

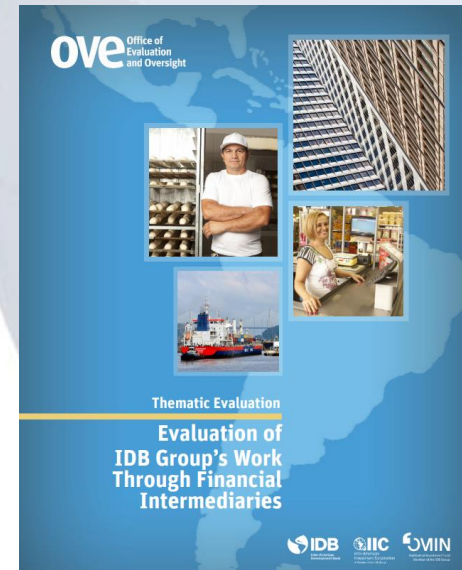
## **Bridging the Finance Gap:** WBG MSME Finance Gap Report vs. Evaluation of IDB Group's Work Through Financial Intermediaries

How do the FI evaluation – and various other information sources – complement and contrast each other?

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January 31, 2018

# Bridging the Finance Gap



WBG MSME Finance Gap Report vs.  
Evaluation of IDB Group's Work  
Through Financial Intermediaries



**IDB** Institutions for People

**Managing Environmental and Social Risks**  
A Roadmap for National Development Banks in Latin America and the Caribbean



**beyondBanking**  
banking on global sustainability

planetBanking equalBanking  
accessBanking clearBanking  
connectBanking learnBanking

**IIC**  
**Sustainability Week**

The Economist Intelligence Unit  
An Index and Study by The Economist Intelligence Unit

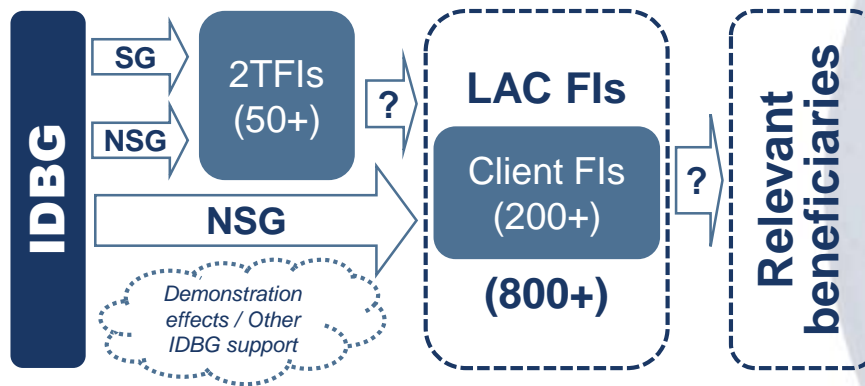
**GLOBAL MICROSCOPE 2015**  
THE ENABLING ENVIRONMENT FOR FINANCIAL INCLUSION

**BANKS AND THE MISSING MIDDLE**  
7<sup>th</sup> REGIONAL SURVEY 2014

Supported by **OVIN**



# FI operations are important to IDBG's business; thus, **OVE** conducted a thorough evaluation



- **Volume 2005-14:** \$17B (14% of IDBG approvals)
- **Role:** cost-effective way to reach smaller beneficiaries
- **Income:** significant, stable, key to NewCo's start up, other DFIs

- **Portfolio** review (466) and in-depth on sample (131)
- **Interviews** management (5), IOs (38), FIs & experts (+100)
- Country **missions** (10), focus groups (16), **survey** (+120)
- DFI **benchmarking** (all 9)
- **Country** A2F profiles (all)



