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FOCUS ON

REPORT ON EXPERT GROUP MEETING ON ENTERPRENEURIAL FINANCE

26-27 March 2015 New York USA

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This report has been developed by the Investment and Technology Unit (ITU) of UNIDO's Business, Investment and Technology Services Branch (BIT). It has been written on the basis of the presentations, contributions and exchanges of good practices by participants on the Expert Group Meeting on Entrepreneurial Finance organized by UNIDO in co-collaboration with UNDESA Financing for Development (FFD) Office and UNCDF, which was held in New York, USA on March 26 and 27, 2015. Contribution of the practitioners and experts participating on the EGM, from broad range of public and private sector organizations, including United Nations (UN) agencies, international financial institutions (IFI), UN Member States, non-governmental organizations (NGO), research organizations, and the private sector have been critical for the creation of the report.

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EXPERT GROUP MEETING ORGANIZERS

UNIDO

UNIDO aspires to reduce poverty through inclusive and sustainable industrial development. According to its mandate, UNIDO seeks to enable the poor to earn a living through productive activities, thus to find a path out of poverty. The Organization provides a comprehensive range of services customized for developing countries and transition economies, ranging from industrial policy advice to entrepreneurship and SME development, and from technology diffusion to sustainable production and the provision of rural energy for productive uses. Within the framework of the enterprise creation and investment promotion programs, UNIDO addresses the existing SMEs financial gap by assisting Governments and National Institutions to strengthen their financial and non-financial business development services. In the area of financial services, UNIDO delivers advisory services and participates in the development of revolving funds, equity and guarantee schemes that are being implemented by national micro and small financial institutions.

UNITED NATIONS
INDUSTRIAL DEVELOPMENT ORGANIZATION

UNDESA - Financing for Development Office

The principal function of the Financing for Development Office in UN DESA (FFDO) is to provide effective substantive secretariat support for sustained follow-up within the United Nations to the agreements and commitments reached at the International Conferences on Financing for Development, as contained in the 2002 Monterrey Consensus and the 2008 Doha Declaration on Financing for Development, and financing for development-related aspects of the outcomes of major United Nations conferences and summits in the economic and social fields, including the United Nations Conference on Sustainable Development, as well as the United Nations development agenda beyond 2015. As part of this function, the Financing for Development Office has collaborated with experts from public and private sectors on a range of issues pertaining to inclusive finance, entrepreneurship and SME development. Among other things, FFDO has organized meetings and produced research on issues such as strengthening access to finance for SMEs, the role of diasporas in promoting entrepreneurship in their countries of origin, and measures to encourage the development of the domestic private sector in developing countries.

UNCDF

United Nations Capital Development Fund (UNCDF) is the United Nations' capital investment agency for the world's 48 least developed countries (LDCs). It creates new opportunities for poor people and their communities by increasing access to financial services and investment capital. It provides seed capital in the form of grants and loans, as well as technical support to help financial service providers reach increased numbers of poor households and small businesses. Over 50 percent of the clients from these institutions are women. The organization also helps local governments finance capital investments for infrastructure, such as water systems, feeder roads, schools, and irrigation schemes that will improve poor peoples' lives. Its programmes are designed to catalyze larger investment flows from the private sector, development partners, and governments, to achieve significant impact.

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INTRODUCTION: ENTREPRENEURIAL FINANCE

Access to adequate capital is one of the biggest hurdles in starting and growing any business and is viewed as a primary prerequisite for accelerating entrepreneurship, enterprise formation, and industrial development; self-sustaining job, income and wealth creation. Over the years, a number of initiatives aimed at facilitating access to finance of small and medium enterprises (SME) have developed around the world and deployed with varying degrees of success. While some progress has been achieved, all available evidence clearly suggests that difficulties do persist and this calls for a fundamental re-examination of financing models and the prerequisites for their success.

The issues affecting entrepreneurs' access to finance were discussed at an Expert Group Meeting (EGM) on Entrepreneurial Finance that brought together practitioners and experts in the field of entrepreneurial finance, with the objective of exchanging experiences and lessons learned. The focus of the EGM was on the financing of SMEs, with particular attention paid to women-owned SME and youth-led enterprises.

Organized by UNIDO in co-collaboration with UNDESA Financing for Development (FFD) Office and UNCDF, the EGM was held in New York on March 26 and 27, 2015. The EGM included: (i) an opening session with introductory remarks from UNDESA FFD, UNIDO, UNCDF, and the SG's Envoy on Youth; (ii) the presentation of a background paper on good practices in entrepreneurial finance; (iii) several plenary sessions devoted to the presentation and discussion of various initiatives on entrepreneurial finance and related topics; and (iv) two parallel thematic group discussions focusing on selected aspects. The EGM agenda is attached in Annex A.

The EGM was attended by representatives of a broad range of public and private sector organizations, including United Nations (UN) agencies, international financial institutions (IFI), UN Member States, non-governmental organizations (NGO), research organizations, and the private sector. The list of participants is attached as Annex B. The presentations and other materials distributed by participants are available upon request.

This report summarizes the evidence presented and the discussions held during the EGM. The report is structured as follows:

Section 2 sets the stage, by introducing key concepts in entrepreneurial finance;

Section 3 presents evidence on the extent of the access to finance constraint;

Section 4 recaps the salient features of the most commonly used financial instruments;

Section 5 summarizes the main themes emerged during the discussion;

Section 6 illustrates the policy and operational recommendations;

Section 7 includes Annexes.

2. KEY APPROACHES IN ENTREPRENEURIAL FINANCE

Entrepreneurial finance has to do with the mobilization of funding for the financing of entrepreneurial ventures. It is a broad concept, as it encompasses a wide range of financial instruments aimed at providing different forms of funding to different types of enterprises, at different stages of their development. The basic concepts are briefly illustrated in the following paragraphs.

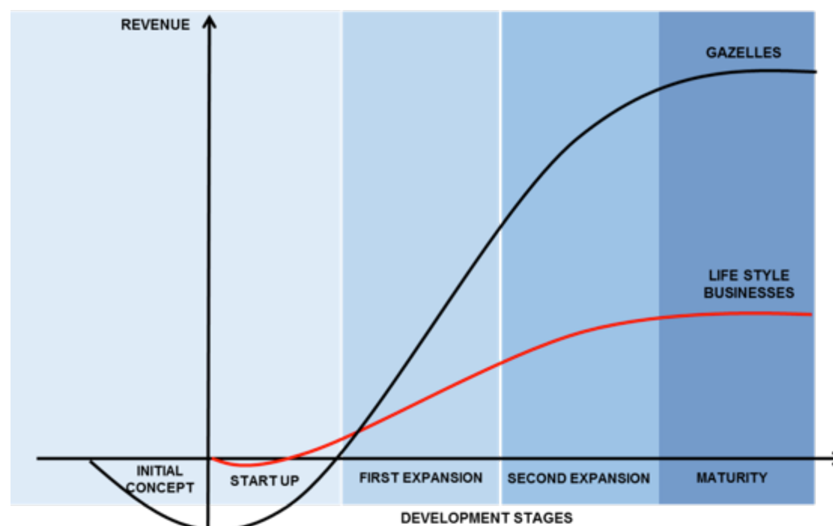
2.1 Types of Enterprises

SME are a highly heterogeneous class and firms can be categorized along a variety of dimensions, such as market orientation (e.g. domestic vs. export market), ownership and management structure (e.g. family-owned and managed firms vs. manager-run firms), etc. A popular categorization, frequently referred to during the EGM, contrasts growth oriented firms, the so-called 'gazelles', with 'life style' businesses. Gazelles are firms with a strong inclination and potential for growth, and in fact they are commonly defined in terms of growth rates over a certain period of time (e.g. at least 10% annual growth in sales and/or employment over a period of three to five years). In contrast, lifestyle businesses are primarily intended to provide a source of income to their owners/managers and are much less concerned with growth.[1] The great diversity of the SME universe is an important element to be considered from an entrepreneurial finance angle, because different typologies of SME have different financing needs and/or display different inclinations towards the utilization of various financial instruments.

2.2 Stages of Development

Firms are also often segmented by stage of growth. A popular categorization makes reference to: (i) firms in early development stages, which include both the proof of concept and start-up phases; (ii) firms in a growth or expansion stage, which can take place in successive leaps (hence, the expressions 'first expansion', 'second expansion', etc.); and (iii) firms that have reached their maturity. In the early stages, firms face a mismatch between the ability to generate and the need for funds, a phenomenon commonly referred to as the 'valley of death'. However, the depth of the 'valley' depends upon the nature of the businesses. In the case of innovative firms, i.e. those with a potential to become 'gazelles' (e.g. developers of new IT applications), significant resources are needed before reaching the point of trading profitably, and failure to cope with this gap may well result in failure. However, if the 'valley' is bridged, rapid growth is expected to ensue at the expansion stage. Instead, in the case of more traditional activities, i.e. those likely to become 'life style businesses' (e.g. retail trade or simple artisanal activities), early stage development requires fewer financial resources (the proof of concept phase is often nonexistent and startup is relatively simple), but subsequent growth rates are much less spectacular. A diagrammatic presentation of these two 'growth models' is provided in Exhibit 1.

EXHIBIT 1 FINANCING AND STAGES OF GROWTH



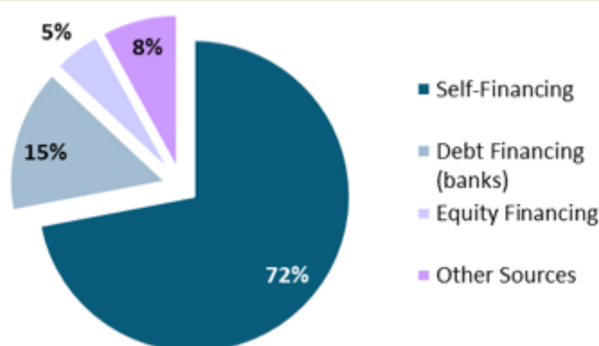
[1]The origins of this distinction can be traced back to a study carried out in the late 1970s showing that the bulk of new employment generated by SMEs was attributable to a limited number of firms. See Birch D L, The Job Generation Process, Massachusetts Institute of Technology, 1979. For a recent overview, see the special section on high growth firms published in the online journal Industrial and Corporate Change, January 2014. The publication is accessible through http://icc.oxfordjournals.org/content/23/1/91.full.

2.3 Main Sources of Funding

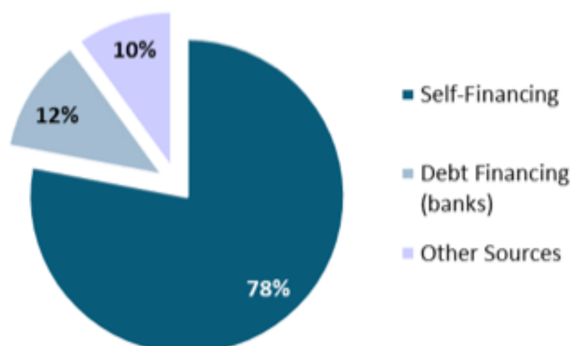
Irrespective of enterprise types and stages of growth, firms predominantly rely on self-financing, i.e. on internally generated financial resources. Data from World Bank Enterprise Surveys (WBES), show that 'internal sources' account for 72% of funds required for investments and for 78% of working capital needs. Overall, 'external sources' of finance account for just about one quarter of all financing needs. Debt financing, in the form of bank loans (see Exhibit 2), is the most important external source of funding (15% for investments and 12% for working capital), followed at great distance by equity financing, which plays a role only for investments. Other sources of external financing include supplier credit, leasing and factoring.

EXHIBIT 2 MAIN SOURCES OF FUNDING AND FINANCIAL INSTRUMENTS - OVERVIEW [2]

Sources of Funding for Investments (%)



Sources of Funding for Working Capital (%)



Source: World Bank Enterprise Surveys

Debt financing essentially consists of loans from commercial banks and other financial institutions, such as development banks. Loans are usually categorized according to their duration (or 'maturity') and purpose, with short term loans (normally less the one year) typically used for working capital needs and medium/long term loans used to finance investments. The provision of debt financing to SME is supported by governments or donors/IFI through the so called 'credit lines', i.e. financing facilities whereby funds are provided to commercial or development banks for further on lending to firms. In certain cases, loans are provided directly to SME by dedicated government bodies or in the framework of special donor/IFI initiatives.

Equity financing involves the injection of risk capital into a business. Unlike debt financing, equity financing also impacts on the ownership structure of the firm, as the capital injection involves a transfer of shares in favor of the financier. Equity financing is provided by private equity (PE) funds, established with financial resources made available by institutional investors (insurance companies, pension funds, etc.) and managed by specialized operators, the so-called 'fund managers'. Venture capital (VC) funds are a subset of private equity funds, targeting investments in high growth firms in the early stages of development. Another sub-category of PE funds is that of the 'impact funds', which seek to reconcile financial returns with the achievement of social and environmental objectives. The development of equity financing is supported by governments and donors/IFI through the participation in the capital of PE/VC funds and, sometimes, the provision of funds for technical assistance.

