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COUNCIL

Meeting of the Council at Ministerial Level, 7-8 June 2023

DRAFT RECOMMENDATION OF THE COUNCIL ON SME FINANCING

JT03520047

THE COUNCIL,

HAVING REGARD to Article 5 b) of the Convention on the Organisation for Economic Co-operation and Development of 14 December 1960;

HAVING REGARD to the standards developed by the OECD in the area of Small- and Medium-sized Enterprises (hereafter “SME”) and entrepreneurship, financial markets, public and corporate governance, financial consumer protection and literacy, access and sharing of data, good statistical practice, regulatory policy, productivity and inclusive growth, digitalisation, green growth and public procurement;

HAVING REGARD to the work and standards developed by other international organisations relevant in the area of SME financing, in particular on the access and sharing of credit information;

RECOGNISING that SMEs, including micro-enterprises, are important engines of innovation, growth, job creation and social cohesion in high income and emerging economies, as well as low-income developing countries (LIDCs);

RECOGNISING that, despite their key economic and social role, SMEs experience gaps in relation to larger companies with respect to access to finance, owing to information opacity, under-collateralisation, high transaction costs and insufficient financial skills;

RECOGNISING that SMEs operate in a rapidly evolving environment shaped by the green and digital transitions, which may require investments, and compliance with standards and regulations, which represent a challenge for SMEs due to more limited skills and financial resources;

RECOGNISING that the twin transitions also represent an opportunity for SMEs and entrepreneurs to strengthen and expand their businesses through the means of digitalisation and more sustainable production and, therefore, contribute to growth and the achievement of global environmental targets;

RECOGNISING that participation in global markets and global supply chains continues to represent an important channel of growth and productivity for SMEs, but that this requires adequate policy support, including in terms of finance;

RECOGNISING that cross-cutting policy strategies to enhance SMEs’ access to finance are needed to provide a coherent framework for government actions in this area, within the broader policy ecosystem for SMEs;

RECOGNISING that SME financing policies have a broad and varied scope, ranging from policies to strengthen framework conditions and support the wider business community, to measures specifically targeted to SMEs, and involve a variety of actors and institutions across multiple levels of government;

RECOGNISING that while bank financing will continue to be crucial for the SME sector across all economies, the need to develop a more diversified set of options for SME financing remains pressing, in order to reduce the vulnerability of SMEs to changes in credit market conditions, strengthen their capital structure, seize growth opportunities and boost long-term investment;

RECOGNISING the role of diverse stakeholders in SME financing ecosystems including, among others, SME representatives and business associations, Central Banks, financial market regulators, public and commercial banks, development finance institutions, equity financiers and Fintech organisations, as well as the value of social dialogue and public-private sector co-operation for effective policy design and implementation;

NOTING that the present Recommendation embodies the 2022 Updated G20/OECD High-Level Principles on SME Financing, first developed in April 2015, welcomed by G20 Leaders and subsequently included in the Compendium of Standards of the Financial Stability Board (FSB) and which were revised in June 2022 by the CSMEE and welcomed by the G20 FMCBG in their July (see Chair's Summary) and October 2022 (see Chair's Summary) meetings and by G20 Leaders in November 2022 (see Leaders' Declaration);

On the proposal of the Committee on Small- and Medium-Sized Enterprises and Entrepreneurship:

I. **RECOMMENDS** that Members and non-Members having adhered to this Recommendation (hereafter the "Adherents") develop cross-cutting policy strategies to enhance SMEs' access to finance, as well as a framework for the monitoring and evaluation of these strategies. To this effect, Adherents should:

1. **Identify SME financing needs and gaps and improve the evidence base** by:

   a. Assessing the extent to which SMEs' financing needs are met and where gaps exist, including through a strong evidence base and a better understanding of SME financing needs and challenges by public authorities and financial suppliers, and in co-operation with relevant stakeholders, such as central banks and financial supervisory authorities, financial and research institutions, financial sector organisations and SME representatives, among others;
   b. Improving statistical information on SME and entrepreneurship financing;
   c. Adapting policy solutions to the heterogeneity of SMEs and SME financing conditions;
   d. Collecting and disseminating more disaggregated data, including breakdowns by size, sector, location, age and stage of development of the firm, legal form of the firm, and gender of the business owner, in order to tailor SME financing policy strategies to specific business needs, as well as longitudinal data to assess impacts of finance over time; and
   e. Encouraging co-operation at the national and international levels among relevant stakeholders in order to increase transparency regarding definitions; improve the comparability of data and indicators, within and across countries, and regulatory co-ordination; and shed light on outstanding financing gaps, issues and good practices.

