

CENTRE FOR ENTREPRENEURSHIP, SMEs AND LOCAL DEVELOPMENT

New Approaches to SME and entrepreneurship finance: Broadening the range of instruments

Final Synthesis Report

Working Party on SMEs and Entrepreneurship (WPSMEE)

This document contains the final synthesis report of the project on “New Approaches to SME and entrepreneurship finance: Broadening the range of instruments”. It highlights key findings and policy messages emerging from the mapping external financing techniques alternative to straight debt, and insights from the case studies on crowdfunding; and on SME securitisation, covered bonds, corporate bonds and private placements.

This synthesis report also contributes to the OECD initiative on New Approaches to Economic Challenges (NAEC).

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1. THE NEW REALITY FOR SME FINANCE

More than half a decade after the start of the global financial crisis, access to finance for SMEs and entrepreneurs remains a major concern globally.

1. The 2008-09 global financial crisis profoundly changed the business environment for SMEs and entrepreneurs, and access to finance was particularly affected. In many OECD countries, the crisis exacerbated the financial constraints typically experienced by SMEs, mainly as a result of information asymmetries in financial markets, and financial resources dried up for the most dynamic enterprises.

2. Across OECD countries, bank lending is still the most common form of external finance for SMEs, but as banks face more rigorous prudential rules and modify their business models, a business environment with less credit is likely to become the “new normal”. There is increasing recognition that SMEs and entrepreneurs are being disproportionately affected by financial reforms, and the rapid pace of their implementation, since they are more dependent on bank finance than large firms and less able to adapt to significant changes in credit markets.

The vulnerability of the SME sector to changing conditions in bank lending has become more evident...

3. The financial crisis underscored the vulnerability of the SME sector to changing conditions in bank lending. The long-standing need to strengthen capital structures and decrease dependence on borrowing has now become more urgent. Indeed, many firms were obliged to increase leverage in order to survive the crisis. What is more, policy responses to the financial crisis may have exacerbated the problem of SME over-leveraging; indeed, emergency stabilization programmes tended to focus on mechanisms that enabled firms to increase their debt (e.g. direct lending, loan guarantees), as funding from other sources became more scarce. Furthermore, since the crisis, banks in many OECD countries have been contracting their balance sheets in order to meet more rigorous prudential rules. Thin capitalization and excessive leverage impose costs on SMEs, in the form of higher interest rates, and increase the risk of financial distress and bankruptcy.

... as have the limitations of traditional debt for new, innovative and fast-growing companies.

4. SMEs and entrepreneurs are often heavily reliant on straight debt to fulfill their start-up, cash flow and investment needs, but traditional debt has limitations for responding to the different financing needs SMEs encounter at different stages of their life cycle. In particular, debt finance is ill-suited for newer, innovative and fast growing companies, which have a higher risk-return profile. The “financing gap” that affects these businesses is often a “growth capital gap”. Substantial funds may be needed to finance projects with high growth prospects, while the associated profit patterns are often difficult to forecast. These financing constraints can be especially severe in the case of start-ups or small businesses whose business model relies on intangibles which are highly firm-specific and difficult to use as collateral in traditional debt relations. Capital gaps also exist for companies seeking to effect important transitions in their activities, such as ownership and control changes. Yet, for most enterprises, there are few alternatives to traditional debt. This represents an important challenge for policy makers in their efforts to support a sustainable recovery and long-term growth, since these companies are often at the forefront in job creation, the application of new technologies and the development of new business models.

There is a pressing need to broaden the range of financial instruments available to SMEs and entrepreneurs ...

5. It is therefore necessary to broaden the range of financing instruments available to SMEs and entrepreneurs, in order to enable them to continue to play their role in investment, growth, innovation and employment. Financial stability, financial inclusion and financial deepening should be considered as mutually reinforcing objectives in the quest for a sustainable recovery and long-term growth. While bank financing will continue to be crucial for the SME sector, a more diversified set of options for SME financing is needed to support long-term investment and reduce the vulnerability of SMEs to changes in the credit market. An effective financial system is one that can supply financial resources to a broad range of companies in varying circumstances and channel financial wealth from different sources to business investments. As the banking sector struggles to adjust to the new regulatory environment, institutional investors and other non-bank players, including wealthy private investors, have a potential role to play in filling the financing gap.

... to improve the resilience of economies and foster new sources of growth.