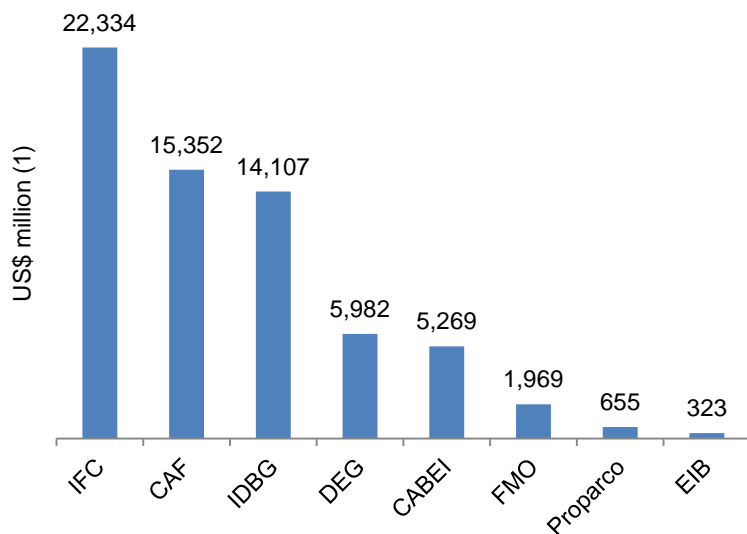
**Main  
Evaluation  
report**

## 11 background papers:

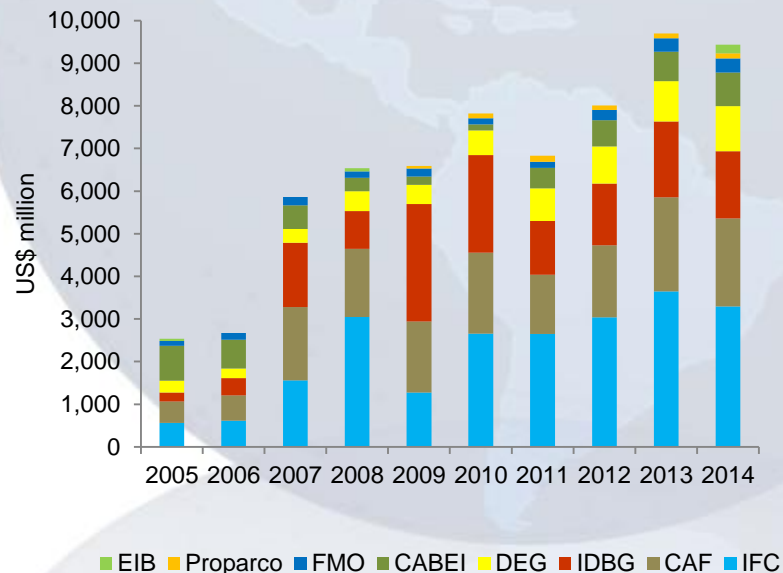
- SME
- Trade finance
- Housing finance
- Leasing & factoring
- Green lending
- E&S safeguards
- DFI benchmarking
- IO surveys
- FI client surveys
- External feedback survey
- A2F country profiles

# Eight DFIs, including IDBG, provided **\$65.9 billion** to FIs in LAC between 2005 and 2014

## IFC, CAF, and IDBG were the top three DFIs financing FIs in LAC in 2005-2014



## The annual FI-investments of the DFIs almost quadrupled from 2005 to 2014



Source: Data provided by DFIs, Annual Reports and OVE calculations. Committed amounts, except for CAF approved amounts.

(1) For European DFIs translated into US\$ at annual average exchange rates.

\* IFC and FMO data include own amounts and syndicated/mobilized amounts.

\*\* OVE estimated IFC's trade financing share in LAC as 30% of its total.

\*\*\* EIB data includes a Euro 150 million credit line in Brazil in 2015.

# Evaluation findings fall into **three main areas**



# Need **clear strategy!**

- **Goal:** Sustainably increase A2F to previously under-served groups
- **Need data ... and coordination public-private!!!**
  - Finance gap report helps – **What!**
  - MIF / IDB Invest also working on supply, enabling environment: **Collaborate!**
  - Need MDBs to work with banking regulators:  
Consistent reporting of MSME finance  
... **according to LOCAL definitions!!!**
- Still need to know: **Why? What to do?**

# Need good **country-level analysis** of A2F barriers to select the appropriate instrument

## Typical A2F barriers (country specific)

## Country needs vs. instruments

- |                           |                             |
|---------------------------|-----------------------------|
| 1. FI funding constraints | 5. Financial sophistication |
| 2. FI risk perceptions    | 6. Regulatory environment   |
| 3. FI client know-how     | 7. Financial infrastructure |
| 4. FI market competition  | 8. Risk-based crowding out  |

FI operations

Other instruments

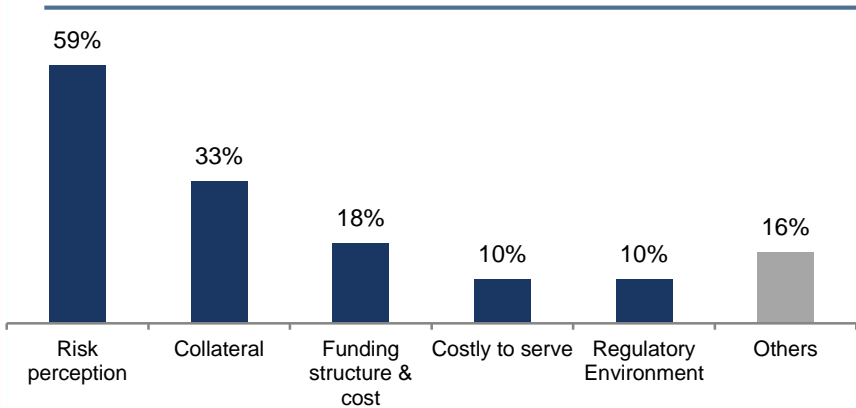
- Limited country-level analysis of A2F barriers
- No focus on competition
- Mostly senior FX loans, though funding rarely a constraint
  - Equity, subordinated debt, and local currency lending can better meet clients' and beneficiaries' needs