Other Financial Instruments: this last category includes three main financial instruments, namely: (i) supplier credit, also referred to as 'trade finance'; (ii) leasing and factoring, often commonly referred to as 'asset based financing'; and (iii) grants. In the case of supplier credit, financing is not provided by a bank or another financial institution but by suppliers of goods or services, which accept a deferred payment. Supplier credit can be relied upon for both for investment financing and working capital purposes. Governments and donors/IFI may support the use of trade finance by providing guarantees to protect the supplier against the risk of non-payment. Leasing and factoring transactions are handled by specialized financial operators, often subsidiaries of commercial banks. Leasing is typically used to finance investments in movable assets (e.g. vehicles, small scale equipment) while factoring is intended to provide working capital funds, through the sales of accounts receivables. Leasing and factoring companies may be supported by governments and donor/IFI through the provision of funding, typically channeled through credit lines as in the case of debt financing. Grants involve the direct subsidization of SME by governments or donors, more rarely by IFI. Grant funding is typically reserved to firms active in areas considered of high social value (e.g. development of eco-friendly products) or promoted by special groups (e.g. disadvantaged youth).

BOX 1 - THE ISSUE OF COLLATERAL

The granting of a loan is usually conditional upon the availability of some collateral, which is intended to protect the bank in case of default. A collateral can be in the form of: (i) a pledge on movable assets (e.g. on a specific piece of equipment), and/or (ii) a mortgage on real estate (e.g. on a building or land holding). According to WBGES data, 78% of loans worldwide are collateralized and the average value of goods/property provided as collateral is 195% the value of the loan. Predictably, these values are somewhat lower in HIC (70% and 164%), but in general there are no major variations across regions. The discrepancy between the value of the loan and that of the collateral is due to the fact that the actual recovery value of the goods/property seized and sold in case of default is generally lower than the initial cost. The mobilization of sufficient collateral is one of the problems most frequently mentioned by SMEs in accessing finance. In order to alleviate the problem, governments and donors/IFI have sometimes devised credit guarantee mechanisms that at least partially reduce the need to provide collateral.

[2] WBGES data refer to surveys covering over 130,000 firms across 135 countries. Data refer to all firms, not just SMEs. However, as SMEs account for the large majority of firms surveyed, the data presented can be regarded as good approximation of the situation for SMEs. For details, see http://www.enterprisesurveys.org/.

EXHIBIT 3 SUMMARY OF FINANCIAL INSTRUMENTS, KEY PLAYERS AND GOVERNMENT & DONOR/IFI SUPPORT

Financial Instrument	Purpose	Key Actors	Type of Government and IFI/ Donor Support
» Debt Financing (loans)	» Investment and working capital financing	» Commercial banks and Development banks	» Credit lines Credit guarantees
» Equity Financing (PE/VC)	» Investment financing	» Fund Managers	» Contributions to PE/VC funds capital
» Trade Finance (supplier credit)	» Investment and/or working capital financing	» Suppliers of goods and services	» Insurance against non-payment
» Asset Based Financing (leasing and factoring)	» Investment (leasing) and working capital (factoring) financing	» Leasing and factoring companies (often subsidiaries of commercial banks)	» Credit lines
» Grants	» Mostly, investment financing	» Government agencies and/or donors, acting directly or indirectly	

2.4 Entrepreneurial Needs

Small and medium enterprises (SMEs) play a vital role for job creation and therefore contribute to overall development and poverty reduction. However, as pointed out by Mr. Krishnan Sharma (UNDESA, FFD Office) in the opening session of the Expert Group Meeting, access to finance is still a major problem for SMEs: in emerging markets, the financing gap is estimated at US$ 2.6 trillion. In order to tackle the problem, a comprehensive approach is required. First, it is essential to strengthen the capacities of financial institutions and intermediaries, so that they can effectively address the needs of underserved market segments. Second, government policy must remove legal and regulatory obstacles that continue to hamper access to finance. Finally, in defining operational tools, it is important to distinguish between various types of businesses, e.g. growth-oriented vs. survival entrepreneurs, as they have different needs and require different services. In this context, special assistance must be provided to informal sector entrepreneurs and rural entrepreneurs.

The linkage between access to finance and entrepreneurship development was highlighted by Mr. Paul Maseli (Director, UNIDO Office New York). The emergence of a lively private sector is a key condition for achieving sustainable and inclusive growth and, in particular, to address the issue of youth unemployment. Yet, access to finance remains a major issue for the advancement of entrepreneurship, and in particular, youth and women are often excluded from traditional banking services. In fact, even in countries where the financial sector features high level of liquidity, marginalized groups often have difficulties in accessing funding. It is therefore crucial to identify mechanisms that can be adapted to different contexts and that can provide the much-needed access to finance to structurally underserved groups. At the same time, while financial services are crucial in certain stages of the enterprise development process, non-financial support is also needed to ensure that whatever financial resources are accessed they can be put to good use.

The need for inclusive financial mechanisms was highlighted by Mr. Tucker (Deputy Director, Financial Inclusion Practice, UNCDF). In its work, UNCDF places a strong focus on young people and engages in targeted initiatives such as: promotion of financial services for youth, youth access to saving schemes as a way into the formal banking sector, projects that proof the business case for financing youth, as well as a number of non-financial services to support young entrepreneurs. Given the important role played by SMEs for job creation and local development, the traditional emphasis on micro finance has to transition into a more holistic approach, capable of delivering results for various typologies of firms. In this context, UNCDF is actively promoting forms of public private partnership with key financial sector players, which also ensures a higher degree of sustainability once specific interventions are completed. UNCDF is also engaged in support to local authorities to promote an enabling environment and transform economic opportunities dynamic private enterprises through public and PPP investments (markets, bus station, roads and storages).

The theme of youth entrepreneurship was further developed by Mr. Ahmad Alhendawi (UN Secretary General's Envoy on Youth). Indeed, improving access to finance alone is not enough, as there is need for an enabling environment that facilitates the emergence and consolidation of new entrepreneurial ventures. In particular, the education system can play a major role, by providing the skills required to equip young entrepreneurs with the necessary entrepreneurial spirit as well as crucial tools to enable them to set up their business. Likewise, the existence of a conducive legal framework constitutes a major precondition for the development of youth entrepreneurship. Regarding financial mechanisms, it is necessary to improve the 'targeting' of existing instruments, so as to avoid situations in which funds are available 'in principle' but de facto not accessible to young entrepreneurs. Furthermore, it is important to consider the challenges faced by entrepreneurs who, having successfully passed the start-up stage, are striving to expand and scale up their business.

It was noted that the EGM was taking place at a critical juncture, during the preparation of the Third International Conference on Financing for Development to be held in Addis Ababa in July 2015. The theme of access to finance is already present in the Zero Draft Document,[3] which inter alia emphasizes the need of "ensuring access to formal financial services for all, including the poor, women, rural communities, marginalized communities and persons with disabilities" (page 8). However, there is still considerable scope for reinforcing and operationalizing the message. Therefore, the EGM was regarded as an excellent opportunity to put forward more operational recommendations that could inform the ongoing negotiations.

[3] Zero Draft of the Outcome Document of the Third Financing for Development Conference, prepared by the Permanent Representatives of Norway and Guyana, March 16, 2015.

3. FIRMS' CONSTRAINTS RELATED TO FINANCE

While there is nearly unanimous consensus about the fact that SMEs as well as women and young entrepreneurs are at a disadvantage in accessing finance, the severity of the constraint shows some variation.

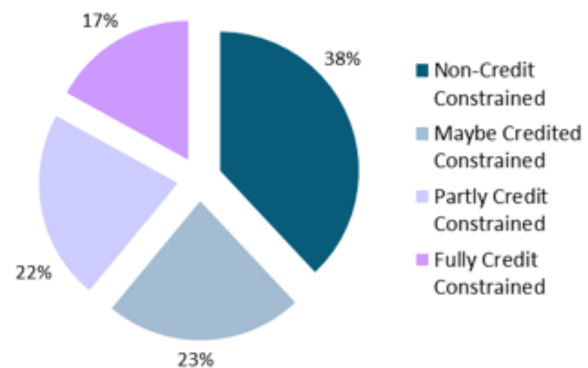
The economics literature on entrepreneurial finance has identified three main obstacles that may prevent SME from obtaining adequate financing.[4] These include: (i) the existence of marked informational asymmetries between small businesses and external providers of funds (banks, investment funds, etc.), which makes it difficult for the latter to differentiate adequately between 'good' and 'bad' firms; (ii) The intrinsic higher risk associated with small scale activities, because they operate in a more competitive environment, and because they have less capacity to withstand adverse developments (e.g. the owner/manager may run into health of personal problems, with disastrous consequences on the firm); and (iii) the existence of sizeable transactions costs in handling SME financing (e.g. the cost of processing a loan application or conducting a due diligence for equity investment is largely the same, irrespective of the amount of money involved).

The extent to which SME actually face difficulties in accessing finance is not easily measurable. Many studies make reference to subjective measures, i.e. the views voiced by SME through surveys, but this is likely to overestimate the severity of the access to finance constraint. An interesting example of a more objective measurement is provided by a recent study on bank lending, which is the predominant source of funding for SME.[5] Making use of a vast dataset from the World Business Environment Survey (WBES), the study found that worldwide, up to 39% of firms may be considered as fully or partly 'credit constrained', compared with 38% of firms non experiencing problems (non-credit constrained) and another 23% in an unclear position ('maybe credit constrained'). The study confirms that SME are a clear disadvantage compared with their larger counterparts, with nearly 50% of firms with fewer than 20 employees being fully or partly credit constrained (Exhibit 4). It is important to note that these figures are likely to underestimate the severity of the access to finance constraint, as WBES do not cover firms with fewer than five employees.

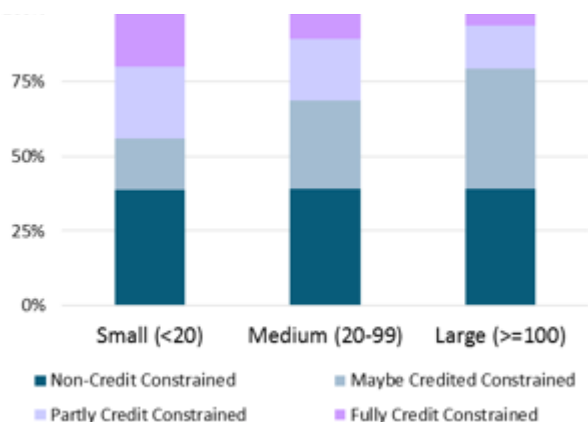
Disaggregated data at the regional level (Exhibit 5) show major variations in the severity of the access to finance constraints. Sub-Saharan Africa (SSA) and Middle East and North Africa (MENA) are clearly the regions where access to finance is more problematic, with well over 50% of all the firms fully or partly credit constrained. Europe and Central Asia (ECA) and Latin America and Caribbean (LAC) are the regions posting the best results, with one quarter/one third of firms facing significant constraints, while East Asia and Pacific (EAP) and South Asia (SAR) are in an intermediate position. Against such a diversity of results, a common trait is that the severity of the access to finance constraint is inversely correlated with size, with the share of fully or partly credit constrained firms being much higher in the case of small businesses in all the regions.