6. Financial markets worldwide are more integrated and interdependent than ever before. Since the crisis, this increased complexity has been under scrutiny as the source of unsustainable fiscal imbalances. There has been a call for the financial system to return to fulfilling its essential role of intermediation and provide the necessary capital for productive activities, in order to increase macroeconomic stability and improve resilience of economies to large shocks. In particular, financial resources should be channeled to support the creation and expansion of firms, as key sources of employment and value generation. Improving financing conditions for SMEs and entrepreneurs and diversifying their sources of financing will contribute to reducing systemic risk, increasing the resilience of the real economy to large shocks and fostering new sources of growth.

2. BROADENING THE RANGE OF FINANCING INSTRUMENTS FOR SMES AND ENTREPRENEURS

Increasingly complex and interconnected financial markets offer opportunities to serve the needs of the SME sector

7. There is an increasing range of financing options available to SMEs, although some of these are still at an early stage of development or, in their current form, are accessible only to a small share of SMEs. Up to now, a lack of awareness and understanding on the part of SMEs, financial institutions and governments of these alternative instruments, their modalities and operations has held back their broader use. Improving knowledge of the full range of financing instruments for SMEs and entrepreneurs represents a first step towards broadening access to these finance options.

8. Traditional debt includes instruments such as bank loans, overdrafts, credit lines and the use of credit cards. This type of finance offers moderate returns for lenders and is therefore appropriate for low-to-moderate risk profiles, i.e. firms that are characterized by stable cash flow, modest growth, tested business models, and access to collateral or guarantees. Alternative financing instruments alter this traditional risk sharing mechanism (see Table 1).

Table 1. Alternative external financing techniques for SMEs and entrepreneurs

Low Risk/ Return	Low Risk/ Return	Medium Risk/ Return	High Risk/ Return
Asset-Based Finance	Alternative Debt	“Hybrid” Instruments	Equity Instruments
<ul style="list-style-type: none"> • Asset-based lending • Factoring • Purchase Order Finance • Warehouse Receipts • Leasing 	<ul style="list-style-type: none"> • Corporate Bonds • Securitised Debt • Covered Bonds • Private Placements • Crowdfunding (debt) 	<ul style="list-style-type: none"> • Subordinated Loans/Bonds • Silent Participations • Participating Loans • Profit Participation Rights • Convertible Bonds • Bonds with Warrants • Mezzanine Finance 	<ul style="list-style-type: none"> • Private Equity • Venture Capital • Business Angels • Specialised Platforms for Public Listing of SMEs • Crowdfunding (equity)

Source: OECD, (2013), *Alternative financing instruments for SMEs and entrepreneurs: The case of mezzanine finance*, OECD, Paris.

Asset-based finance is a widely used instrument to provide working capital to young and small firms on more rapid and flexible terms than traditional lending

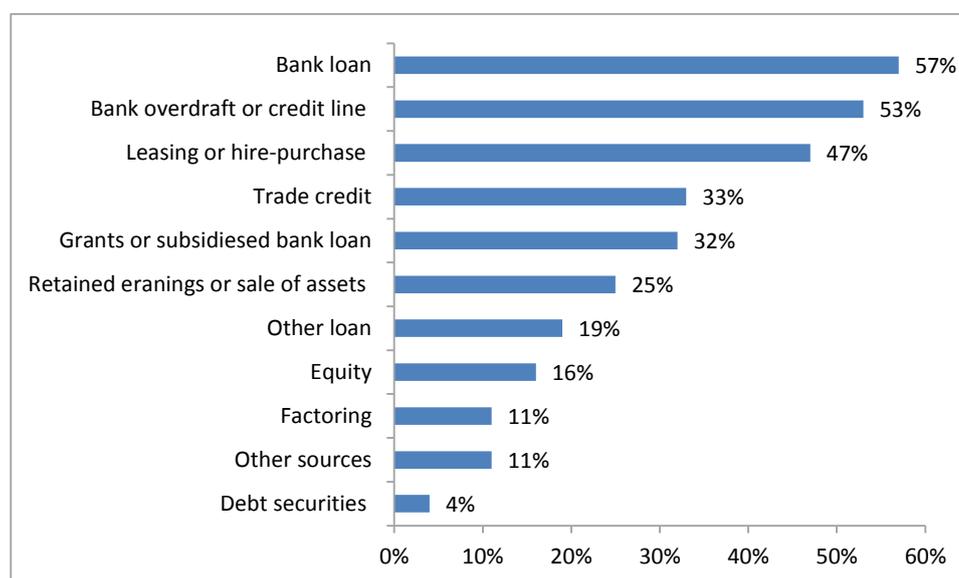
9. At the one end of the risk/return spectrum are financing instruments that sustain the short and medium-to long-term financing needs of SMEs, but rely on different mechanisms than traditional debt. This is the case of asset-based finance (e.g. asset-based lending, factoring, leasing), whereby a firm obtains cash, based not on its own credit standing, but on the value of specific assets, including accounts receivables, inventory, machinery, equipment and real estate.