MSME Finance Gap Report: → Valuable input for “HOW MUCH” MSME finance is missing.  
Need also: WHY is it missing? ... and WHAT TO DO?

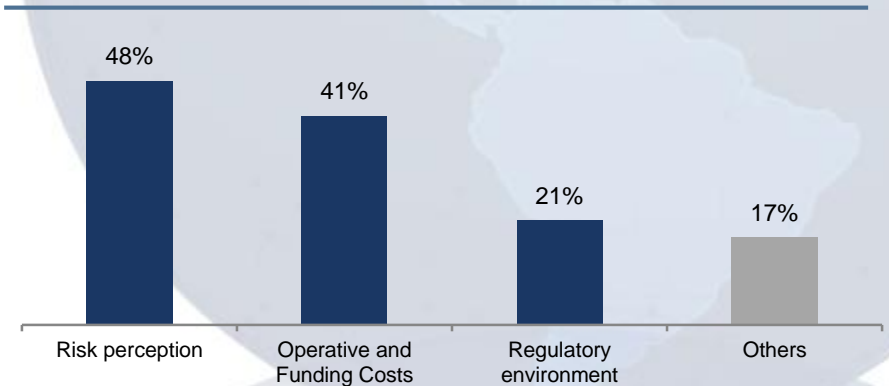


# Greatest challenge perceived by FIs: Borrowers' informality → increasing risk perception

Risk perception the biggest challenge for serving SMEs (n=49)



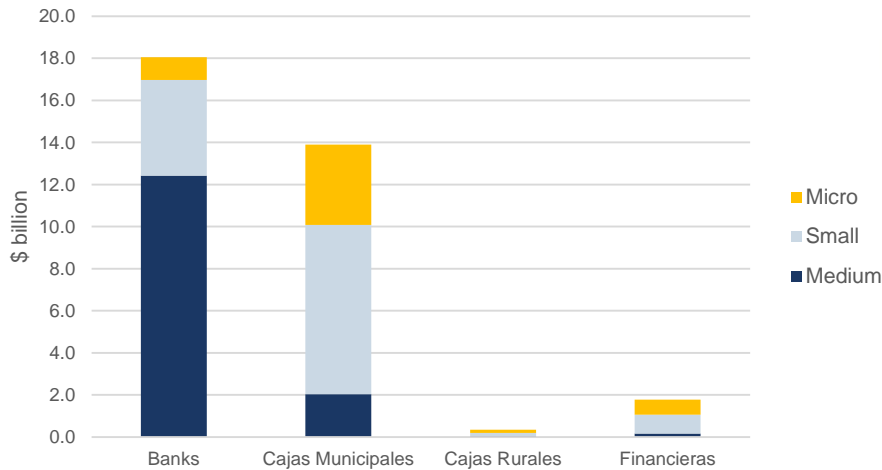
Similarly, risk perception the biggest challenge for serving microenterprises (n=29)



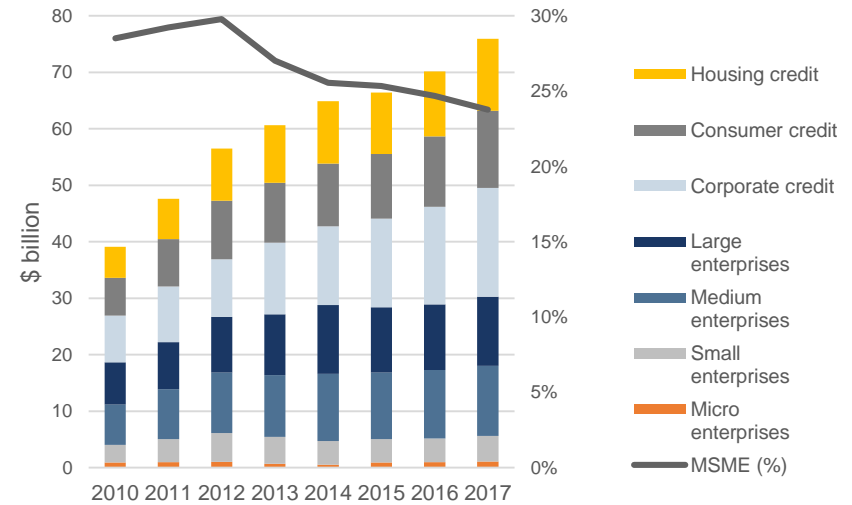
Source: OVE survey with client FIs, 2015

