Innovative Mechanisms for Financing MSMEs: FinTech Solutions and Policy Actions in Asia

Shigehiro Shinozaki
Financial Sector Specialist (SME Finance)
Sustainable Development and Climate Change Department
Asian Development Bank

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MSMEs in developing Asia, especially women-led MSMEs, have faced the highest financing gap in the world.

**MSME Finance Gap in Developing Economies**

<table>
<thead>
<tr>
<th>Region</th>
<th>Micro ($ billion)</th>
<th>SME ($ billion)</th>
</tr>
</thead>
<tbody>
<tr>
<td>East Asia &amp; Pacific</td>
<td>2,110</td>
<td></td>
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<tr>
<td>Europe &amp; Central Asia</td>
<td>1,236</td>
<td></td>
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<tr>
<td>Latin America &amp; Caribbean</td>
<td>1,098</td>
<td></td>
</tr>
<tr>
<td>Middle East &amp; North Africa</td>
<td>93</td>
<td></td>
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<tr>
<td>South Asia</td>
<td>291</td>
<td></td>
</tr>
<tr>
<td>Sub-Saharan Africa</td>
<td>245</td>
<td></td>
</tr>
</tbody>
</table>

**Women-led MSME Finance Gap in Developing Economies**

<table>
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<tr>
<th>Region</th>
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<th>SME ($ billion)</th>
</tr>
</thead>
<tbody>
<tr>
<td>East Asia &amp; Pacific</td>
<td>103</td>
<td></td>
</tr>
<tr>
<td>Europe &amp; Central Asia</td>
<td>67</td>
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<tr>
<td>Latin America &amp; Caribbean</td>
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<td>Middle East &amp; North Africa</td>
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<td>South Asia</td>
<td>23</td>
<td></td>
</tr>
<tr>
<td>Sub-Saharan Africa</td>
<td>42</td>
<td></td>
</tr>
</tbody>
</table>

Source: Recomposed from IFC, 2017. MSME Finance Gap.
Both supply-side and demand-side factors constrain access to finance.

Barriers to Accessing Financial Institutions

- Collateral/guarantee
- Lending policy of FI
- Complicated procedures
- Exclusive lending attitude of FI
- High lending rate
- Short loan term
- SMEs' insufficient management
- No demand on SMEs
- SMEs' lack of knowledge
- Phillips (PHI): 63
- Kazakhstan (KAZ): 98
- Papua New Guinea (PNG): 19
- Sri Lanka (SRI): 15
- People's Republic of China (PRC): 303
- Malaysia (MAL): 60
- Republic of Korea (KOR): 28
- India (IND): 40

Notes: Percentage as the share of SMEs that answered yes plus somewhat yes from five scale scores (yes, somewhat yes, neutral, somewhat no, and no) about barriers to access finance. Valid samples: the Philippines (PHI): 63; Kazakhstan (KAZ): 98; Papua New Guinea (PNG): 19; Sri Lanka (SRI): 15; People's Republic of China (PRC): 303; Malaysia (MAL): 60; Republic of Korea (KOR): 28; India (IND): 40.
Source: Author’s compilation.
Strict banking regulation may be a contributing factor.

- Basel III may negatively affect banks’ lending attitude to SMEs.
  - Basel III requires banks to have tighter risk management as well as greater capital and liquidity.
  - Resulting asset preference and deleveraging of banks could limit the availability of funding for SMEs.
    - Capital requirements
    - Liquidity framework
    - Leverage ratio framework
MSMEs as main beneficiaries of FinTech. New players & alternative finance products have been emerging.
Digital finance highly contributes to reducing financing gap in developing Asia.

Potential Impact of Digital Finance on Access to Finance in Asia

- MYA - credit
- MYA - payments/transfers
- CAM - savings
- CAM - credit
- CAM - payments/transfers
- PHI - savings
- PHI - credit
- PHI - payments/transfers
- INO - payments/transfers
- INO - credit
- INO - savings

Gap to be reduced by digital finance (% of gap) and Unmet demand (% of demand)

INO=Indonesia, PHI=Philippines, CAM=Cambodia, MYA=Myanmar.
Digital finance can create $2.1 trillion in new credit and $4.2 trillion in new deposits globally.