EXHIBIT 4 ACCESS TO FINANCE CONSTRAINT FOR SME - OVERVIEW

All Firms (%)



Firms by Size (%)

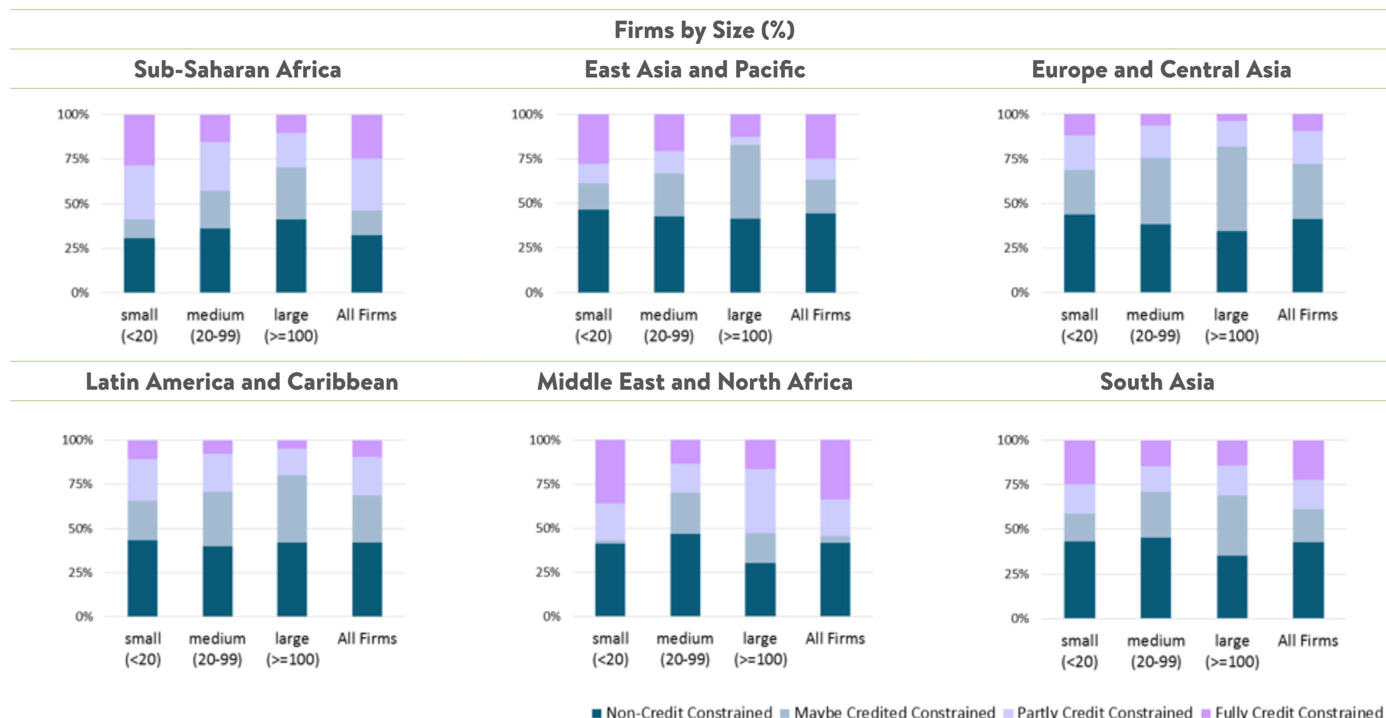


Source: Kuntchev and others (2014)

[4] The literature on obstacles to SME financing is enormous. Two classical references include Allen B and G Udell (2006) A More Complete Conceptual Framework for SME Financing, Journal of banking and Finance and Cull R and others (2005) Historical Financing of Small- and Medium Size Enterprises, National Bureau of Economic Research.

[5] Kuntchev V, R Ramalho, J Rodríguez-Meza and J S. Yang (2014) What have we learned from the Enterprise Surveys regarding access to finance by SMEs?

EXHIBIT 5 ACCESS TO FINANCE CONSTRAINT FOR SME – DISAGGREGATED DATA



Source: Kuntchev and others (2014)

Overall, the above data suggest that access to finance, both in general and for SME, is related to two main factors, the general level of development and the degree of sophistication of the financial sector, with the ECA and SSA regions being the polar cases. The exception to this pattern is the MENA region, where the difficulties in accessing finance cannot be linked to these factors (most countries are classified as middle income and banking sectors are well developed), but seem to be due to weaknesses in the legal and institutional framework and/or to the volatile political situation.

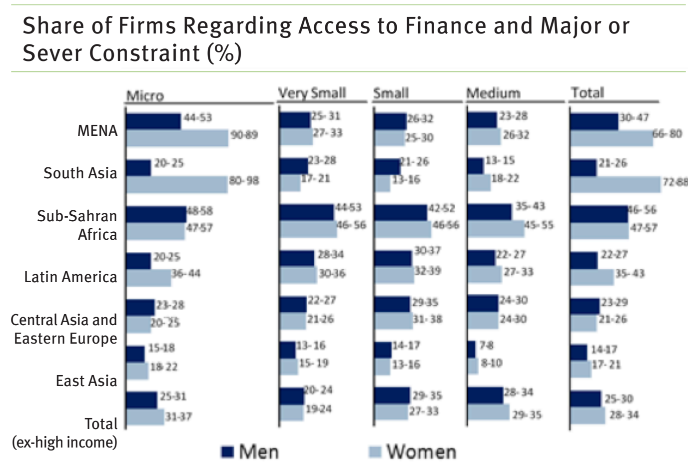
3.1 Access to Finance for Women-Owned Firms

Women are widely regarded to face greater difficulties than men in accessing financing, but the empirical evidence is not univocal, with different sources pointing in different directions. A recent econometric study making use of a rich dataset from Global Financial Inclusion surveys, found that women are less likely to use financial services and in particular less likely to have access to formal credit.[6] The study also found that legal discrimination against women and gender norms contribute to explain some of the difference. In countries where women face legal restrictions in their ability to work, head a household, choose where to live, and receive inheritance, women are less likely than men to own a bank account as well as to save and borrow.

A fairly bleak picture also emerges from the surveys investigating perceptions about business constraints. The results of a study carried by the International Finance Corporation (IFC), in the framework of the Global Partnership for Financial Inclusion (GPFI) and also based on WBES data, are presented in Exhibit 6 .[7] Overall, 31% of women-owned SME report access to finance as a major or severe constraint, compared with 28% of men-owned firms.[8] The financing constraints are perceived as more severe by women-owned firms across virtually all regions and enterprise sizes. Only in the ECA region, women-owned feel less financially constrained than their male-owned counterparts, while the difference is minimal in SSA. In contrast, the situation is particularly negative in the MENA and SAR regions, where the share of women-owned firms perceiving a major or severe constraint is much higher than that of male-owned SMEs.

EXHIBIT 6 ACCESS TO FINANCE CONSTRAINT FOR WOMEN OWNED FIRMS – FIRMS PERCEPTIONS

Share of Firms Regarding Access to Finance and Major or Sever Constraint (%)



Notes: data for MENA refer to only one country. In SAR, micro enterprises account for a disproportionate share of firms surveyed and heavily influence the total

Source: IFC (2011)

Perceptions are somewhat contradicted by data on actual behavior, which suggest a comparatively better situation. As shown in Exhibit 7, despite the prevailing pessimistic perceptions, female-owned SME are more likely than their male counterparts to apply for a loan. Even more importantly, loan approval rates are quite similar across gender lines, with women-owned firms achieving comparatively better results in the ECA and SSA regions. As shown in Exhibit 8, there are some differences across regions in terms of average loan size relative to the firm's income, but only in the MENA region women-owned

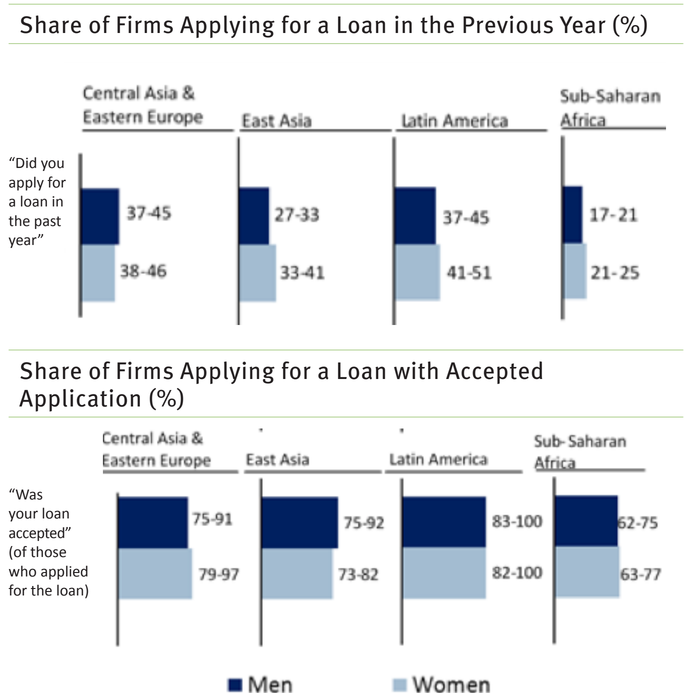
[6] Demirguc-Kunt A, L Klapper, and D Singer (2013) Financial Inclusion and Legal Discrimination Against Women - Evidence from Developing Countries.

[7] McKinsey/IFC (2011) Assessing and Mapping the Global Finance Gap for Women-owned MSMEs.

[8] Women-owned firms are defined as those firms having at least one female owner, irrespective of the share of ownership.

enterprises are at clear disadvantage. In terms of sectors, women-owned firms active in retail tend to get comparatively smaller loans whereas the situation is more favorable in manufacturing and services.

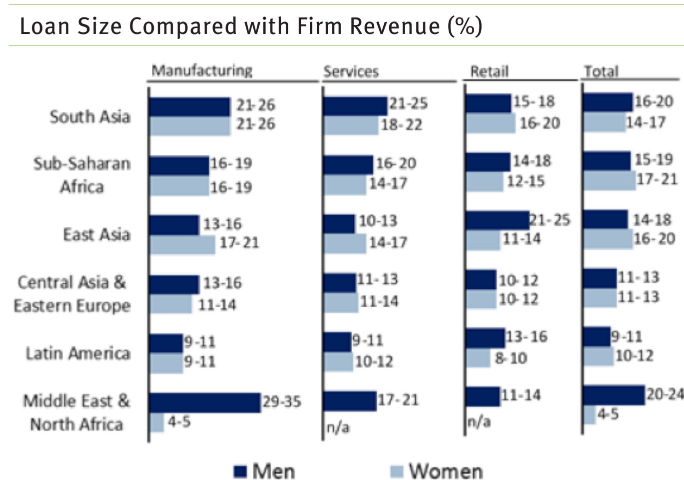
EXHIBIT 7 ACCESS TO FINANCE CONSTRAINT FOR WOMEN OWNED FIRMS – LOAN APPLICATION AND APPROVAL RATES



Notes: data for MENA and SAS are not available.

Source: IFC (2011)

EXHIBIT 8 ACCESS TO FINANCE CONSTRAINT FOR WOMEN OWNED FIRMS – RELATIVE SIZE OF LOANS



Notes: totals for sectors are not available

Source: IFC (2011)

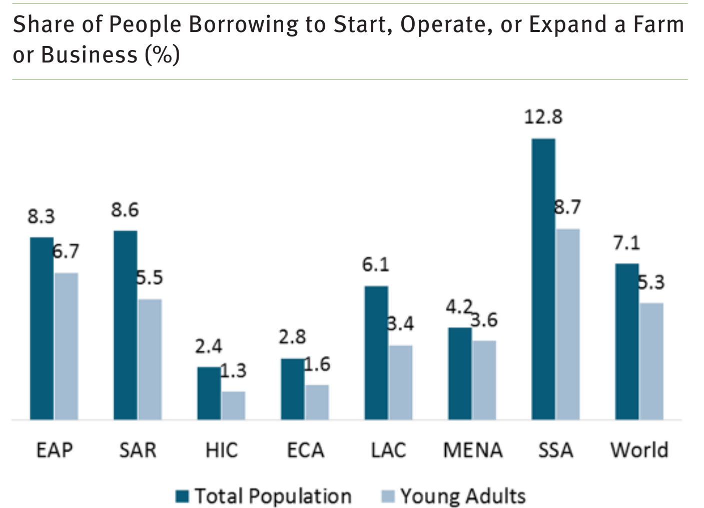
3.2 Access to Finance for Young Entrepreneurs

Raising finance is widely regarded as a major problem for young people and qualitative studies have often suggested that lack of finance is a significant constraint for youth-led businesses. For instance, a joint EU/OECD study found lack of financial support to be an important obstacle for young entrepreneurial individuals in European countries.[9] Similar conclusions can be found in case studies on developing countries conducted by Youth Business International (YBI).[10] However, these studies tend to rely on self-declarations or anecdotal evidence, and there are indications that the severity of the access to finance constraint may be over-reported. In fact, studies from the Global Entrepreneurship Monitor (GEM) have noted that "[w]hile access to finance is often the most visible constraint, it is not necessarily the primary inhibitor of youth entrepreneurial development."[11]

In the absence of comprehensive data on the access to finance for youth-led firms, it is difficult to understand the full dimension of the problem. It would be important to strengthen age disaggregated data collection on the side of banks and intermediaries, both on accepted borrowers and entrepreneurs who have not received a loan.

Some elements however, can be derived from the results of the Global Financial Inclusion (Global Findex) surveys carried out by the World Bank, which measure the proportion of people who have 'borrowed to start, operate, or expand a farm or business', with separate data for the total population (age 15+) and for young adults (age 15-24).[12] As shown in Exhibit 9, at the global level, the proportion of borrowers for business purposes among young adults is 5.3% compared with 7.1% in the total population. There are, however, significant differences across regions: in HIC, ECA and LAC the share of young borrowers is little more than half the corresponding value in the total population, whereas the difference is much less marked in EAP and MENA.

