SME Finance

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IFC | International Finance Corporation
WORLD BANK GROUP

Creating Markets, Creating Opportunities

SMEs play a central role in the creation of dynamic, competitive and inclusive economies

Growth & Competitiveness

- SMEs are considered a key **engine of economic growth**.
- SMEs contribute **~40% of GDP** in emerging economies[1].
- SMEs are essential to creating competitive economies by **promoting innovation, increased competition**, and improved products and services.
- SMEs play an important role in **value chains** as critical suppliers to corporates (both domestic and MNCs) that link to global markets.

Inclusion

- Certain SME segments are largely unable to access financing, creating a **drag on financial activity/opportunity** among those segments.
- Women-owned, rural and agri-related, and informal SMEs, and SMEs in IDA/FCS are among the **most excluded**.
- SMEs are also critical channels for the **delivery of goods and services** to the poor and to underserved markets.

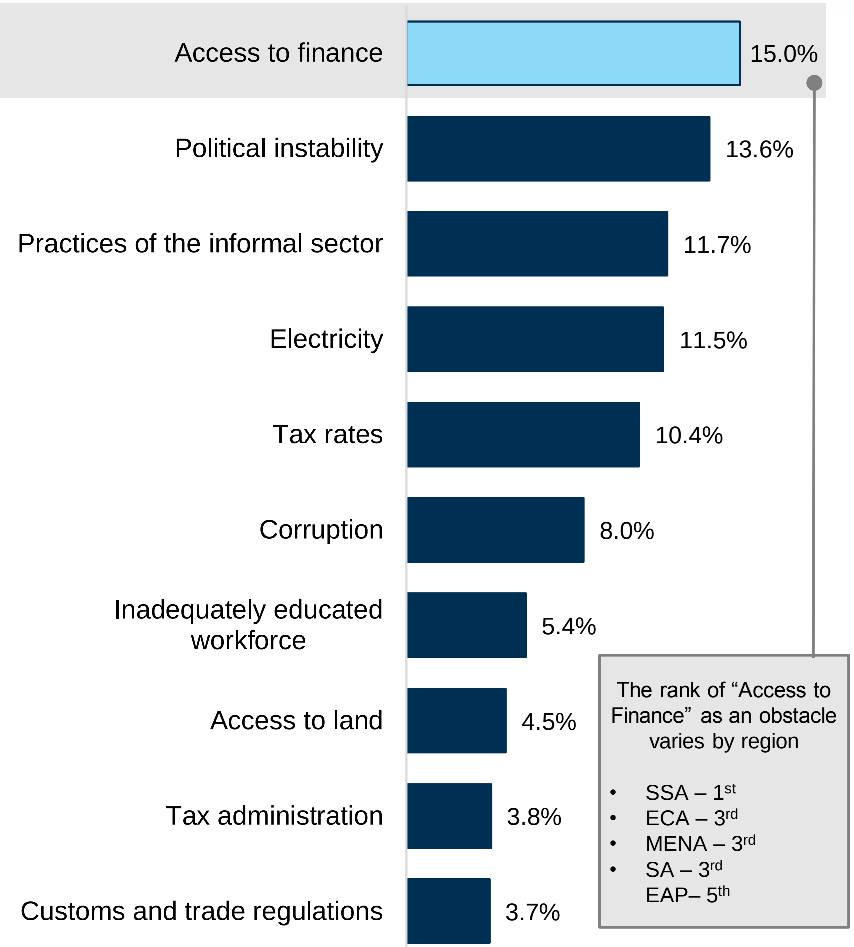
Jobs

- **600 million new jobs** will be required in emerging markets by 2030, of which 40% are expected to be generated from formal SMEs[2].
- SMEs are **major job creators,** contributing over 90% of net job growth in developing economies[3].

Sources: 1. IFC-McKinsey, "Two Trillion and Counting", 2010; 2. World Development Report 2012;
3. Gemechu Aga, David C. Francis and Jorge Rodriguez Meza, 2015, Policy Research working paper; no. WPS 7493

Access to finance (A2F) is one of the biggest obstacles for SMEs; addressing this obstacle will help SMEs grow

SMEs identify "Access to Finance" as the most significant obstacle that their enterprise faces[1]



* Results are a simple average of Small and Medium enterprise survey results across 99 LIC and MIC countries, in which firms identify their "Biggest Obstacle" out of 15 possibilities

SME access to finance is constrained by both supply- and demand-side factors

SME Demand for Finance

- Lack of fixed collateral / weak property rights
- Lack of track record (poor financial records, unpredictable cash flows)
- High cost of doing business (lack of scale, weak infrastructure, formalization costs)
- Poor financial and management skills