10. The key advantage of asset-based finance is that firms can access cash faster and under more flexible terms than through conventional secured lending, regardless of their balance sheet position and future cash flow prospects. Furthermore, with asset-based finance, firms that lack a credit history, face temporary shortfalls or losses, or need to accelerate cash flow to seize growth opportunities, can access working capital in a relatively short time. Asset-based agreements often allow for revolving funds; as advances are paid off, the borrower can secure additional funds backed by other assets. In addition, asset-based financiers do not generally require any equity or personal guarantee from the entrepreneur. On the other hand, the costs incurred and/or the complexity of procedures may be substantially higher than those associated with conventional bank loans, and funding limits are often lower than in the case of traditional debt.

11. Asset-based finance is widely used by SMEs across OECD countries, and increasingly in emerging economies, to meet their working capital needs, support domestic and international trade, and, in some cases, for investment purposes. In Europe especially, the prevalence of these instruments for SMEs is about on par with conventional bank lending (Figure 1). Asset-based finance has grown steadily over the last decade, in spite of repercussions of the global financial crisis on the supply side.

Figure 1. Relevance of financing types for SMEs, EU-28, ECB/EC SAFE survey, 2014

(% firms that used in the past or considered using in the future)



Source: ECB/EC.

12. Policies to promote asset-based finance relate primarily to the regulatory framework, which is key to enable the use of a broad set of assets to secure loans. Across OECD countries, active policies exist to support asset-based finance for businesses that are unable to meet credit standards associated with long-term credit. In particular, factoring has been supported as a means to ease SMEs' access to trade finance and promote their inclusion in value chains.

The potential of alternative debt instruments in the capital markets to finance SME investment is starting to be recognized.

13. Alternative debt differs from traditional lending in that investors in the capital market, rather than banks, provide the financing for SMEs. Alternative forms of debt, such as corporate bonds, have had only limited usage by the SME sector, even within the larger size segment which would be suited for structured finance and could benefit from accessing capital markets, to invest and seize growth opportunities. Corporate bonds typically require the issuer to have a certain size and scale, an established credit history and earnings record, and limited volatility on revenues and earnings. As most SMEs do not meet these criteria, in the bond market they would attract low rating and high coupons and have limited dividends to cover these regular payments.

14. On the other hand, corporate bonds present some advantages for mid-sized firms that can meet the criteria requested by the market, and which can respond to the reporting requirements linked to bond issuance. Financing with corporate bonds can be an especially attractive option when market interest rates are low, as the coupon rates over the life of the bond can be set at a convenient rate, and still attract investors. Also, unlike equity, issuing bonds does not dilute ownership or the control of the company.

15. To foster the development of a corporate bond market for SMEs, mainly mid-caps, policy makers have targeted transparency and protection rules for investors, to favour greater participation and liquidity. Recent programmes have also encouraged the creation of SME trading venues and the participation by unlisted and smaller companies. In some countries, public entities participate with private investors to funds that target the SME bond market, with the aim of stimulating its development.

16. In some countries, the regulatory framework allows private placements of corporate bonds by unlisted companies, which are subject to less stringent reporting and credit rating requirements. However, insufficient information on issuers and a lack of standardized documentation; illiquid secondary markets; and differences in insolvency laws across industry players and jurisdictions currently limit the development of these markets.

SME loan securitization is receiving increasing attention as a way to support capitalization of banks and foster SME lending

17. Debt securitization and covered bonds are instruments for the refinancing of banks and for their portfolio risk management; these instruments have developed at a high pace in the past decade. Through securitization, various types of contractual debt are pooled and sold to investors, who acquire rights to receive the cash collected from the financial instruments that underlie the security.