EXHIBIT 9 ACCESS TO FINANCE CONSTRAINT FOR YOUNG ENTREPRENEURS – BORROWING FOR BUSINESS PURPOSES



Source: Own elaborations based on Global Findex datasets

It is important to note that the above data does not provide a precise measure of the disadvantage faced by young entrepreneurs, because they do not take into account differences in entrepreneurship ratios across the various age groups. Information on entrepreneurship ratios can be retrieved from the GEM dataset, which includes data on early stage entrepreneurial activity as well as on established entrepreneurs.[13] As shown in Exhibit 10, entrepreneurship ratios for young adults are lower than those in the total population, with differences

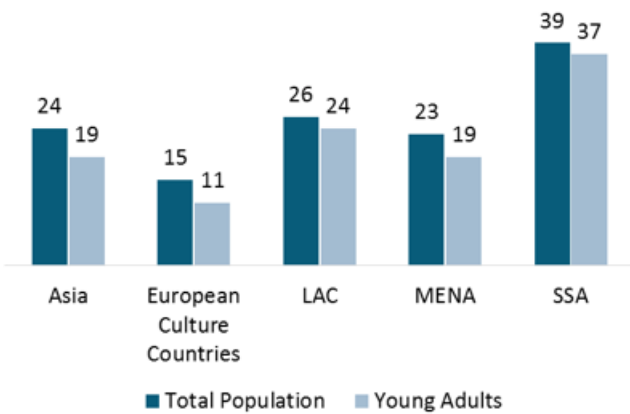
[9] EU/OECD (2012) Policy brief on youth entrepreneurship: Entrepreneurial activities in Europe.
[10] YBI (2010) Youth entrepreneurship - Beyond collateral.

[11] GEM (2015) Future Potential - A GEM perspective on youth entrepreneurship 2015.
[12] For information on the Global Financial Inclusion surveys see http://datatopics.worldbank.org/financialinclusion/home
[13] GEM data cover: (i) nascent entrepreneurs, i.e. those who have taken steps to start a new business, but have not yet paid salaries or wages for more than three months; (ii) new entrepreneurs, i.e. those who are running new businesses that have been in operation for between three months and 42 months; and (iii) established business owners, i.e. those who are running a mature business, in operation for more than 42 months. For details, see GEM (2015) Future Potential - A GEM perspective on youth entrepreneurship 2015.

ranging between two and five percentage points depending upon the region. While GEM and Global Findex figures are not perfectly comparable,[14] overall this evidence indicates that Global Findex data overstate the access to finance constraint for youth-led firms.

EXHIBIT 10 ACCESS TO FINANCE CONSTRAINT FOR YOUNG ENTREPRENEURS - ENTREPRENEURSHIP RATIOS

Share of Nascent, New and Established Entrepreneurs (%)



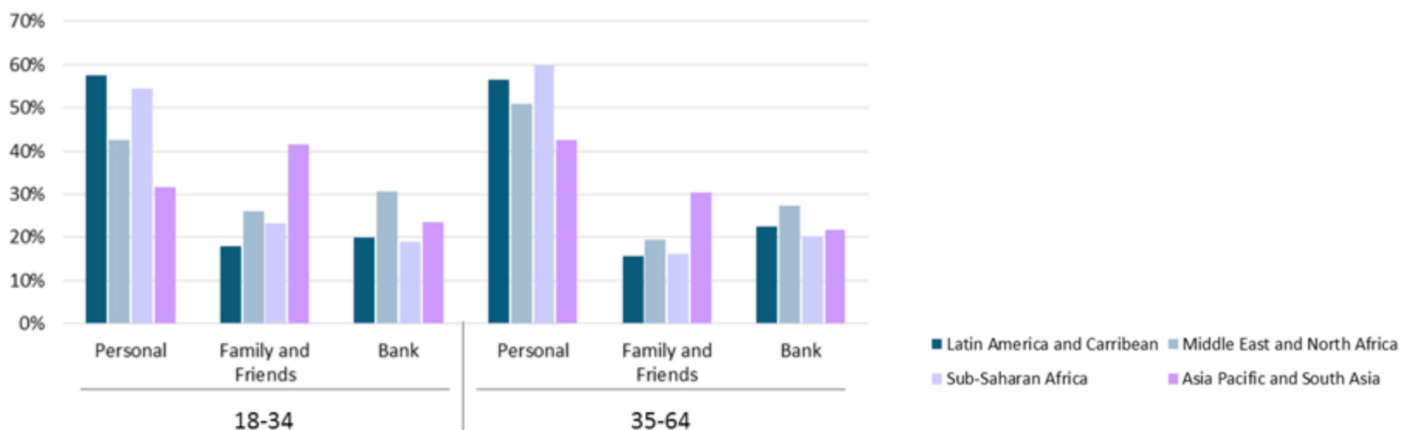
Source: Own elaborations based on GEM datasets

3.2.1 Young Entrepreneurs' Main Sources of Funding

Information on the main sources of funding utilized is provided in a recent report from Youth Business International (YBI) and the Global Entrepreneurship Monitor (GEM). The study shows that new entrepreneurs count mostly on personal savings and family & friends, although there are differences across regions (e.g. the use of bank financing is significantly higher in the Middle East and North Africa). Interestingly, the reliance upon the various sources of funding does not show major differences between young and adults (Exhibit 11).

EXHIBIT 11

Sources of the Majority of Money to Start Business (%)



[14] Both GEM and Global Findex data originate from large scale surveys, involving thousands of interviewees, which reduces the risk of bias. However, GEM covers a smaller number of countries, adopts a slightly different classification of countries (e.g. European Culture Countries only loosely correspond to the aggregate of HIC and ECA), and – most importantly – average values are unweighted averages, which means that smaller countries carry the same weight than larger ones.

4. MAIN FINANCIAL INSTRUMENTS

4.1 Credit Lines Contribute to Increase the Volume of Lending but Often Miss Target Beneficiaries

Credit lines are the most widely used instrument in SME finance, in both developed and developing countries. The volumes are quite significant. For instance, over the FY2006-2012 period, the World Bank Group (WBG) approved SME-targeted credit lines for some US$ 10 billion, of which US$ 7.5 provided by the IFC. The value of funding made available through SME credit lines by other IFI ranges from about US$ 4 billion for the European Bank for Reconstruction and Development (EBRD) and to US$ 1 billion in the case of the African Development Bank (AfDB). The main issue is that often the target groups are not well defined. As a result, there are many cases of credit lines that, despite being nominally targeted at SME, ended up funding large enterprises. Vivid examples are provided by a recent evaluation of WBG's assistance to SME. For instance, in the case of two large World Bank operations in Turkey (worth a total of some US$ 1.2 billion), the average loan size was, respectively, US$ 2.5 and 0.8 million, values scarcely attuned with the needs of a typical Turkish SME.[15] Obviously, there are also cases of well-targeted credit lines, effectively reaching out SME borrowers, with average loan sizes more aligned with the amounts typically sought by small enterprises (say, in the US$ 20,000 to US$ 200,000 range). Frequently, these credit lines are accompanied by the provision of technical assistance (TA) to help intermediary banks in the design and implementation of financial products and operating modalities tailored to SME needs. An example is provided in Box 2.

4.2 Direct Lending Schemes Allow for Better Targeting But at the Cost of High Transaction Costs

Direct lending schemes involve the provision of financing directly to SME or other intended beneficiaries, without the involvement of financial intermediaries. In principle, direct lending allows for a more targeted assistance, avoiding the problems that often afflict credit lines. However, direct lending typically entails high administrative costs relative to the typical size of financing. In the case of SMEs, direct lending is still used by governments both in developed and developing countries (e.g. the various industrial and agricultural development schemes managed by the Development Bank of Ethiopia). Instead, cost effectiveness considerations have induced donors/IFI either to discontinue their direct financing schemes (this is the case of IFC's African Enterprise Fund, Small Enterprise Fund, and South Pacific Investment Fund) or to broaden eligibility criteria, de facto abandoning the SME financing space (this is the case of the EBRD's Local Enterprise Facility).

Direct lending remains a commonly used tool in the case of special target groups, in particular young entrepreneurs. In particular, direct lending schemes for young entrepreneurs are quite common in OECD countries, with notable examples including the Start-Up Loans in the United Kingdom, the Futurpreneur loans in Canada, and the micro loans and prêt d'honneur granted by several organizations in France. This model is becoming increasingly common also in developing countries, as shown by Malaysia's Youth Entrepreneur Fund, Burkina Faso's Cred'Art

BOX 2 - KFW'S SME CREDIT LINES (VARIOUS COUNTRIES)

A review of twelve credit lines extended by the Kreditanstalt für Wiederaufbau (KfW) since the early 2000s, suggests a good ability to reach SME clients. In all cases but one, the target groups were clearly identified, either by making reference to national SME definitions or through the specification of detailed eligibility criteria. Accordingly, in ten cases the average value of loans was below € 100,000, with eight credit lines providing loans worth on average less than € 50,000. In most cases, funding was provided in local currency or borrowers had the possibility of choosing between local and hard currency. Terms and conditions were set by participating banks, although in most cases KfW required that loans be medium or long term. In most cases, the credit lines were accompanied by the provision of TA, consisting of capacity building and training or consulting services for market research and product design. In a few cases, TA support was also extended to final beneficiaries (e.g. assistance in business planning). The financial performance was generally positive, with only one credit line experiencing significant repayment problems (50% of the portfolio in arrears at the time of the evaluation). Data on the impact of funding on SME borrowers are available only in certain cases, but generally suggest a positive effect in terms of employment and sales.[16]

[16] Evaluations of KfW's credit lines can be accessed through https://www.kfw-entwicklungsbank.de/International-financing/KfW-Development-Bank/Evaluations/Results/

[15] WBG – IEG (2014) The Big Business of Small Enterprises - Evaluation of the World Bank Group Experience with Targeted Support to Small and Medium-Size Enterprises, 2006–12

(targeting young artisans), Kenya's Youth Enterprise Fund, and Morocco's YouthInvest scheme. An example of a successful direct lending scheme in France is provided in Box 3.

BOX 3 - ASSOCIATION POUR LE DROIT À L'INITIATIVE ÉCONOMIQUE (FRANCE)

Established in 1988, the Association pour le droit à l'initiative économique (ADIE) is a non-governmental organization promoting self-employment among the disadvantaged. ADIE's target population includes a large share of people relying on public assistance, originating from impoverished urban areas and with a modest level of education. ADIE provides financial support in the form of micro loans and unsecured personal loans (prêts d'honneur). Total financial assistance cannot exceed € 10,000, but this maximum level is rarely achieved and since 2010, the average value of micro loans has been in the order of € 3,000 – 3,500, while unsecured loans have averaged at about € 2,000. Over the last few years, non-performing loans have ranged between 9% and 7%, while losses have hovered around 2.5%. Despite the extensive use of volunteers (who constitute the bulk of mentors), administrative costs are quite significant, at about € 1,600 per firm created, i.e. about one third of the total average financing granted. The survival rate of ADIE assisted firms is similar to that of all French newly created firms, which, considering the features of the target population, must be regarded as a positive result. The average job creation is about 1.3 per new firm established.[17]

[17] ADIE (2013) Etude d'impact.

4.3 Equity Financing Can Significantly Improve Performance But Is Suitable Only for a Minority of Firms

Equity is often deemed a preferable form of financing as it does not place an 'excessive' burden on firms (no rigid repayment terms, no interest burden). However, an equity investment involves relinquishing part of control, which does not appeal to the majority of firms ('lifestyle businesses').

Equity financing has become an important instrument in entrepreneurial finance, in both developed and developing countries. For instance, in the EU, investment funds have become a preferred form of public intervention in the attempt to boost growth and innovativeness.

Since 2009, government agencies have been the most important investors in venture capital funds, accounting for more than 30% of funds raised. In developing/emerging countries, the IFC is the main player, with a portfolio in excess of US$ 3 billion invested in some 180 funds, followed by the EBRD, with a portfolio of some US$ 2.3 billion invested in about 100 funds. Equity investment is resource intensive activity and even in the case of 'SME-oriented' funds, transaction costs induce to focus on relatively larger deals. For instance, over the 2001 – 2011 period, the average investment of IFC-participated SME funds was in the order of US$ 4 million, a figure well above the amounts that can be normally absorbed by a typical SME. There are however cases of investment funds adopting a more flexible approach, and capable of reaching out a considerable number of small enterprises. An example of a fund specialized in the SME segment is provided in Box 4.

BOX 4 - BUSINESS PARTNERS (SOUTHERN AND EASTERN AFRICA)

Based in South Africa, Business Partners (BP) is specialist provider of risk finance to SME. BP makes extensive use of quasi equity instruments (royalty loans) that retain the essence of risk capital investment - performance-related remuneration - without the complexity of equity investments. Financing is complemented with the provision of technical assistance and mentoring services. BP has been able to effectively serve the SME market and the model is being replicated in other African countries. In particular, since the mid-2000s, BP established a fruitful cooperation with the IFC and other donors/IFI for the setting up of similar schemes in Eastern and Southern Africa. In South Africa, over the last few years BP has made about 300-350 investments/year, worth an average US$ 300,000, and supporting an estimated 10 – 15,000 jobs/year. In Kenya and Rwanda, since 2006 BP made about 150 investments, worth an average of US$ 200,000, and supporting 10,000 jobs.