# MDBs should encourage regulators to systematically collect relevant data

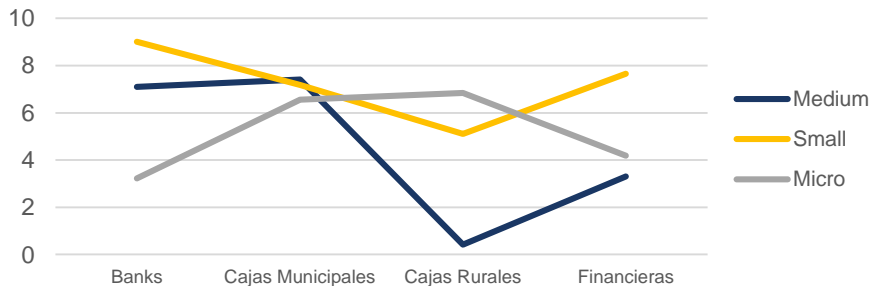
### 2017 Portfolio of MSME loans - Peruvian FIs



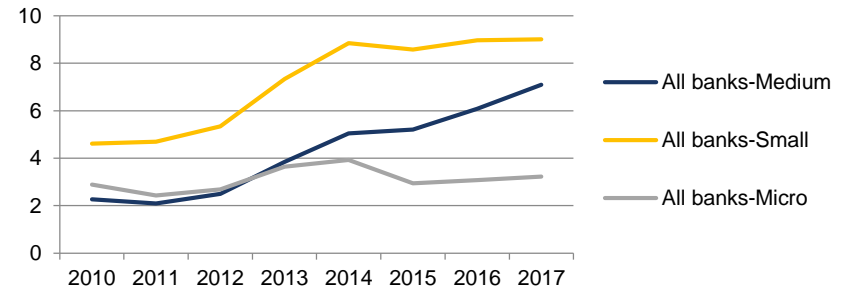
### Evolution of bank lending in Peru



### NPLs by type of enterprise and FI (Peru, End-2017)



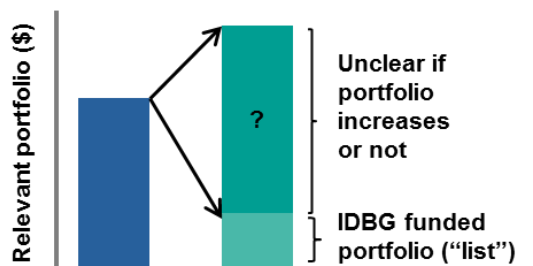
### NPLs of MSME Loans - Peruvian Banks



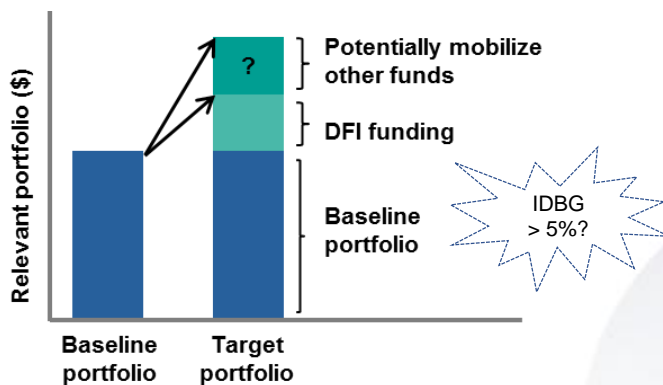
# Need to structure operations and select instruments to foster change