South Asia has the highest potential of benefits from DFS.

Digital channels are more actively utilized than bank branches for daily transactions in Asia.
Digital banking has an increasing trend but still low penetration in developing Asia.

Business Opportunities for MSMEs

- Labor productivity growth is slowing in developing Asia and estimated to continue.
- FDI inflows to Asia create opportunities for MSMEs to increase productivity.

**Labor Productivity Growth**

**FDI Net Inflows in Asia and the Pacific**


Tech-based MSMEs

- The Fourth Industrial Revolution can create more tech-based MSMEs with more jobs, while the potential of reducing workforces from large/established firms.

- Tech-based MSMEs play a critical role of increasing national productivity, benefitting from FDI and active participation in global value chains.

- MSMEs’ innovation capability requires investment in R&D, human capital, and technology transfer & commercialization, suggesting the need for more market-based financing options.
Low investment in R&D makes MSMEs’ innovation capability remain weak.

Source: Recomposed from World Bank Enterprise Surveys Data. PHI (2015), INO (2015), MAL (2015), and THA (2016). First four items: % of firms; last two items: proportion of investments (%).
Approaches to reduce supply-demand gap in MSME finance

Credit data infrastructure
- Credit bureau data
- Credit risk database
- Cloud/online data
- Telecom data
- e-commerce data
- Credit bureau data
- Credit risk database
- Cloud/online data
- Telecom data
- e-commerce data

Secured lending legal reform
- Asset based finance

Credit guarantees
- Credit guarantee facility
- Regional CGIs
- Portfolio credit guarantees
- Client data

Credit rating/credit scoring services
- Online collateral registry
- Pledgeable assets (movable assets)
- Enforcement

Optimal credit guarantee ratio

MSMEs

Financial education
Alternative MSME Finance Models: Online Supply Chain Finance

1. Supplier (MSME)
   - Upload invoice
   - Request finance
   - Provide finance

2. Buyer
   - Approve invoice
   - Payment at maturity

3. Financier
   - Provide finance

4. Online Platform
   - Verification
   - Alternative data stock

5. Accounting software

Smart contract

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Alternative MSME Finance Models:  
Public-Private Sector Collaboration and Digital Solution

**A. Crowdfunding segment**

**B. SME incubation segment**

I. Growth capital financing to SMEs via partner financial institutions & the Exercise Market

II. Capacity building programs via partner institutions

III. Connect SMEs with good business models to the Exercise Market

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**Promising SME pool**

- Selected/Prioritized Businesses (seed/start-up/early-stage firms)

**SME recruiters**

- Banks
- Venture capital
- Regional incubation center/BDS

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**Public APEX Fund**

(SME Incubation Fund)

- Funded by the govt., bi-or multilateral donor(s)

**Crowdfunding platform management company**

**Exchange market**

**Exercise Market**

**A. Crowdfunding segment**

**B. SME incubation segment**

**Investors (mainly individuals/supporters for the business)**

- Fund 1
- Fund 2
- Fund 3
- Fund 4

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**Agri-business**

**Woman-led SME**

**Tech-based SMEs**

**Social enterprises**

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**SRO-operated OTC**
Policy Implications in Asia

- Policy actions are required to encourage the shift to digital in MSME finance.
  
  ✓ Diverse **financing options** well fit to the demand on MSMEs, with use of digital technology.
  ✓ Develop **infrastructure** for DFS: a national payment switch, digital identity, and open API.
  ✓ Develop methodologies to secure **quality & reliable data** for analysis, product design, and risk management.
  ✓ **Regulation as an enabler** for innovative finance products & services.
  ✓ Strengthen **financial integrity** to keep a financial system transparent, given the AML-CFT.
  ✓ Address **consumer protection** and facilitate **competition** further.
  ✓ Enhance **digital finance literacy** among MSMEs.
Thank you for your attention.

For further questions:
Shigehiro Shinozaki
Financial Sector Specialist (SME Finance)
Sustainable Development and Climate Change Department
Asian Development Bank
Email: sshinozaki@adb.org