4.4 Credit Guarantees Squarely Address the Issue of Collateral Mobilization, But Are Exposed to The Risk of Moral Hazard

Credit guarantees aim at 'incentivizing' the use of existing resources in favor of SME and other target groups by reducing the losses incurred by banks in case of default. However, as in any risk transfer mechanism, credit guarantees are structurally exposed to the risk of moral hazard and opportunistic behavior, which requires the adoption of appropriate counter measures (partial protection against default, wide portfolio diversification). Credit guarantees are an effective instrument to support SME. In EU countries, the average size of guarantees typically ranges between € 30,000-40,000 (Italy and France) and € 120,000 (Germany and the Netherlands). Considering a 50 - 70% coverage ratio, this implies loans worth between € 50,000 and € 200,000.[18] In other countries and regions, the value of guarantees vary considerably, with lower values in India and Latina America and higher values in North African and the Middle East. Irrespective of these regional differences, in general the value of guarantees is compatible with the typical financing needs of SME. Credit guarantee can also be structured to support special target groups, such as start-ups and young prospective entrepreneurs. However, the focus on certain categories of borrowers is somehow in conflict with the basic principle of risk diversification and a high coverage ratio (sometimes up to the full amount of loans) is required.
In turn, this may reduce the quality of the screening done by banks, resulting in significant losses. An example of the effects

[18] For a recent review of credit guarantee operations see OECD (2013) SME and Entrepreneurship Financing: The Role of Credit Guarantee Schemes and Mutual Guarantee Societies in supporting finance for small and medium-sized enterprises.

of such a perverse mechanism is provided by South Africa's Khula guarantee program, that in the late 2000s experienced a default ratio of about 80%.[19] Due to moral hazard considerations, for a long time donors/IFI have been skeptical about credit guarantees, although there are some important exceptions. The experience of USAID is illustrated in Box 5.

BOX 5 - USAID'S DEVELOPMENT CREDIT AUTHORITY (VARIOUS COUNTRIES)

Established in 1999, the Development Credit Authority (DCA) provides credit guarantees to banks, micro finance institutions and leasing companies. Over the FY 1999-2012 period, USAID allocated to DCA some US$ 120 million. However, as these funds only correspond to expected losses, DCA's 'firepower' is much greater, up to 25-30 times. Indeed, since establishment DCA extended guarantees worth US$ 3.7 billion to some 330 banks and financial institutions across 74 countries. DCA guarantees have proved highly effective in reaching out underserved SME: out of nearly 20,000 loans approved over the 2008 – 2010 period, 72% went to firms with up to 5 employees, of which about half were 'first time' borrowers.[20] DCA's prudent approach (credit guarantees usually do not exceed 50% of the loan) resulted in a very low default ratio, which at end 2013 stood at just 1.85% of the portfolio.

[19] Timm S. (2012) How the state and private sector can partner to boost support SMEs: Lessons from Chile & Malaysia.
[20] Storm L. (2013) Unlocking Growth Through Credit Guarantees An overview analysis of loans to woman-owned SMEs.

5. MAIN THEMES OF THE MEETING

During the EGM a variety of initiatives were presented by participants, involving the deployment of various instruments (both financial and non-financial), reflecting different approaches (e.g. with focus on the 'demand' or 'supply' sides of the financial market), and with significant differences in scale and scope (from small pilot initiatives to large, multi-country programs). In several cases, the initiatives presented were not strictly focused on entrepreneurial finance issues, and dealt with the broader theme of 'entrepreneurship development', both in general and for special target groups.[21] Such a diversity of experiences greatly contributed to enrich the debate but also made more difficult to properly compare the results achieved by the different initiatives, in terms of effectiveness and efficiency. Accordingly, several participants called for an effort in segmentation, with a clearer identification of the target beneficiaries and, therefore, of the specific, operational objectives of the various families of interventions.

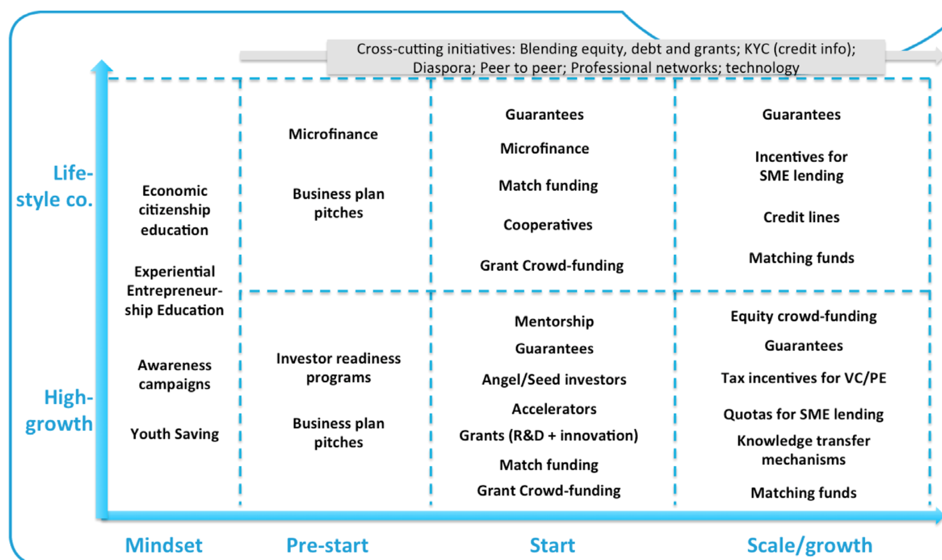
5.1 Key Principles for Cost-effective and Scalable Models of Entrepreneurial Finance

The theme of cost effectiveness and scalability was discussed in one of the two break-out sessions. It was found that the development of cost-effective and scalable models of entrepreneurial finance should take into consideration three principles, namely:

- Principle 1: Segmentation and Tailoring. Recipients and investors should be segmented in terms of size (e.g. microfinance vs. SME) and type (e.g. high-growth start up vs. life style entrepreneur). This will help to ensure that gaps can be better analyzed and addressed.
- Principle 2: Multi-Stakeholder Approach. Models for entrepreneurial finance should always include four different stakeholders working together in partnership: (i) Government – to ensure appropriate regulatory framework; (ii) DFIs – to ensure facilitation, knowledge sharing and compounding; (iii) Private sector- to bring in ideas & framework from private sector and ensure sustainability; and (iv) Grass-roots organizations – provide bottom-up input.
- Principle 3: Monitoring. Models should always include a monitoring component ex-ante in order to track performance. This will be particularly important to disprove myths and build track-record. However, monitoring efforts should be aware of tipping point when cost of monitoring exceeds its value.

Putting into practice the above three principles, would produce a mapping such as the one shown in Exhibit 12, which differentiates between lifestyle enterprises and high growth enterprises, at the various stages of development (i.e. pre-start, start-up, growth).

EXHIBIT 12 EXAMPLE OF MAPPING



[21] Notable examples include the UN-Habitat´s Urban Youth Fund, the activities of Making Cents International, the projects implemented by the Fondazione Giacomo Brodolini, as well as the mentorship initiatives mentioned by the G20 Young Entrepreneurs Alliance representative

5.2 Financial and Non-Financial Instruments

The linkage between financial and non-financial instruments was a recurrent theme during the meeting and was also extensively debated in one of the thematic discussion groups.[22] Two different categories of non-financial services (NFS) were discussed. The first refers to the technical assistance provided by donors/IFI to banks and other financial institutions to better align their operations to the needs of SMEs and other special target groups. In this case, technical assistance is typically aimed at devising new financial products (e.g. loans specifically targeted at working women) and/or developing new loan application screening mechanisms (e.g. scoring systems less dependent upon past credit history), and restructuring internal procedures (e.g. delegation of powers to branches, so as the make the interaction with SMEs more fluid). The second type of NFS relates to the assistance provided by governments and donors/IFI to SMEs in order to increase their chances of accessing finance. This encompasses a wide range of services, from assistance in the development of business plans and loan applications to the provision of hands-on advisory to enhance firms 'investor readiness' and/or to connect firms with potential providers of funds.[23] Regarding specifically the assistance provided directly to SME, the main aspects emerged from the discussion can be summarized as follows: (i) support must be carefully tailored to the needs of intended beneficiaries, which in turn requires a segmentation by type of entrepreneur/firm and stages of development (see above); (ii) NFS need to be closely linked with the deployment of financial instruments, to ensure that funding is effectively put to good use; (iii) in certain cases, namely for businesses in the early stage of development, there is a case for the provision of subsidized services. However, donor/IFI should strive to avoid distortions in the market; (iv) irrespective of financing modalities (subsidy vs. market prices), non-financial assistance should be channeled through specialized providers and not through banks or other financial institutions, so as to avoid potential conflicts of interest; and (v) greater efforts are to be deployed to ensure an accurate measurement of the results achieved.

5.3 Novel Financial Tools

The deployment of innovative financial instruments better suited to serve the needs of SMEs as well as women/youth-owned firms was advocated by several participants. The discussion focused on three main typologies of innovative instruments or intervention modalities, namely: (i) crowdfunding; (ii) impact investing; and (iii) the blending of grant money with financing at commercial terms.

The theme of crowdfunding attracted considerable attention, although views were somewhat divided. Some participants stressed that peer-to-peer lending can be an attractive solution for small businesses that lack collateral or a credit history to access traditional bank lending. In a similar way, equity crowdfunding was mentioned as a potential complement or substitute for seed financing for entrepreneurial ventures and start-ups that have difficulties in raising capital from traditional sources. At the same time, some participants highlighted the existence of significant regulatory obstacles limiting the expansion of crowdfunding, especially for securities-based crowdfunding, which is still not legal in some countries. As a result, the volume of transactions is still quite limited, even in advanced countries.[24]

Impact investment was also extensively discussed by EGM participants. The 'triple bottom line' approach typical of impact investing, which combines financial returns with social and environmental impact, was found to be an important complement to other, more traditional financial instruments. Some presentations documented the rapid growth of impact investing market but at the same time highlighted some significant limitations. Indeed, the bulk of impact investing money has so far been invested in micro finance institutions, whereas SME have been able to attract only limited resources. In this respect, impact investing suffers from the same limitations of more traditional equity financing instruments (see above), as transaction costs tend to increase the average size of deals and the complexity of investment operations reduces the pool of investable firms.[25] The mismatch between the typical size of impact investing deals and the typical financial needs of SME is confirmed by various studies. For instance, recent research on impact investing in East Africa, found that nearly 90% of all the funds invested were allocated to deals worth more than US$ 1 million, a figure well in excess of typical SME financial needs.[26]

Blending involves the combination of grant money with other sources of funding, typically loans, provided at commercial terms. Grants can be used to reduce the cost of financing, through interest subsidies, or to mitigate risk, providing a buffer against possible losses. Blending has been extensively used in the past for infrastructure projects but its utilization in the area of SME financing is relatively recent. Examples of large blending initiatives include the Global SME Finance Facility, promoted by the IFC and supported by a grant from DFID,[27] and the Western Balkans Enterprise Development and Innovation Facility, with grants from the EU budget complementing loans from the European Investment Bank (EIB) and the EBRD. Examples of operations featuring 'blending' elements presented at the EGM include the UNIDO project 'Productive Work for Youth in Armenia' and the Souk At-tanmia project in Tunisia, supported by the AfDB. As noted during the discussion, the main potential advantage of blending lies in the leverage effect of grants, as relatively modest grant allocations can provide a risk buffer for much larger volumes of loans. However, the magnitude of the leverage effect depends upon the specific circumstances, ranging from very high values (in the case of the Global SME Finance Facility one dollar of grant contribution is expected to generate eight to ten dollars of lending) to much more modest values.

5.4 Limited Information on Impact, Sustainability, and Cost Effectiveness

For many initiatives illustrated during the EGM the information on the results achieved only concerned outputs (i.e. the number of SME or young entrepreneurs served by a certain scheme) and, sometimes, the most immediate outcomes (i.e. the number of surviving firms after a certain period), whereas limited information was available on longer term impact. To a large extent, this is due to the recent nature of many initiatives presented, which obviously prevents a comprehensive as-

[22] The results of the thematic group discussion are summarized in Annex C.

[23] An example of this type of assistance was provided in the presentation made by Capital Pitch. For more details, see http://capitalpitch.com/.

[24] For a recent review of developments in the crowdfunding market, see OECD (2015) New Approaches to SME and entrepreneurship finance: Broadening the range of instruments - Final Synthesis Report.