2. **Improve transparency in SME finance markets** by:

   a. Reducing information asymmetries in finance markets to encourage greater investor participation and reduce financing costs for SMEs;
   b. Ensuring that information infrastructures for credit risk assessment support an accurate evaluation of the risk involved in SME financing;
   c. Standardising, to the extent possible and appropriate, credit risk information and making it accessible, in line with data protection standards, to relevant market participants and policy makers to foster both debt and non-debt SME financing, including by making such infrastructure available online;
   d. Supporting accessibility of this information at the international level to foster SMEs' cross-border activities and participation in global value chains taking into consideration the implications for data privacy and use; and

e. Considering open banking and other arrangements, which also support competition in the banking sector, while ensuring data protection and privacy rights.

3. **Design and implement regulations that support a range of financing instruments for SMEs, while ensuring financial stability and investor protection** by:

a. Taking measures so that regulations are proportionate to the risks of different financing instruments and profiles of investors, including those offered by Fintech institutions, while also considering their impact in terms of financial inclusion:
b. Taking into account the combined effects of regulations on SME finance and avoiding unnecessary regulatory fragmentation;
c. Avoiding undue administrative and reporting burdens for SMEs in the area of finance, including through digitalisation, where appropriate, and providing adequate measures on insolvency proceedings;
d. Ensuring that the flexibility provided to SMEs, particularly in the equity space, is compatible with investor protection, integrity of market participants, corporate governance, and transparency;
e. Encouraging good corporate governance in SMEs to enhance their access to equity markets;
f. Designing legal, tax and regulatory frameworks that foster the development of diverse sources of finance; and
g. Supporting international regulatory coordination to promote cross-border financing for SMEs.

4. **Promote financial inclusion for SMEs and ease access to formal financial services, including for informal firms,** by:

a. Maximising the number of SMEs which have access to and use formal financial services and products at a reasonable cost and mobilising financial inclusion as an important tool to reduce business and labour informality;
b. Ensuring that national financial inclusion strategies include a review of the legal and regulatory framework of the financial sector; define a public intervention strategy and identify appropriate delivery instruments; and offer tools for groups excluded from or underrepresented in the formal banking sector;
c. Providing adequate attention to microfinance schemes, particularly in developing countries, to enhance entrepreneurs' access to small amounts of funding at a more affordable cost; and
d. Harnessing the potential of financial technologies (Fintech) and Fintech institutions to extend banking and other financial services to wider segments of the population.

5. **Enhance SMEs' financial skills and strategic vision in order to enable them to develop a long-term strategic approach to finance and improve business resilience and prospects** by:

a. Supporting the financial literacy of SME managers, as a way to improve their awareness, understanding and ability to use a broad range of available financial instruments, including alternative and digital ones, and to be aware of changes in legislation, public support and programmes for SMEs;
b. Collecting evidence on the financial skills of SME managers to inform such efforts;
c. Encouraging SME managers to devote due attention to finance issues, acquire skills (including digital skills and understanding of sustainable finance issues) for accounting and financial and risk planning, improve communication with investors and respond to disclosure requirements;

d. Supporting efforts that aim to improve the quality of start-ups' business plans and SME investment projects, especially for the riskier segment of the market; and
e. Tailoring programmes to the needs, levels of financial literacy and levels of digitalisation of different constituencies and target groups, including groups that are underserved by financial markets and that have limited digital access and skills, and to different stages in the SME business cycle, including early stages.

6. **Strengthen SME access to traditional bank financing** by:

a. Pursuing efforts to improve banks' capacity to lend to SMEs through measures that may include credit guarantees, securitisation, credit insurance, credit mediation, and adequate provisioning for loan losses;
b. Strengthening risk mitigation measures by making use of new technologies and mechanisms for underwriting risk, while recognising the role of relationship lending in easing access to finance for SMEs and related risks;
c. Fostering effective and predictable insolvency regimes that ensure creditor rights while supporting healthy companies and offering a second chance for entrepreneurs who have gone through a transparent and orderly insolvency process;
d. Ensuring that SMEs are afforded credit on reasonable terms, taking into consideration macroeconomic and credit market conditions, and with appropriate consumer protection measures in place;
e. Enabling the use of a broader set of assets beyond fixed collateral by SMEs to secure loans, including through the establishment of collateral registries for moveable assets and through careful consideration of the use of intangible assets, including intellectual property rights, as collateral (particularly for knowledge-based companies and start-ups);
f. Fostering the use of verifiable credit information to improve credit risk management for lenders and access to funding for borrowers; and
g. Exploring the use of consumer-permissioned alternative data, including online data, to enhance credit risk assessment, while ensuring privacy and personal data protection.