Bank Supply of Finance

- Higher cost of lending (acquisition, costly distribution networks, small size of transaction, high capital/provisioning costs)
- Risk appetite (poor credit information, risk modeling, solvency & enforcement regimes)
- Undeveloped product offering (complexity of cross-selling, loan officer capabilities)
- Pricing constraints and distortions (interest rate caps/subsidies)

[1] Source: Enterprise Surveys

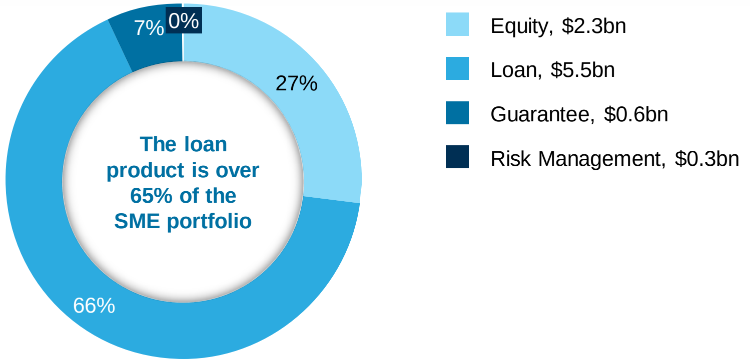
Market trends and technology are affecting the supply and ease of obtaining SME finance

	Evidence	A2F Impact
Increased business need of serving SMEs	• Increasing **banking penetration** and shrinking margins on corporate and government debt are leading to more banks interested in the SME segment. SME operations produce a 3-6% ROA while bank wide operations deliver a 1-3% ROA[1]	+
Increasing regulatory challenges	• FIs are looking to de-risk their balance sheets due to **higher capital charges** required by regulators, increasing the difficultly of lending to SMEs. Capital required for an SME loan is 3.75 – 5x the capital required for a top-rated corporate loan under Basel III • In addition, 76 governments have introduced **interest rate caps**[2] to protect consumers from higher interest rates. However, this policy decision typically increases constraints for small firms and underserved segments to access finance	−
Integration of SMEs into domestic/ global value chains (GVCs)	• Multinational corporations are catalyzing the increase in cross-border trade as well as technology to **link buyers, sellers and financiers** in new value chains. The ability of SMEs to participate in GVCs can yield substantial benefits, including spill-overs of production technology and managerial know-how[3]. To this end, in 2015, the G20 focused on promoting better integration of SMEs into GVCs, in particular in low-income developing countries (LIDCs)[4]	+
Effects of digital disruption	• Fintechs and other digital platforms are **threatening the banking landscape** by offering channels that expand access, lower costs and deliver expanded financial services. However, while there is great potential to impact the SME finance space, most existing models have focused primarily on payment solutions and the retail segment • FIs are responding by adapting disruptive technology to make **better, faster lending** decisions (30% cost reduction in customer acquisition when using mobile wallets)[5], making credit decisions on **first time customers** (data analytics), and providing SMEs with tools to **overcome information deficiencies** (non-financial services)	+

1 IFC SME Banking Knowledge Guide, 2010
2 WB Policy Research Working paper, Interest rate caps around the world: still popular, but a blunt instrument, 2014
3 OECD and WBG report on Inclusive Global Value Chains, 2015
4 Financing Growth; SMEs in Global Value Chains: The case for a coordinated G20 policy approach
5 Gates Foundation, How Agent Banking Changes the Economics of Small Accounts, 2010