[25] This point was raised in particular in the presentation made by CGAP, which noted that the biggest constraint faced by impact investing is "too few investable grade firms in which to invest".

[26] Global Impact Investing Network and Open Capital (2015) The Landscape for Impact Investing in East Africa.

[27] DFID (2012) Global SME Finance Initiative - Business Case.

sessment.[28] Practical considerations, however, combined with methodological issues, which often make it difficult to rigorously assess the impact of entrepreneurial finance initiatives, due to the difficulty of controlling for 'confounding' factors.[29] A similar situation concerns the assessment of sustainability, for which very limited evidence was also provided. This is particularly the case for the influence exerted by various interventions on the behavior of banks and other financial institutions, i.e. whether the interventions have resulted in a stable re-orientation of lending activities towards SME or other intended target groups. Finally, limited evidence was also generally available regarding the cost effectiveness of the various initiatives. In fact, only in a few cases presentations included information on the budgetary implications of interventions, in terms of cost of per unit of output or outcome achieved (e.g. cost per loan granted or cost per surviving firm).[30] Given the growing pressure exerted by the difficult economic and financial conditions in many donor countries, the issue of cost effectiveness is obviously of major importance for the identification of good practices in entrepreneurial finance.

5.5 Lack of data and the need of M&E framework

As implied by the above considerations on impact and cost effectiveness, the assessment of entrepreneurial finance initiatives is often confronted with an acute scarcity of data. This is primarily due to the fact that most initiatives are often channeled through private sector actors (banks, PE/VC funds), whose management information systems (MIS) are usually not conceived to provide the information necessary to assess the success of donor/IFI initiatives. In particular, financial intermediaries tend to segment clients according their own criteria, which often vary from bank to bank and generally differ from the definitions and criteria of interest for donors/IFI. For instance, the definition of 'small business' used by banks are not homogenous and in any event have usually no relationship with 'official' definitions of SME. Similarly, banks have difficulties in providing data on loans extended to women-owned firms or youth-led businesses, because information on the gender and age of the sponsors, although in principle available in loan applications, is rarely incorporated in MIS. Problems are even more acute regarding performance variables, such as the employment generated or incremental sales, as data on the workforce of borrowers are not collected systematically by banks while information on sales is often regarded as confidential. In order to appropriately document the achievements of entrepreneurial finance initiatives it is therefore necessary to develop comprehensive M&E frameworks capable generating the data required by donors/IFI without excessive interference in financial intermediaries operations. The problem is currently being addressed by various donors/IFI, through the development of new approaches to the M&E of entrepreneurial finance initiatives. An interesting example is provided by the impact evaluation exercise currently ongoing in the framework of the Global SME Finance Facility, an initiative launched by IFC with DFID support.[31]

5.6 Legal and policy reform initiative

Several EGM participants highlighted the need to complement the deployment of specific entrepreneurial finance instruments with measures aimed at improving the legal, regulatory and institutional framework for financing transactions. Regarding debt financing, three main themes emerged from the discussion, namely: (i) the establishment or improvement of the legal and institutional framework for the registration of collateral (pledges on movable assets and mortgages on real estate property), which can greatly enhance the ability of small firms to leverage their assets in order to access credit; (ii) the establishment or improvement of credit information systems (credit bureaus operating on a commercial basis as well as centralized 'credit risk systems' operated by central banks), which can help banks in the identification of creditworthy borrowers and therefore reduce the cost of financing; (iii) the improvement of the legal and institutional framework for insolvency resolution, which can increase the banks' confidence in the ability of recovering at least part of their funds in case of default, with a positive effect on lending attitudes.[32] In the case of asset-based financing, two aspects were mentioned, namely: (i) the improvement of the legal and regulatory framework (including tax treatment provisions) for leasing, which is a particularly well suited form of financing for certain types of investments (typically, movable assets, like vehicles, agricultural equipment); and (ii) the improvement of the legal and institutional framework for factoring (especially regarding contract law provisions allowing for the transfer of receivables), which can greatly assist small businesses in smoothing their working capital needs. Finally, several participants noted that equity financing operations are heavily influenced by the legislation on corporate governance. As PE/VC funds typically only take minority shareholdings, it is necessary to strengthen legal provisions on information disclosure and on the protection of minority shareholders' rights. The existence of well-functioning stock exchange markets is also widely regarded as an important condition for the development of private equity, although the majority of transactions involving SME are actually exited through 'trade sales' (i.e. the shares bought by PE/VC funds are sold back to the owners/managers).[33]

[28] This is the case, for instance, of the UNIDO project 'Productive Work for Youth in Armenia', that has been operational only for a couple of years. An evaluation was expected to be carried out after the EGM.

[29] The methodological issues confronted in the evaluation of SME financing instruments are neatly illustrated in World Bank (2012) Impact Assessment Framework: SME Finance. A major impact evaluation exercise is currently ongoing in the framework of the Global SME Finance Facility, an initiative launched by IFC with DFID support. See http://ifcext.ifc.org/IFCExt/Pressroom/IFCPressRoom.nsf/0/93D7F6A1ADF92057852579E6004F8B25

[30] A notable exception was Making Cents International's work on financial inclusion, for which unit cost estimates as well information on benchmarks were available.

[31] See http://ifcext.ifc.org/IFCExt/Pressroom/IFCPressRoom.nsf/0/93D7F6A1ADF92057852579E6004F8B25.

[32] These aspects were extensively mentioned in the presentations made by WBG representatives.

[33] For a comprehensive review of legal and institutional factors influencing PE/VC operations, see Klonowski D (editor), Private Equity in Emerging Markets: The New Frontiers of International Finance, Palgrave, 2012.

6. RECOMMENDATIONS

6.1 Policy Recommendations

The elements emerged during the EGM led to the formulation of a set of policy recommendations. These recommendations are presented in Box 6 below.

BOX 6 - RECOMMENDATIONS OF THE EXPERT GROUP MEETING ON ENTREPRENEURIAL FINANCE

On the occasion of the Expert Group Meeting on Entrepreneurial Finance organized by UNIDO in co-collaboration with UNDESA and UNCDF, attended by European Investment Bank, Child and Youth Finance International, IFC, ILO, Fondazione Brodolini, Making Cents International, OECD, Ernst &Young, Capital Pitch, G20 Youth Entrepreneurs Alliance, UN Habitat, UNDP, UN Women, UNAoC, USAID and the World Bank, it was recognized the urgency of ensuring adequate access to finance for [youth and women-led] start-up and growth oriented enterprise.

Stemming from ample of rich contributions and exchanges of good practices, the participants call upon Governments, the civil society, as well as the private sector, particularly the financial sector, to consider and implement the following recommendations:

1. Create a more conducive regulatory and financial framework at country level to promote innovative entrepreneurial finance schemes such as equity & venture capital, quasi-equity, equity crowd funding and business angels investment (i.e. tax incentives for investment and innovation, review of investment related laws, enhance bankruptcy laws, etc.)

2. Incentivize and promote education programs, entrepreneurial and technical training, peer to peer mentoring, to make entrepreneurs (particularly youth and women) bank or investor ready (i.e. support seed accelerators, technology incubators, prototyping facilities, technology transfer systems, etc.).

3. Invest in strengthening the entrepreneurial ecosystem to facilitate the creation of start-ups and the development of MSMEs, particularly for women and youth (i.e. support young/women entrepreneurs' organizations, startup events/hackathons, venture capital associations, business angel's networks, IP offices, etc.)

6.2 Operational Recommendations

Operational recommendations focused on two aspects, namely: (i) the setting up of a platform for communication and knowledge sharing that would allow to continue the discussion initiated at the EGM; and (ii) the development of a toolkit/sourcebook providing a systematic review of the advantages and disadvantages of various financial and non-financial instruments in the area of entrepreneurial finance.

Regarding specifically the proposed toolkit/sourcebook:

- The document should focus **primarily on the theme of entrepreneurial finance.** However, considering the substantial attention paid by the EGM to the broader theme of entrepreneurship development, the coverage could be extended to encompass also some measures aimed at fostering entrepreneurship development.
- The toolkit/sourcebook should cover the whole range of financial transactions from **early stage financing** (i.e. before a firm has reached commercial viability, which includes seed and start-up financing) through **first expansion financing** (i.e. when a business has been operating profitably for some time and is seeking to scale up operations);
- The initiatives to be reviewed should include both **operational instruments**, encompassing both financial and non-financial instruments, and **legal and policy reform initiatives**, aimed at creating a more conducive environment;
- The focus should be primarily on initiatives implemented **in developing countries.** However, whenever relevant, the experience gained in other contexts, typically OECD countries, would also be covered;
- The toolkit/sourcebook is not meant to be a simple collection of interventions but rather is expected to **focus on initiatives that fulfill basic criteria for being regarded as 'good practices'.** These criteria were defined in the Background Paper for the EGM and include the ability to: (i) effectively reach the target group(s) (effectiveness criterion); (ii) exert a positive influence on beneficiaries' performance (impact criterion); and (iii) achieve results at a reasonable cost (efficiency criterion);
- Finally, considering the continuous evolution in the field of entrepreneurial finance, **the toolkit/sourcebook should be regarded as a 'live document'**, susceptible of being easily updated as additional evidence about old or new initiatives becomes available. This has important operational implications, as it requires the adoption of a 'modular format', so as to allow for the rapid updating of the information.

Details about the possible structure of the proposed toolkit/sourcebook are provided in Annex D.

7. ANNEXES

ANNEX A – EGM AGENDA

THURSDAY 26 MARCH 2015	
10:00 – 11:00	*Opening session:* » Mr. Ahmad Alhendawi, SG's Envoy on Youth » Mr. Paul Maseli, Director, UNIDO Office in New York » Mr. Krishnan Sharma, UNDESA, Financing for Development Office » Mr. Mr. John Tucker, Director, Financial Inclusion Practice Area UNCDF
11:00 – 12:30	*Presentation:* Overview and introduction to the main challenges (UNIDO, UNDESA, UNCDF) Presentation of preliminary findings of the research and best practices (UNIDO)
Lunch break	
14:00 – 18:00	*Presentation on best practices by participants* Moderators M. Carcò / M. Landi

FRIDAY 27 MARCH 2015	
09:30 – 12:30	*Thematic group discussion (to produce recommendations)* Cost effectiveness and replicability/scalability of funding mechanisms for entrepreneurship finance Financial and non-financial mechanisms: integration of non-financial services in financial facilities
Lunch break	
14:00 – 16:00	Summary of key findings from the group discussions (group rapporteurs) Wrap-up and the way ahead
16:00 – 16:30	*Closing remarks (UNIDO, UNCDF, UNDESA)*

ANNEX B – LIST OF EGM PARTICIPANTS

NAME	AFFILIATION	POSITION
Mr. Ahmad Alhendawi	OSGEY	SG's Envoy on Youth
Mr. Paul Maseli	UNIDO	Director Office in New York
Mr. John Tucker	UNCDF	Deputy Director, Financial Inclusion Practice Area
Mr. Krishnan Sharma	UNDESA - FFD	Senior Economic Affairs Officer
Ms. Monica Carco'	UNIDO	Chief, Investment & Technology Unit
Mr. Matteo Landi	UNIDO	Industrial and Youth Employment Expert
Ms. Marianna Petrosyan	UNIDO	National Team Leader of the UNIDO Project "Productive work for youth in Armenia"
Mr. Roberto Zavatta	UNIDO	Expert on SMEs Finance
Ms. Maria Kloss	UNIDO	Liaison officer to UNDESA Youth focal point
Ms. Nicola Shepherd	UNDESA	Focal Point for Youth
Ms. Maria Perdomo	UNCDF	YouthStart Program Manager
Ms. Christel Alvergne	UNCDF	Deputy Director, Local Development Finance
Ms. Noella Richard	UNDP	Youth Policy Specialist
Ms. Charu Bist	UNDP	Jobs and Livelihoods, Sustainable Dev. Cluster
Ms. Aparna Dalal	ILO	Social Finance Unit
Ms. Sarah Gammage	UN WOMEN	OIC for the Economic Empowerment section
Mr. Jon-Andreas Solberg	UN Habitat	Policy and Strategy Advisor
Mr. Kris Boschmans	OECD	Policy Analyst, Centre for Entrepreneurship, SMEs and Local Development
Mr. Joseph Obi	USAID - DCA	Africa Portfolio Manager
Ms. Paola Ravacchioli	EIB	Investment Officer, Equity Division, Directorate for Operations outside the EU
Mr. Emanuele Santi	AfDB	Senior Economist
Ms. Minerva Kotei	IFC	SME Finance Forum/Women's Finance Hub
Ms. Mayada El-Zoghbi	CGAP	Senior Financial Specialist
Mr. Timothy Nourse	Making Cents International	President, Making Cents International
Ms. Ines Gramegna	Child & Youth Finance International	Innovations Coordinator
Mr. Kevin J. Langley	G20 Young Entrepreneurs Alliance	President, USA Chapter
Mr. Jeremy Liddle	Capital Pitch	CEO
Ms. Francesca Buonanno	Fondazione Giacomo Brodolini	Senior Advisor

New York, April 2015

Contents

1. **Financial and non-financial mechanisms: integration of NFS into FS**
2. Cost effectiveness and replicability/scalability of funding mechanisms for entrepreneurial finance

Contents

1. Financial and non-financial mechanisms: integration of NFS into FS
2. **Cost effectiveness and replicability/scalability of funding mechanisms for entrepreneurial finance**

Cost-effective and scalable models of entrepreneurial finance should take into consideration 3 principles

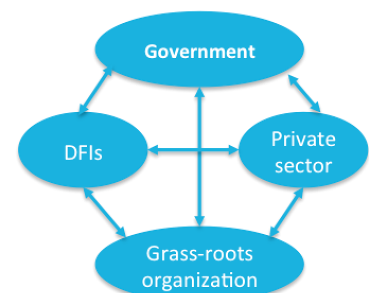
1 SEGMENTATION AND TAILORING

Recipients and investors should be segmented in terms of size (e.g. microfinance vs. SME), and type (e.g. high-growth start up vs. livelihoods entrepreneur). This will help to ensure that gaps can be analyzed and addressed.