18. Securitization allows banks to transform SME loans in their balance sheets into liquid assets, which can be used to increase lending itself. Also, securitization reduces the bank's exposure to credit risk, which is transferred to the capital market. This has important implications in the light of the recent financial reforms (i.e. Basel III), as risky assets are taken out of the banks' balance sheets and the capital to risk-weighted asset ratios is improved. Ultimately, by giving capital relief, securitization reduces the bank's total cost of financing.

19. Covered bonds work similarly to securitized debt, except that assets remain on the issuer's consolidated balance sheet. Thus, they cannot help to strengthen the issuer's capital ratio. Asset encumbrance implies that they are seen as a complement, rather than as substitute to securitization. At the same time, because covered bonds are secured, they are considered to be less risky than unsecured bank bonds, which implies low-cost funding for the issuer.

20. However, in the wake of the financial crisis, debt securitization has come under scrutiny and criticism, as one major driver of risk leveraging and financial instability. Although it was not at the core of the financial turmoil, SME loan securitization, which had started to expand just before the crisis, came to a halt or decreased significantly, affected by contagion in financial markets and in public perceptions. Over the last few years, however, it has attracted renewed attention by policy makers and financial authorities, as an important instrument to foster SME lending.

Crowdfunding is still in the early stages of development as a source of business finance, but is expected to play an increasing role in the future, as this instrument becomes more regulated.

21. Crowdfunding has grown rapidly since the mid-2000s, and at an increasing rate in the last few years, although it still represents a very minor share of financing for businesses. One specificity of this instrument, by which external finance is raised from a large audience through web platforms, is that it

serves to finance specific projects rather than an enterprise. It has been used in particular by non-profit organisations and the entertainment industry, where non-monetary benefits or an enhanced community experience represent important motivations for donors and investors. Nevertheless, over time, crowdfunding has become an alternative source of funding across many other sectors, and it is increasingly used to support a wide range of for-profit activities and businesses.

22. While donations, rewards and pre-selling currently lead the industry, lending and equity based crowdfunding are expected to play an increasing role in the future. Peer-to-peer lending can be attractive for small businesses that lack collateral or a credit history to access traditional bank lending. Equity crowdfunding can provide a complement or substitute for seed financing for entrepreneurial ventures and start-ups that have difficulties in raising capital from traditional sources.

23. The development of the Web 2.0 has been critical to the diffusion and evolution of crowdfunding platforms and practices and efficient banking systems have eased their development, by providing the infrastructure for payments, as well as information about the creditworthiness of the entrepreneurs. However, while the pace of technological developments has enabled a rapid diffusion of crowdfunding, the regulatory environment has limited the expansion of its use, especially for securities-based crowdfunding, which is still not legal in some countries. Hence, in recent years, crowdfunding has received close attention by regulators in some OECD countries. The exemptions to general rules to secure investors or the implementation of ad hoc regulation are expected to facilitate the growth of the industry.

With the support of public programmes, hybrid instruments are increasingly available to lower-tier SMEs

24. Hybrid instruments, which combine debt and equity features into a single financing vehicle, have developed unevenly in OECD countries. Hybrid techniques represent an appealing form of finance for firms that are approaching a turning point in their life cycle, when the risks and opportunities of the business are increasing, a capital injection is needed, but they have limited or no access to debt financing or equity, or the owners do not want the dilution of control that would accompany equity finance. This can be the case of young high-growth companies, established firms with emerging growth opportunities, companies undergoing transitions or restructuring, as well as companies seeking to strengthen their capital structures. At the same time, these techniques are not well-suited for many SMEs, as they require a well-established and stable earning power and market position, and demand a certain level of financial skills.

25. The use of hybrid instruments, such as mezzanine finance, which lies in the middle of the investors' risk/return spectrum (Table 2), has followed divergent patterns in the aftermath of the crisis. The commercial market contracted and, in some countries where private lenders were in retreat, recourse to officially supported mezzanine credit grew substantially, as governments stepped in to fill the void. However, throughout the recovery, as banks retreated from lending to non-investment grade companies, debt financing targeting private capital markets has been increasing.