More than half of the SME business is providing loans to intermediaries

SME Finance Committed Portfolio by Product,
Average FY14-16



SME Finance Committed Volume by Product,
Average FY14-16

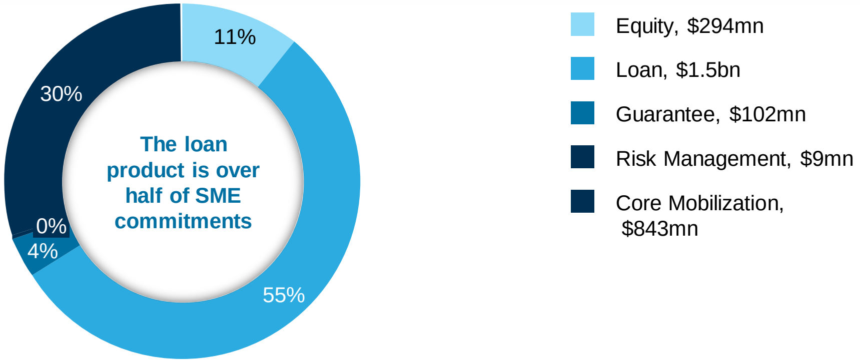


FIG Own Account Volume by Firm Size,
Average FY14-16

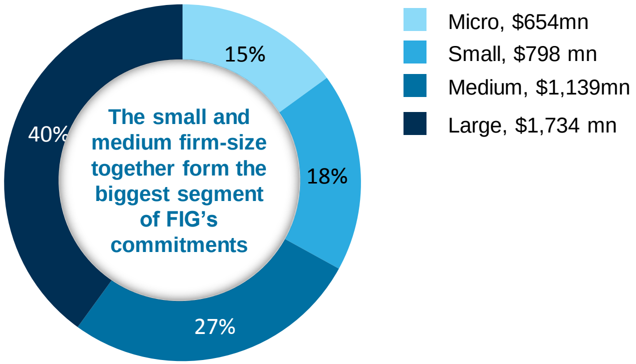
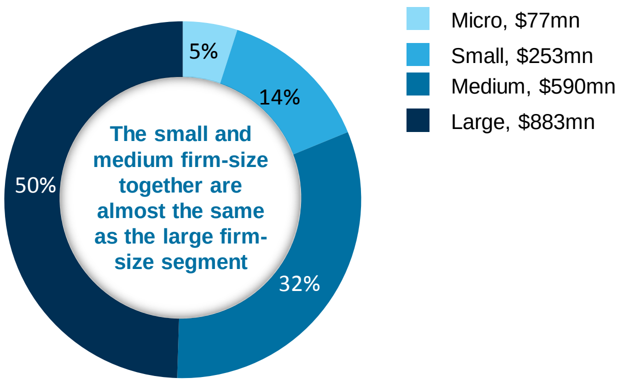


FIG Core Mobilization Volume by Firm Size,
Average FY14-16



Analysis of SME Reach from IFC Financial Institution Clients

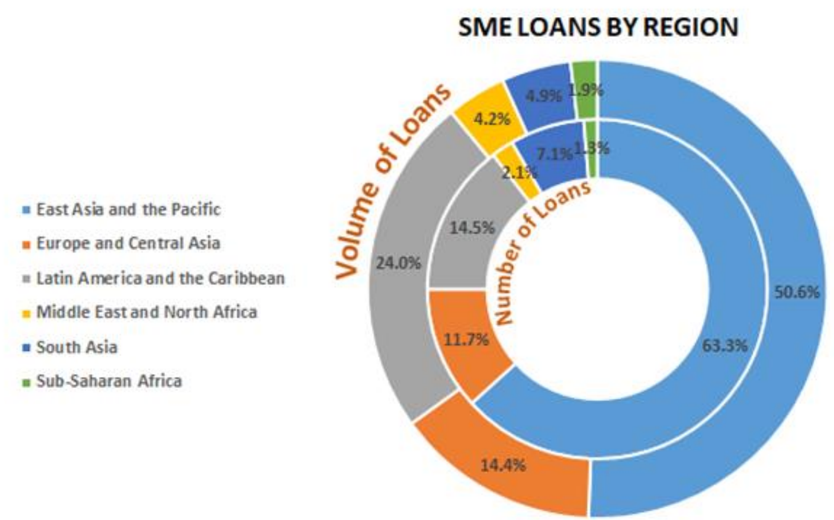
Every year IFC requests FI clients to provide IFC with information about their loan portfolio, deposits and other business related data.[1] Through this Reach Survey, IFC tracks and analyzes financing outreach to the final recipients, including SMEs. Using IFC's proxy SME loan definition, it is estimated that these clients **had 8.3 million SME loans totaling $350 billion**.

IFC collected and extrapolated 2016 data from 344 clients in 92 countries, which had over 8.3 million SME loans totaling $351 billion. Table 1 and Chart 2 show regional distribution of SME loans by volume and number.

IFC FI Clients' SME Outstanding Loan Portfolio by Region, 2016

Region	SME Loans	
	# million	$ billion
East Asia and the Pacific	5.3	177.8
Europe and Central Asia	1.0	50.5
Latin America and the Caribbean	1.2	84.3
Middle East and North Africa	0.2	14.8
South Asia	0.6	17.2
Sub-Saharan Africa	0.1	6.6
Total Loans	8.3	351.1

IFC FI Clients' SME Outstanding Loan Portfolio Distribution (%), 2016



IFC FI Clients' Loans to Women and Women-owned SMEs[2]

	Number of Loans to Women	Total volume of Loans to Women	Number of Loans to Women	Total volume of Loans to Women	NPLs
SME	262,200	7.17 b	15.5%	8.6%	4.1%

[1] IFC collected and extrapolated 2016 data from 344 clients in 92 countries, which had over 302 million loans outstanding worth over $1.7 trillion. This included retail, micro, SME and corporate loans. Of these, 304 clients globally received financing for MSME-related activities.
[2] 162 out of the 344 FI clients provided gender-disaggregated data. These clients provided 15.5% of total SME loans by number to women-owned firms.