2 MULTI-STAKEHOLDER APPROACH

Models for entrepreneurial finance should always include a 4 different stakeholders working together in partnership:

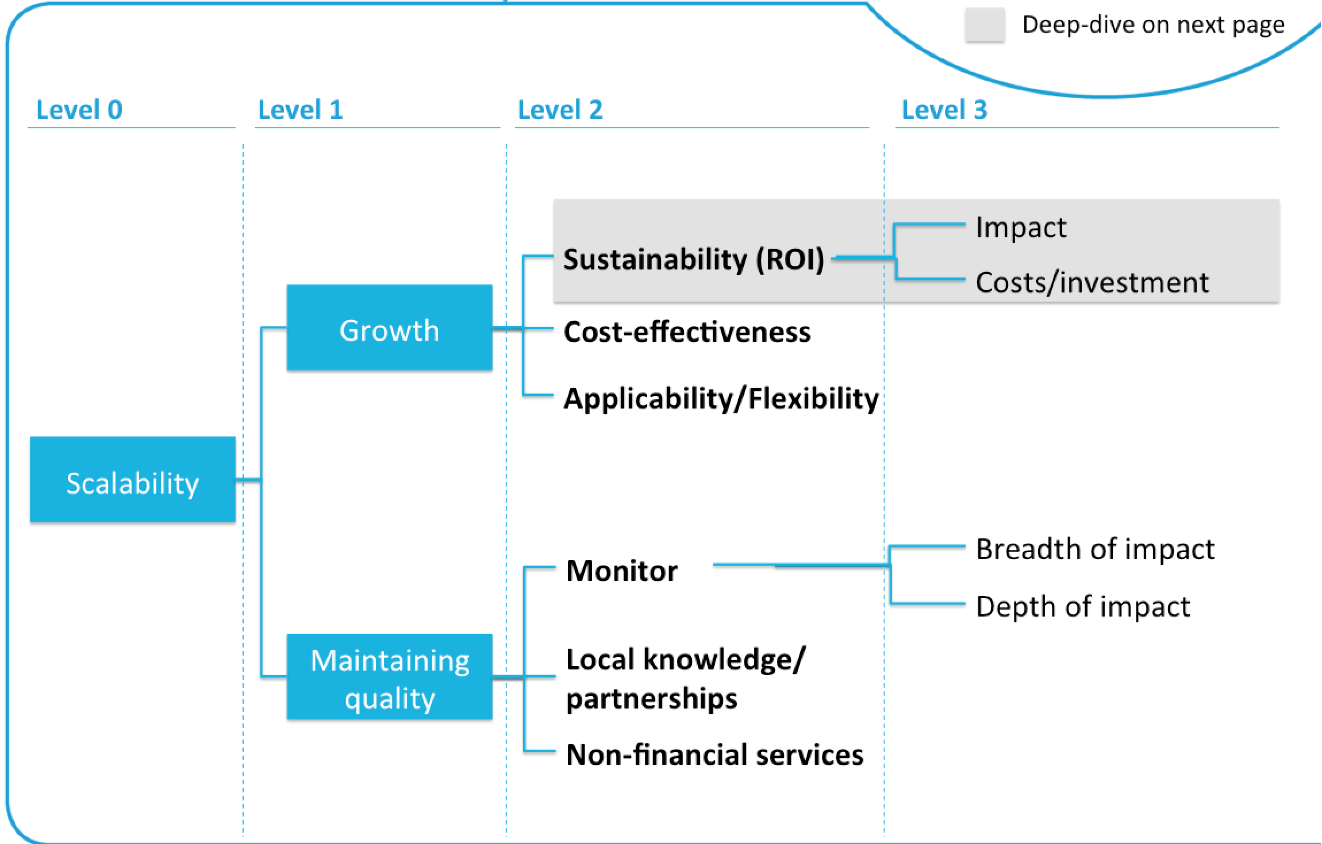
(a) Government – to ensure appropriate regulatory framework
(b) DFIs – to ensure facilitation, knowledge sharing and compounding
(c) Private sector- to bring in ideas & framework from private sector and ensure sustainability
(d) Grass-roots organizations – provide bottom-up input



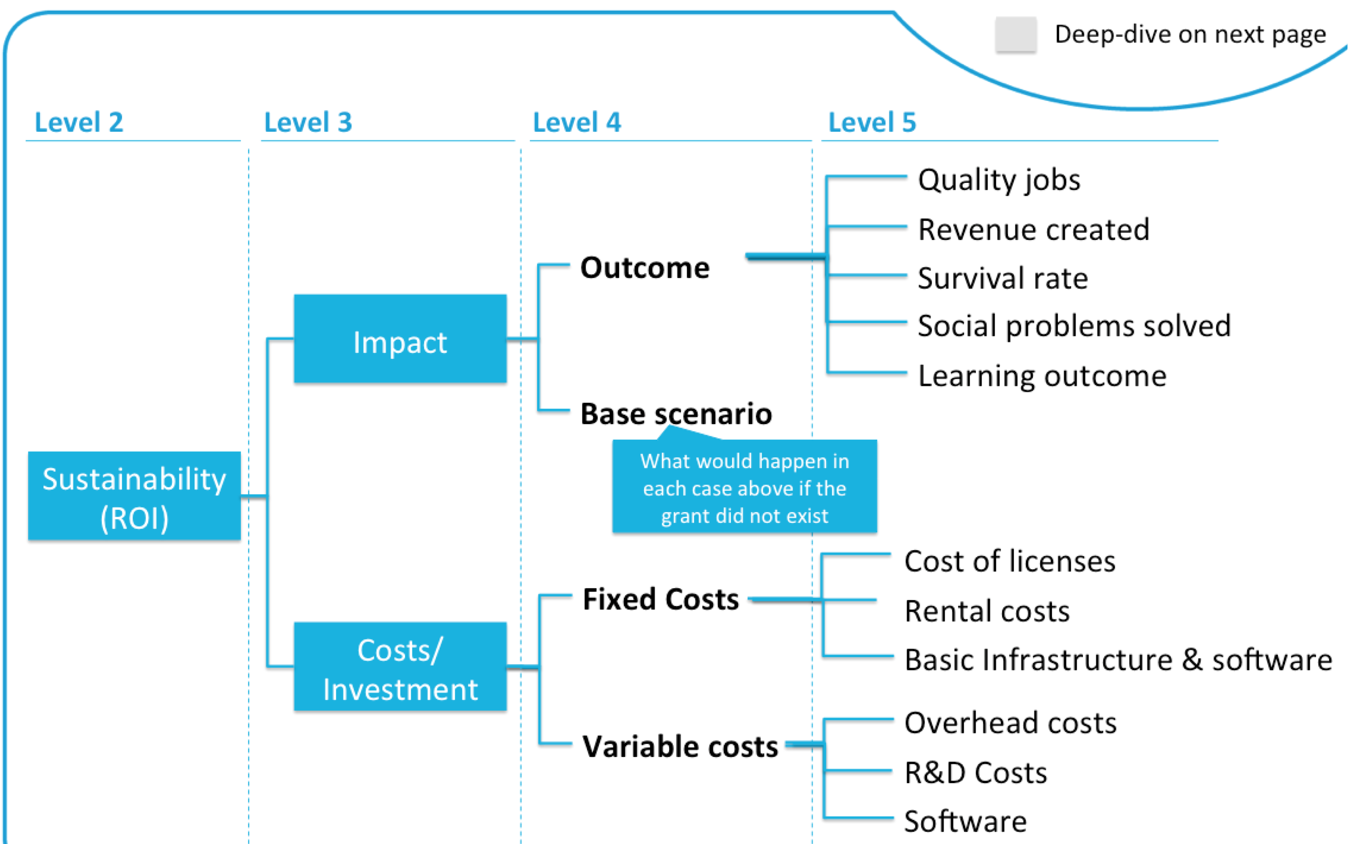
3 MONITORING

The model should always include a monitoring component ex-ante in order to track performance. This will be particularly important to disprove myths and build track-record. Note monitoring efforts should be aware of tipping point when cost of monitoring exceeds its value

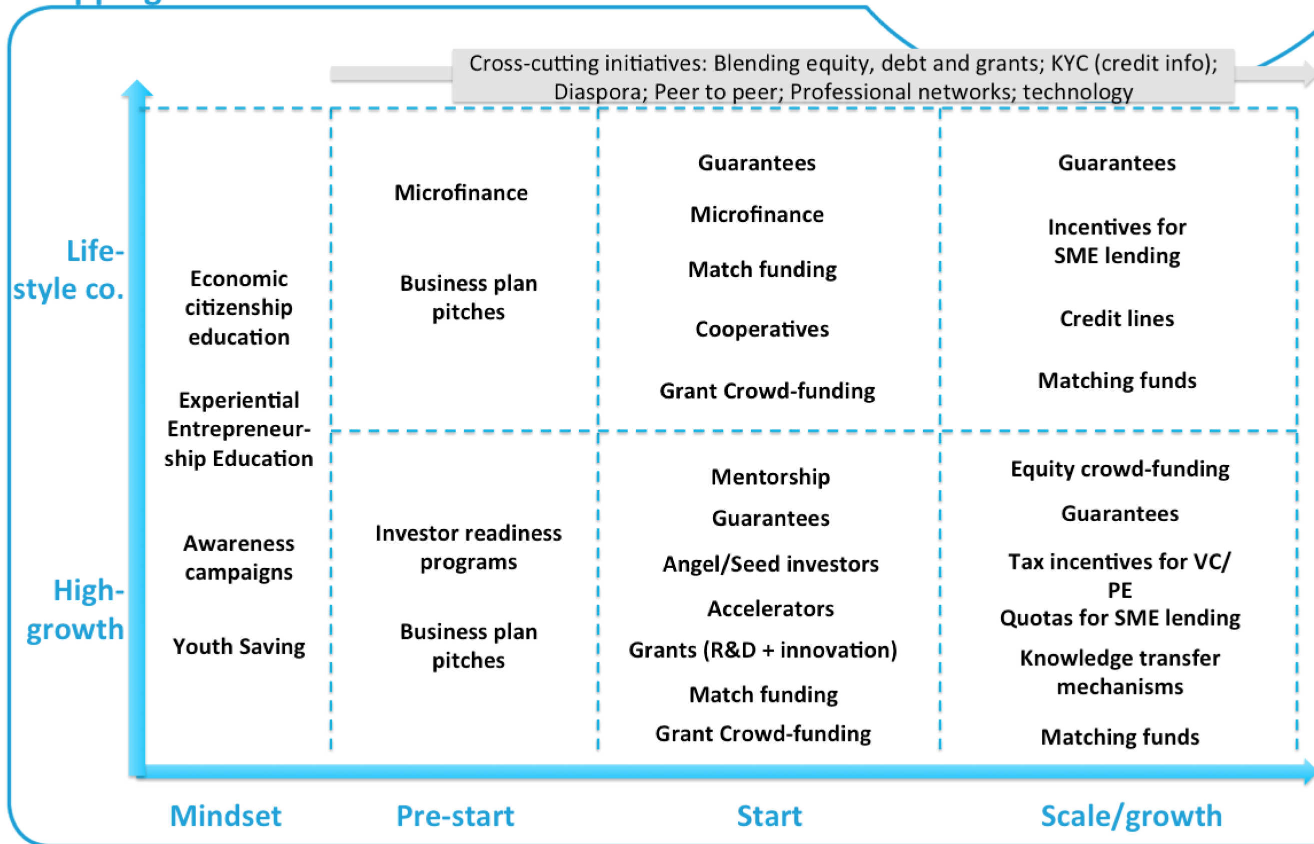
Scalability was seen as the over-arching theme, and was broken down into its components



Sustainability will be a key determinant of scalability



Putting into practice principles 1 to 3, would produce a mapping such as the one below



Note: these examples are not comprehensive but rather exemplify the type of mechanisms that were presented during the EGM

ANNEX D – POSSIBLE STRUCTURE OF THE PROPOSED TOOLKIT/SOURCEBOOK

D.1 PROPOSED STRUCTURE

As discussed at the EGM, the toolkit/sourcebook could be articulated into a **series of thematic chapters, each dealing with a different type of intervention**. At this stage, it is envisaged that the toolkit/sourcebook should include the following chapters:

- Financial Instruments – Debt Financing;
- Financial Instruments – Equity/Quasi Equity Financing;
- Financial Instruments – Guarantees;
- Financial Instruments – Others;
- Non-Financial Instruments – Support to Businesses;
- Non-Financial Instruments – Support to Financial Intermediaries;
- Legal and Policy Reform Initiatives.

