work is done to clarify the rules that govern key financial intermediaries. To this end, an international effort to collate items that require clarification and agreement would provide a valuable first step in this necessary process, as also would efforts to identify and promote examples of legal and regulatory 'best practice' in regulating financial services for SMEs between different jurisdictions.

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