Table 2. Comparison of mezzanine finance and other financing techniques

	Senior debt	Mezzanine	Equity
Economic perspective	Debt	Equity	Equity
Legal perspective	Debt	Debt	Equity
Ranking	Senior	Contractually subordinated	Junior
Taxation	Debt interest deductible	Debt interest deductible	Tax on capital
Covenants	Comprehensive restrictions	Tracks senior, but looser	None
Security	Yes -1 st ranking	Yes -2 nd ranking	No
Investor's involvement in management	No direct involvement	Moderate involvement; board seats	Direct involvement
Purpose	Contractually specified	Not specified	Not specified
Term	4-5 years	5-10 years	Open ended
Interest Costs	Cost of funds + 255-350 basis points	150-300 basis points above senior	None
Repayment	Amortizing from cash flow	Bullet* upon exit or at maturity	None
Warrants	None	Almost always	None
Total Expected Return	5-13%	13-25%	>25%

* The payment for the principal is not made over the life of the loan, but rather as a lump-sum payment at exit or maturity.

Source: adapted from Credit Suisse (2006), "Mezzanine Finance. A hybrid instruments with a future", Economic Briefing no. 42

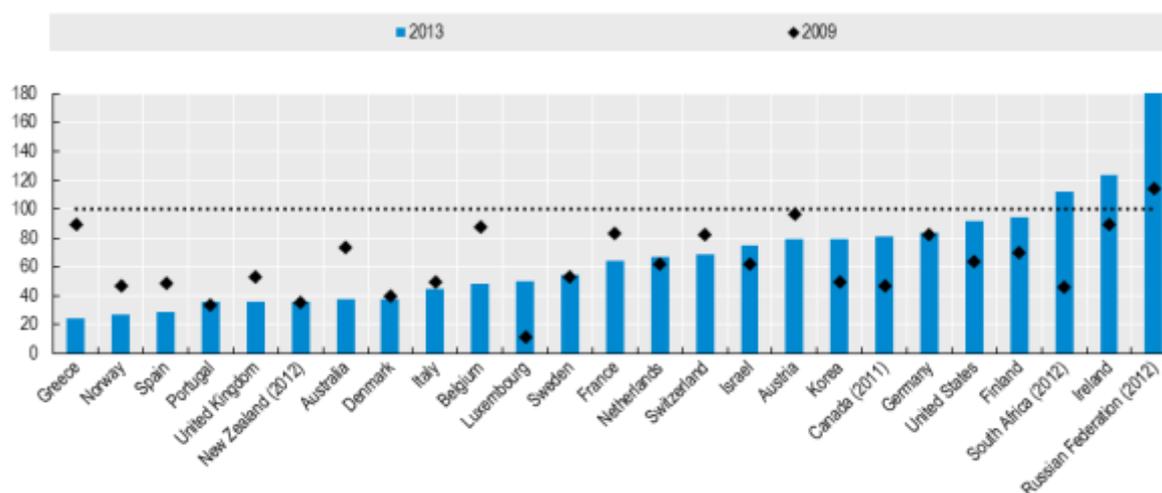
26. In recent years, with the support of public programmes, it has become increasingly possible to offer hybrid tools to SMEs with lower credit ratings and smaller funding needs than what would be the practice in private capital markets. Governments and international organizations mainly intervene through: i) participation in the commercial market with investment funds that award mandates to private investments specialists; ii) direct public financing to SMEs under programmes managed by public financial institutions; iii) guarantees to private institutions that offer SMEs the financial facility and; iv) funding of private investment companies at highly attractive terms.

Private equity investment has developed substantially in recent decades, partly offsetting stagnation in public markets

27. Equity finance is key for companies that seek long-term corporate investment, to sustain innovation, value creation and growth. Equity financing is especially relevant for companies that have a high risk-return profile, such as new, innovative and high growth firms. Seed and early stage equity finance can boost firm creation and development, whereas other equity instruments, such as specialized platforms for SME public listing, can provide financial resources for growth-oriented SMEs.

28. Across OECD and non-OECD countries, private equity investments have developed substantially over the last two decades. This has partly offset the stagnation in public markets, although, following the global financial crisis, exit options have become more challenging for private equity investors. In particular, venture capital and angel investing have been providing new financing opportunities for innovative, high growth potential start-ups, mainly, though not exclusively, in high-tech fields. Their role has been increasing over the last decade, as the industry has become more formalized and organized, including through syndicates, associations and networks, although the global financial crisis severely affected the venture capital industry. In 2013, in most countries the level of venture capital investments was still below the pre-crisis level, and, in some cases, below the level it reached in 2009 (Figure 2).

Figure 2. Venture Capital trends (2007 = 100)



Source: OECD (2014), Entrepreneurship at a Glance 2014, OECD Publishing.