## Fostering and measuring development results

Now:  
Use of  
IDBG  
proceeds



Preferred:  
Increase in  
FI's  
relevant  
portfolio

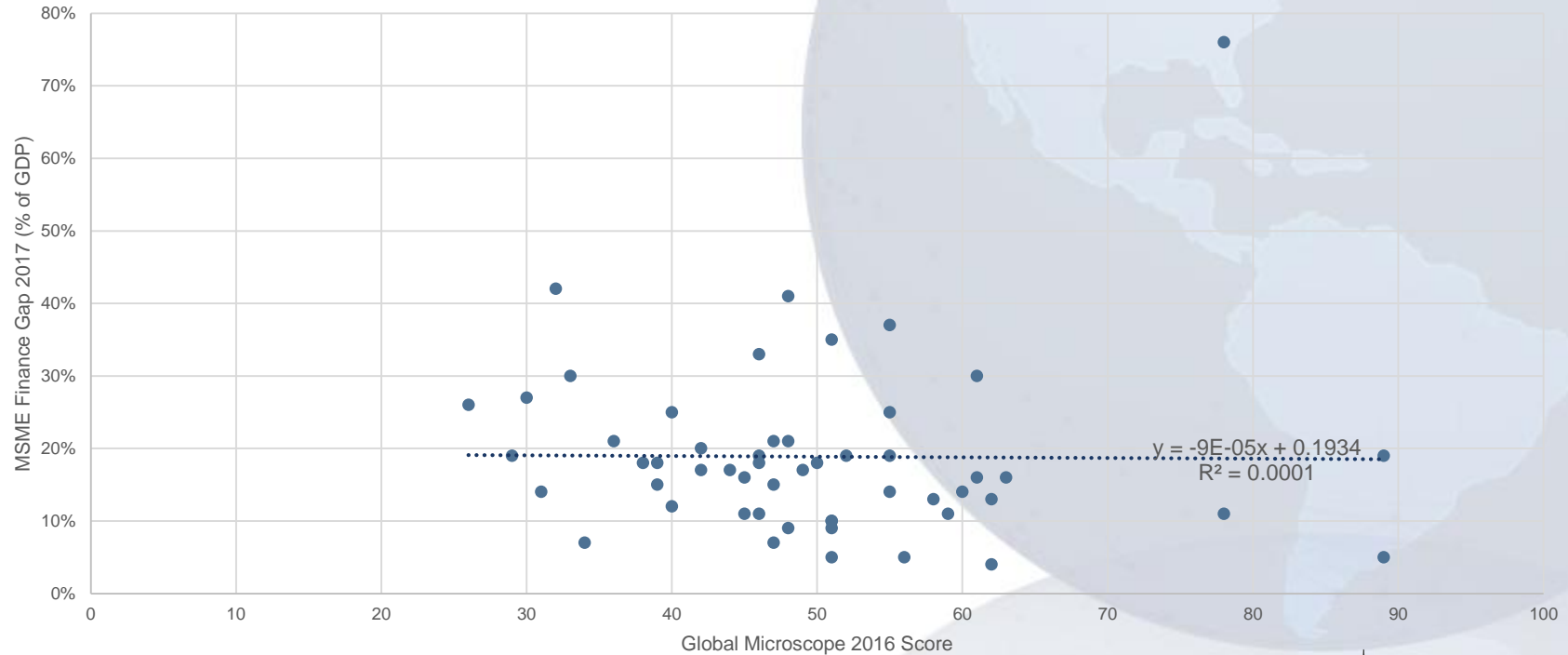


## Instrument choice

- **Funding alone:** weak motivator
- **Need strategic alignment – move to FI's definition of MSMEs**
- **Biggest constraint:** informality – information about creditworthiness
- **Positive:** TA to support new business, topics ... but limited funds for FI work

# Correlation: MSME Finance Gap vs. Global Microscope?

No correlation: MSME Finance Gap and Global Microscope Score



**Why???**

Look at sub-components:  
Capacity of regulator  
Credit reporting



# OVE's recommendations aim to **strengthen development impact** through FI operations



1. **Develop and implement a meaningful IDBG-wide strategic approach for working through FIs**, including criteria for when to use a sovereign guarantee, FI selection and terms, and what instruments to use



2. **Better integrate FI work across IDBG into Country Strategies** to address A2F barriers. WHAT is missing for WHICH SEGMENT and WHY?



3. **Seek ways to generate income for IDBG, other than from just lending spreads**, to facilitate the use of a wider, more targeted range of instruments



4. **Strengthen M&E and IDBG accountability for results**, to be able to generate and manage adequate incentives and instruments.  
MOVE TO COUNTRY / FI DEFINITION AND TRACK PORTFOLIOS VS. MARKET!



5. **Review and strengthen the application of E&S safeguards to FI operations**, to effectively mitigate risks and help build capacity in LAC FIs and countries.

# Summary

- MSME Finance Gap Report clearly adds value – WHAT is missing?
- Need to better understand data – outliers?
- MDBs need to work with banking regulators: Better data.  
→ Better policy choices. → Better tool selection
- Still need to know why: Informality – difficulty assessing creditworthiness. Tools:
  - Online payments – cashflow based lending
  - Work with suppliers/distributors of larger companies
- Demonstrate: MSME is profitable business!

# Thank you

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IDB – OVE

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