7. **Enable SMEs to access diverse non-traditional financing instruments and channels** by:

a. Fostering access to a sufficiently broad range of SME financing instruments in order to obtain the form and volume of financing best suited to SMEs' specific needs and the stage of the firm life cycle, as well as to reduce SME vulnerabilities to financial shocks, recognising the complementary nature of the role of banks and other financing channels, including Fintech institutions;
b. Supporting multiple and competing sources of finance for SMEs as well as undertaking targeted outreach efforts to increase entrepreneurs' awareness of the available financing options;
c. Supporting the development of alternative financial instruments for SMEs that aim to attract a wider range of investors, including institutional investors, and to enhance their understanding of SME markets;
d. Fostering asset-based finance to enable young and small firms to finance working capital on rapid and flexible terms;
e. Encouraging supply chain and trade finance to support the integration of SMEs in national and global value chains;
f. Encouraging sustainable and transition finance to support the integration of SMEs in these markets;

g. Enhancing alternative forms of debt to enable SMEs to invest, expand and restructure;
h. Providing due policy attention to the development of hybrid tools and equity and quasi-equity instruments to strengthen SMEs' capital structure and boost investment in innovative start-ups and high-growth SMEs, while giving special consideration to venture and private equity financing, including capital for seed, early and later stage investments.

8. **Leverage the role of financial technologies, Fintech institutions and digital relationships to reduce barriers in SMEs' access to finance** by:

a. Encouraging responsible financial innovation, including through bank and non-bank partnerships, that supports the provision of affordable SME financing, reaches underserved market segments and regions, and increases competition among providers of financial services
b. Enabling financial technologies and Fintech institutions that generate consumer-permissioned alternative data and use machine-learning models to enhance credit risk assessment, including through collaboration with traditional financial institutions and especially in underserved markets where information asymmetries are more pronounced;
c. Leveraging Fintech institutions to disburse loans more rapidly and to provide SMEs with the types of financing suited to their needs
d. Fostering digital banking to reduce transaction costs in banking services, simplify customer relationship management, and offer product-based finance solutions;
e. Encouraging digital payment systems that can support SMEs through safer and timelier payments, modernised point of sale services, increased transparency of transactions and improved bookkeeping, while reducing transaction costs in banking services and simplifying customer relationship management;
f. Exploring innovation through experimentation, including through the use of regulatory sandboxes;
g. Ensuring that regulatory frameworks for new Fintech institutions take a technology-neutral approach and reducing unnecessary regulatory barriers to entry for Fintech providers of financial instruments for SMEs;
h. Monitoring and sharing information across countries on regulatory and supervisory approaches to Fintech; and
i. Taking due account of consumer protection concerns, including the collection and use of personal data and the security of transactions on digital platforms.

9. **Strengthen the availability and uptake of sustainable finance for SMEs** by:

a. Facilitating SMEs' access to a range of tailored sustainable finance instruments suitable to their diverse needs and ambitions to enable them to contribute to reaching climate and other sustainability-related objectives;
b. Complementing financial support with non-financial support, including resources, tools, digital and Fintech solutions and educational services, in order to close gaps in SMEs' awareness and knowledge of sustainable finance, improve SMEs' reporting capabilities, strengthen investment-readiness and boost SMEs' demand for and access to sustainable finance;
c. Promoting the inter-operability of definitions, data, taxonomies, and methodologies related to the measurement of environmental, social and governance (ESG) factors and integration of ESG standards to support the demand for and supply of sustainable finance; and

d. Considering proportionality in sustainability reporting requirements, including for SMEs in the supply chains of reporting enterprises, in line with SMEs' ability to measure and report on their ESG data performance and efforts; and flexible timelines for the implementation of climate- and sustainability-related disclosures and considerations, including transition plans, in SMEs' business practices, while supporting capacity building for reporting and compliance.