29. Venture capital funds and business angels are characterized by different motivations, targets, scale and operating models, but are highly complementary in the financing continuum for early stage firms. Business angels need a well-functioning VC market to provide the follow-on finance that some of the businesses they support will require. At the same time, a well-developed angel market can create more investment opportunities and increase the deal flows for VCs.

30. Policy makers have placed increasing attention on these equity markets, as a way to mobilise financial resources and entrepreneurial expertise towards innovative ventures. The policy mix has been largely composed of supply-side measures, such as tax incentives, direct investment and co-investment, support to industry networks and associations, to increase visibility and scale and favour match-making with entrepreneurs. To a lesser degree, policies target also training, mentoring and coaching for investors. As in the case of other instruments, the demand side has received less policy attention and resources, although countries are increasingly implementing measures that target the skills of existing or would-be entrepreneurs.

Public listings of SME equity have the potential to provide funding for innovative and high-growth SMEs, but markets are currently small

31. For decades, private market participants and officials have been seeking to encourage the development of specialized exchanges or similar trading platforms to satisfy the demand of SMEs for equity finance. Public listing of SME equity through primary and secondary issuance has the potential to provide funding for a company's growth and can support subsequent debt financing. Existing SME owners can realise their capital gains and tap a wider investor universe, including retail investors and sophisticated long-term institutional investors.

32. A number of equity markets targeting smaller listings have been established in different parts of the world. Compared to generic stock exchanges, specialized platforms for SMEs, or "new markets", offer more flexible listing criteria, eased disclosure requirements and comparatively low admission cost so as to cater to SMEs. At the same time, new markets typically adopt operating practices to preserve investor interest and market integrity.

33. Despite their potential, the share of SME financing provided through capital markets is currently very small. Important obstacles to the wider use of public equity for SMEs remain to be resolved. In addition to cost, red tape and reporting requirements, cultural factors and management practices also constitute challenges for SMEs. Lack of confidence to go through the offering process, fear of being exposed to share price volatility, aversion to sharing sensitive information, but also lack of education around the process of listing and life after an IPO are other reasons for SME reluctance to join equity capital markets. In addition, entrepreneurs tend to be unwilling to relinquish ownership or control of their business or accept potential lock-in periods upon listing.

34. On the investor side of the market, financiers are confronted with high monitoring costs relative to the level of investment, regulatory obstacles and investor protection considerations. Low levels of liquidity in SME growth markets (inherent in the SME asset class) act as one of the main deterrents to investment in public SME equity.

35. Policy has sought to mobilize retail investment to address the lack of liquidity in SME equity markets, for instance by increasing the threshold level at which public disclosure and related requirements kick in, or by providing tax breaks for investment in unquoted companies which may subsequently list. Recent regulatory approaches recognize that these platforms may require tailored regulation and infrastructure, to facilitate access by SMEs while preserving investor interest. In some countries, new markets offer growth-oriented entrepreneurs dedicated services, such as the introduction to experienced investors, or the possibility to retain a higher level ownership than a traditional IPO.

3. KEY CHALLENGES AND POLICY IMPLICATIONS

The challenges to SME uptake of alternative financing instruments need to be addressed...

36. Common obstacles exist for the SME sector to fully reap the benefits of a more diversified financial offer through alternative financing instruments. Policy makers and stakeholders need to address these challenges if the increasingly complex financial system is to serve the needs of the real economy.

... by improving SME skills and strategic vision for their financing needs...

37. SME skills and strategic vision are a key ingredient in any effort to broaden the range of financing instruments. The limited awareness and understanding about alternative instruments on the part of start-ups and SMEs have limited the development of these markets. It is not only a matter of increasing knowledge about individual instruments, but also supporting SMEs in developing a long-term strategic approach to business financing, that is, understanding how different instruments can serve different financing needs at specific stages of the life cycle, the advantages and risks implied, and the complementarities and possibility to leverage these sources.

38. It is also necessary to improve the quality of start-ups' business plans and SME investment projects, especially for the development of the riskier segment of the market. In many countries, a major impediment to the development of equity finance for young and small businesses is the lack of "investor-ready" companies. Furthermore, SMEs are generally ill-equipped to deal with investor due diligence requirements. Indeed, an increasing concern about the lack of entrepreneurial skills and capabilities and low quality of investment projects is driving more policy attention to the demand side, although supply-side policies are still prevalent. This includes measures such as training and mentoring.