The aspects to be analyzed under each of the above chapters are summarized in the table below.

CHAPTER	CONTENTS
Financial Instruments – Debt Financing	Review of various mechanisms deployed by donors/IFI/governments involving the provision of funding to commercial banks for further on lending to enterprises, commonly referred to as 'credit lines'. Analysis disaggregated by: (i) target groups (e.g. generic SME vs. women/youth-owned businesses); (ii) purpose of credit lines (investment vs. working capital financing); and (iii) level of concessionality (e.g. fully commercial credit lines vs. schemes involving a grant element).
Financial Instruments – Equity/Quasi Equity Financing	Review of investment funds established or participated by donors/IFI/governments with the purpose of providing risk capital to enterprises. Investment funds can be segmented based on: (i) the stage of financing targeted (seed funds, start-up funds, expansion funds); and (ii) the overall orientation (commercially oriented funds vs. impact funds).
Financial Instruments – Guarantees	Review of mechanisms aimed at alleviating collateral requirements through the provision of credit guarantees, commonly referred to as 'guarantee funds'. A distinction can be made depending upon: (i) the nature of guarantee funds (mutual funds vs. public funds); (ii) the operating modalities adopted (individual guarantees vs. portfolio guarantees); and (iii) the target groups (generic SME guarantee funds vs. schemes targeting special groups).
Financial Instruments – Others	Review of: (i) various types of leasing (financial leasing, hire-purchase arrangements); (ii) factoring (with and without recourse); (iii) other forms of asset based financing (namely, warehouse financing); as well as (iv) innovative financing instruments, in particular crowdfunding.
Non-Financial Instruments – Support to Businesses	Review of two categories of interventions, namely: (i) initiatives aimed at increasing the chances of accessing finance (pre financing stage), which range from basic financial literacy programs to the provision of hands-on assistance in the preparation of business plans and/or loan applications; and (ii) initiatives aimed at supporting the proper utilization of the funds received (post financing stage), including the provision of targeted technical assistance, the secondment of managerial staff (e.g. AMSCO), and mentoring schemes.
Non-Financial Instruments – Support to Financial Intermediaries	Review of interventions aimed at increasing the capabilities of banks and other financial intermediaries to serve the intended target groups, through (i) the development of new financial products and related marketing strategies, and (ii) the adaptation of the organizational structure (i.e. the delegation of powers to branch managers).
Legal and Policy Reform Initiatives	Review of measures aimed at establishing/improving: (i) collateral registries for both movable and immovable assets (pledges and mortgages); (ii) credit information systems; (iii) the legal and regulatory framework for asset-based financing and for innovative financial instruments (crowdfunding); and (iv) the legal and institutional framework for insolvency (mechanisms for the seizing and sale of collateralized assets).

Each chapter could include: (i) a brief **overview of the salient features of the instrument;** (ii) a short **description of selected operations**, with an indication of reasons why they can or cannot be regarded as a 'good practice'; and (iii) a summary of the **lessons learned**. The main text of the toolkit/sourcebook would be supplemented by annexes with the detailed profiles of the selected good practices.

D.2 TEMPLATE PROFILE FOR GOOD PRACTICES

TITLE OF OPERATION	
Basic Features	
Nature/Mission	
Structure/Organization	
Activities	
Geography	
Key Figures	
Operations	
Target Group(s) and Transactions	
Financial Instruments	
Non-financial Instruments	
Terms and Conditions	
Performance	
Financial Performance	
Outreach Capability	
Impact	
Cost Effectiveness	
Other Aspects/Background Information	
Sources	

D.3 SOURCES OF INFORMATION

Issues in entrepreneurial finance have already been addressed is a variety of studies and operational documents which provide an important basis for the development of the toolkit/sourcebook. Two category of documents that are particularly relevant for the purpose include: (i) **evaluation studies** of previous entrepreneurial finance operations; and (ii) **policy documents and operational guidelines** developed by donors/IFI. Another useful source is the **Donor Committee for Enterprise Development** (DCED), which over the years has systematically investigated issues related to SME financing as well as other relevant themes. Finally, useful information can be derived from **other sources**, including a series of studies on SME recently published by the OECD, some World Bank Policy Research Working Papers, the evaluations on financial inclusion carried out by the Abdul Latif Jameel Poverty Action Lab (J-PAL), as well as a few scholarly publications focusing on the effectiveness of various financial and non-financial instruments. A selected list of these documents is provided below.

EVALUATION STUDIES

- ADB (2008) Special Evaluation Study - Private Equity Fund Operations
- AFD (2012) Assessing Credit Guarantee Schemes for SME Finance in Africa - Evidence from Ghana, Kenya, South Africa and Tanzania, Working Paper
- AfDB (2013) Independent Evaluation of Non-Sovereign Operations - 2006-2011
- Arráiz I, M Meléndez and R Stucchi (2011) The Effect of Partial Credit Guarantees on Firm Performance: the Case of the Colombian National Guarantee Fund, Inter-American Development Bank
- EBRD (2005) Special Study - Delivery Mechanisms for MSME Financing A Synthesis Report
- EBRD (2006a) Special Study - Regional Venture Funds Programme - Russian Federation
- EBRD (2007) Special Study - Post-Privatisation Funds.
- EBRD (2010) Operation Performance Evaluation Review - EU/EBRD SME Facility
- EBRD (2012) Special Study – EBRD - Italy Western Balkans Local Enterprise Facility (LEF) - (Western Balkans).
- EBRD (2013a) Equity Funds Portfolio Update - Data as of June 2012
- EBRD (2013b) Local Enterprise Facility
- EC (2013) Evaluation of the European Union's Support to Private Sector Development in Third Countries – Final Report.
- EIB (2013) Report on results of EIB operations outside the EU – 2012
- FAO (2013) Four case studies on credit guarantee funds for agriculture
- IDB – OVE (2003) MIF Evaluation – Development of Venture Capital
- IDB – OVE (2007) Evaluation of the Bank's Global Multisector Credit Operations – 1990 to 2005.
- IDB – OVE (2013a) Approach Paper - Comparative Analysis SME Models Supported by IDB: The Case of Brazil
- IDB – OVE (2013b) Second Independent Evaluation - Multilateral Investment Fund - Final Report to Donors
- IDB - OVE (2014) A Comparative Analysis of IDB Approaches Supporting SMEs: Assessing Results in the Brazilian Manufacturing Sector
- IFC (2000) An Evaluation of IFC's Investments through the Africa Enterprise Fund
- IFC (2011) Strengthening Access to Finance for Women-Owned SMEs in Developing Countries
- López Acevedo G and H W Tan (eds) (2011) Impact evaluation of SME programs in Latin America and Caribbean, The World Bank
- WBG – IEG (2006) World Bank Lending for Lines of Credit - An IEG Evaluation
- WBG – IEG (2008) Financing Micro, Small, and Medium Enterprises, an Independent Evaluation of IFC's Experience with Financial Intermediaries in Frontier Countries
- WBG – IEG (2009) The World Bank Group Guarantee Instruments 1990–2007
- WBG – IEG (2013) World Bank Group Support for Innovation and Entrepreneurship - An Independent Evaluation
- WBG – IEG (2014) The Big Business of Small Enterprises - Evaluation of the World Bank Group Experience with Targeted Support to Small and Medium-Size Enterprises, 2006–12
- World Bank (2010) Impact Evaluation of SME Programs in Latin America and the Caribbean
- World Bank (2012) Impact Assessment Framework: SME Finance

POLICY AND OPERATIONAL DOCUMENTS

- AfDB (2010) Bank Group Financial Sector Strategy and Action Plan (2011-2016), Governance and Financial Reforms Department
- AfDB (2013a), Inclusive Growth and Job Creation – AfDB Africa SME Program – Revised
- AfDB (2013b) Supporting the Transformation of the Private Sector in Africa - Private Sector Development Strategy
- AfDB (2013c) Private Sector Development Policy of the African Development Bank
- EBRD (2006) Micro, Small and Medium-Sized Enterprises Strategy
- EBRD (2012) Financial Sector Strategy
- IDB (2011) Private Sector Development Strategy: Fostering Development through the Private Sector
- IFAD (2012) Private-Sector Strategy - Deepening IFAD's engagement with the private sector
- IFC (2011) SME Finance Policy Guide
- IFC (2013c) Road Map FY14-16 - Leveraging the Private Sector to Eradicate Extreme Poverty and Pursue Shared Prosperity

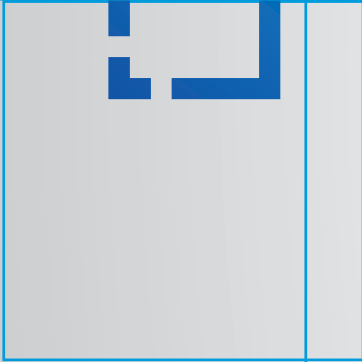
- WBG (2007) Financial Sector Strategy of the Worlds Bank Group
- WBG (2009) Private Sector Development Strategy
- WBG (2012) World Bank Group Innovations in Leveraging the Private Sector for Development: A Discussion Note
- WBG, Operational Manual http://go.worldbank.org/DZDZ9038D0

DCED

- Small enterprises http://www.enterprise-development.org/page/small-enterprises
- Women's economic empowerment http://www.enterprise-development.org/page/wed
- Inclusive business http://www.enterprise-development.org/page/inclusive-business
- Business environment reform http://www.enterprise-development.org/page/business-environment-reform-

OTHER SOURCES

- Batra G and S Mahmood (2003) Direct Support to Private Firms: Evidence on Effectiveness, World Bank Policy Research Working Paper 3170
- Benavides G and A Huidobro (2008) Are Loan Guarantees Effective? The Case of Mexican Government Banks, Banco de México
- Boocock G, M N Shariff (2005) "Measuring the Effectiveness of Credit Guarantee Schemes: Evidence from Malaysia", International Small Business Journal
- Cho Y and M Honorati (2013) Entrepreneurship programs in developing countries: A meta regression analysis, World Bank Policy Research Working Paper 6402
- J-PAL's work on finance and microfinance http://www.povertyactionlab.org/finance-microfinance
- Kuntchev V, R Ramalho, J Rodríguez-Meza and J S. Yang (2014) What have we learned from the Enterprise Surveys regarding access to finance by SMEs? World Bank Policy Research Working Paper 6670
- McKenzie D and C Woodruff (2012) What are we learning from business training and entrepreneurship evaluations around the developing world? World Bank Policy Research Working Paper 6202
- OECD (2013) SME and Entrepreneurship Financing: The Role of Credit Guarantee Schemes and Mutual Guarantee Societies in supporting finance for small and medium-sized enterprises
- OECD (2013) Financing SMEs and Entrepreneurs 2013: An OECD Scoreboard
- OECD (2015) New Approaches to SME and entrepreneurship finance: Broadening the range of instruments Final Synthesis Report Working Party on SMEs and Entrepreneurship.
- Saadani Y, Z Arvai and R Rocha (2011) A Review of Credit Guarantee Schemes in the Middle East and North Africa Region, World Bank Policy Research Working Paper 5612
- Storm L. (2013) Unlocking Growth Through Credit Guarantees An overview analysis of loans to woman-owned SMEs
- Timm S. (2012) How the state and private sector can partner to boost support SMEs: Lessons from Chile & Malaysia



ACCESS

INNOVATION

Office of the
Secretary-General's
Envoy on Youth

U N
D P

International
Labour
Organization

UN
WOMEN

UN HABITAT
FOR A BETTER URBAN FUTURE

OECD
BETTER POLICIES FOR BETTER LIVES

USAID
FROM THE AMERICAN PEOPLE
Development
Credit Authority
Putting local wealth to work

European
Investment
Bank

IFC
International
Finance Corporation
WORLD BANK GROUP

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