10. **Strengthen the resilience of SME finance in times of crisis** by:

a. Ensuring the rapid delivery of SME financing programmes to support liquidity in times of crisis, including through the simplification of eligibility requirements and procedures, while safeguarding accountability;
b. Mobilising a wide range of instruments and traditional and non-traditional channels, including by leveraging relationship lending and digital delivery systems;
c. Reaching vulnerable SMEs and entrepreneurs that may be disproportionately affected by crises and may face challenges in accessing existing policy measures;
d. Monitoring the implementation and uptake of support measures and adjusting them as appropriate during the crisis;
e. Considering reductions of broad-based support and shifts towards more targeted measures during the recovery phase, including those that contribute to structural objectives; and
f. Managing the phasing out of exceptional support measures through carefully designed and well-communicated exit strategies, in order to enable viable firms to adjust to their withdrawal.

11. **Encourage timely payments in commercial transactions and public procurement** by:

a. Fostering transparency in Business to Business (B2B) and Government to Business (G2B) transactions to enhance the cash flow of small business suppliers, while recognising that timely payments are often essential in the cash-flow management strategies of small companies;
b. Ensuring that SMEs, which are particularly vulnerable to late payments or non-payment, are offered clear and appropriate payment terms which are respected in practice; and
c. Designing, implementing and enforcing domestic laws that discourage late payments in commercial transactions, including for cross-border trade.

12. **Design public programmes for SME finance which ensure additionality, cost effectiveness and user-friendliness** by:

a. Pursuing policy coherence across all levels of government and between government and non-government bodies dealing with SME finance, based on reliable evidence;
b. Defining target populations, eligibility criteria, credit risk management and fee structures in public programmes which are easy to understand for SMEs; and
c. Ensuring that the administrative burden and compliance costs of new and existing policies are proportionate to the service provided, the impact on beneficiary firms and the broader economy, as well as to the nature and size of the targeted businesses.

13. **Adopt principles of risk sharing for government-supported SME finance instruments** by:

a. Fostering public programmes that help catalyse and leverage the provision of private resources, especially in risk capital markets, recognising that, under certain conditions, public schemes can be effective in kick-starting the offer of SME financing;
b. Leveraging private resources and competencies to enhance the resilience of SME financing, particularly in the face of rapid economic and regulatory change;
c. Designing policies that aim to encourage the participation of private investors and develop appropriate risk-sharing and mitigating mechanisms with private partners to ensure proper functioning of public measures, including the allocation of government resources to their most efficient use, the avoidance of excessive risk-taking against the public interest (i.e. moral hazard), and potential crowding-out effects; and
d. Encouraging multilateral development banks, national development banks, public funds and other public and private institutions to promote SME financing, including sustainable finance for SMEs, directly and indirectly, in particular when SMEs are underserved by commercial banks.

14. **Monitor and evaluate public programmes to enhance SME finance** by:

a. Promoting regular ex ante and ex post evaluation based on clearly defined, rigorous and measurable policy objectives and impacts, and in co-operation with financial institutions, regulators, SME representatives and other stakeholders;
b. Ensuring that evaluation findings feed back into the process of policy making, in particular when measures fail to meet their stated objectives or are found to have undesirable impacts;
c. Using new data, depending on availability, to potentially produce more timely evaluation results, while maintaining appropriate standards of confidentiality;
d. Pursuing the establishment of national and international core metrics for the evaluation of SME financing programmes in order to help improve benchmarking of the impact of these programmes within and across countries; and
e. Encouraging regional, national and international policy dialogue and exchange of experiences on how to monitor and evaluate public programmes to enhance SME financing.

II. **ENCOURAGES** relevant stakeholders, including financial institutions and SME associations, to disseminate and follow this Recommendation;

III. **INVITES** the Secretary-General and Adherents to disseminate this Recommendation.

IV. **INVITES** non-Adherents to take account of and adhere to this Recommendation.

V. **INSTRUCTS** the Committee on SMEs and Entrepreneurship to:

a) Serve as a forum for exchanging information and experience with respect to the implementation of this Recommendation through a multi-stakeholder and interdisciplinary dialogue on SME and entrepreneurship financing;

b) Support the efforts of Adherents to implement this Recommendation through continued analysis of specific SME financing instruments and policies, data collection and development of indicators; and

c) Report to Council on the implementation, dissemination and continued relevance of this Recommendation no later than five years following its adoption and at least every ten years thereafter.