... designing effective regulation that balances financial stability and the opening of new financing channels for SMEs...

39. The regulatory framework is a key enabler for the development of instruments that imply a greater risk for investors than traditional debt finance, from asset-based finance to equity financing. Thus, designing and implementing effective regulation, which balances financial stability, investors' protection and the opening of new financing channels for SMEs, represents a crucial challenge for policy makers and regulatory authorities. This is especially the case given the rapid evolution in the market, resulting from technological changes as well as the engineering of products that, in a low interest environment, respond to the appetite for high yields by financiers. New financing models are emerging that may engage relatively inexperienced investors, such as in the case of crowdfunding, or in which the misalignment of incentives may place at risk the stability of the system, which is made more vulnerable to risk by an increased interconnectedness of financial markets.

40. Securitization is a case in point in this regard. Recent regulatory initiatives address pitfalls brought to the fore during the global financial crisis, such as the misalignment of interests between originators and investors and of regulatory capital with credit risk, as well as the lack of due diligence by investors. However, regulatory reforms intended to make the financial sector safer are perceived to be unduly onerous by many investors, who are withdrawing from the market. Also, the lasting uncertainty arising from expected regulatory revisions creates disincentives to investors and hampers the re-launch of the market. Certainty is part of a sound regulatory framework for investors.

41. Also, efforts should be made to foster the wider use of public equity for SMEs, which is currently held back by high costs, regulatory burdens, lack of liquidity and trading practices that create disincentives for intermediaries. The right balance between administrative and regulatory burden and due diligence needs to be achieved, so that the flexibility provided to SMEs does not compromise investor protection, integrity of market participants, corporate governance or transparency. Policy should provide incentives that encourage capital market participants to take a longer-term approach, and offer additional services to

growth-oriented entrepreneurs. Creating the right ecosystem for public equity for SMEs will also support the development of other, non-traditional SME equity instruments such as equity private placements, equity crowdfunding, listed funds (with potential co-funding and risk sharing between the private and public sectors), and corporate venturing.

... developing information infrastructures to reflect more accurately the level of risk associated with SME financing and encourage investors' participation ...

42. Addressing information asymmetries and increasing transparency in the markets are priorities to boost the development of alternative financing instruments for SMEs. Information infrastructures for credit risk assessment, such as credit bureaux or registries or data warehouses with loan-level granularity, can reduce the perceived riskiness investors fear when approaching SME finance and help them identify investment opportunities. More reliable information about risk may also help reduce the financing costs which are typically higher for SMEs than for large firms. The higher risks and costs stem from the large heterogeneity and opacity of the SME sector, with entrepreneurs often less prone, willing or able to share risk-sensitive information.

43. In some countries, policies seek to address the information gap between SMEs and potential investors by facilitating their direct interaction, with different degrees of public engagement, from awareness campaigns to brokerage and match-making. In the business angel market, for instance, public action has largely aimed at improving information flows and networking opportunities between financiers and entrepreneurs. In some cases, however, the facilitation efforts have not produced the desired results, due to the lack of maturity of local markets, i.e. little scale or lack of investor-ready companies. This highlights the need for a policy mix that takes into account existing limitations on both the supply and the demand sides.

... implementing policies that leverage private resources and develop appropriate risk-sharing mechanisms with the private sector...

44. For some hybrid or equity instruments, policy makers face the challenge of kick-starting the offer for SMEs, or extending it to SMEs with lower credit ratings and smaller financial needs than those usually served by private investors, while ensuring long-term sustainability. In the aftermath of the global financial crisis, as private investors withdrew from some market segments, public policies have also aimed at sustaining these markets, with governments stepping in to fill, at least in part, the financing gap for innovative or growth-oriented enterprises. As a result, the public share of funding in these higher risk segments has significantly increased. A key challenge now is to leverage private resources and develop appropriate risk-sharing mechanisms with private partners.

... and improving the evidence base.

45. In spite of their growing importance for financiers and SMEs, the evidence about the use of these various tools by SMEs, and how different instruments respond to their needs, is currently patchy. The lack of hard data on non-debt financing instruments represents an important limitation for the design, implementation and assessment of policies in this area. This limitation is particularly critical when seeking to take account of SME heterogeneity in the process of policy design. Micro data and micro level analysis

are essential to improve understanding about the different needs of the SMEs sector and may help to better understand the potential and challenges of new business models emerging in the financial sector.

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