# The Impact of the Global Crisis on SME and Entrepreneurship Financing and Policy Responses

Contribution to the OECD Strategic Response to the Financial and Economic Crisis

Centre for Entrepreneurship, SMEs and Local Development

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# FOREWORD

Access to financing continues to be one of the most significant challenges for the creation, survival and growth of SMEs, especially innovative ones. The problem is strongly exacerbated by the financial and economic crisis as SMEs and entrepreneurs have suffered a double shock: a drastic drop in demand for goods and services and a tightening in credit terms, which are severely affecting their cash flows. Governments are responding generally by three types of measures aimed at: *i*) supporting sales and preventing depletion of SMEs' working capital; *ii*) enhancing SME's access to liquidity; *iii*) helping SMEs to maintain their investment level. The present report brings to the attention of governments recommendations to tackle the long-standing deficiencies in the SME financial environment, as well as to prepare SMEs and entrepreneurs for a phase of innovation-led growth.

In October 2008, the OECD Working Party on SMEs and Entrepreneurship (WPSMEE) started a debate on the impact of the global crisis on SMEs and entrepreneurs' access to finance and on government responses in this area. A survey among member and non-member countries was subsequently conducted in January and February 2009 to gather information on the situation and on the measures adopted or to be adopted by governments, in order to contribute to *the OECD Strategic Response to the Financial and Economic Crisis* launched by the Secretary General. Twenty-nine countries, the European Commission and the European Investment Fund responded to the questionnaire. The results of this exercise were discussed at the *Turin Round Table*, which was held in Italy on 26-27 March 2009, under the auspices of the WPSMEE at the invitation of Banca Intesa Sanpaolo.



This report, entitled *The Impact of the Global Crisis on SME and Entrepreneurship Financing and Policy Responses,* presents the findings of the survey and the outcome of the discussion at the Turin Round Table, which gathered more than 100 participants from thirty seven countries/ economies and international financial institutions.

The report has been prepared by a team of the SME and Entrepreneurship Division of the OECD Centre for Entrepreneurship, SMEs and Local Development (CFE), led by Marie-Florence Estimé (Deputy Director, CFE) and including Yasuhiko Yoshida and Jorge Galvez Mendez, together with Lorraine Ruffing (Consultant, Senior Advisor to UNCTAD). Paul Dembinski (Director, Observatoire de la Finance, Geneva) and his team, and Glenda Napier (FORA, Copenhagen), sponsored by Switzerland and Denmark respectively, provided important inputs.

Both the report and the Turin Round Table benefited from the close guidance of the WPSMEE informal Steering Group on SME and Entrepreneurship Financing, chaired by Salvatore Zecchini, President, IPI, Italy. The report also reflects valuable comments expressed by WPSMEE delegates and delegates of the Committee on Industry, Innovation and Entrepreneurship (CIIE), its parent committee.

The report was transmitted to the OECD Secretary General Angel Gurría, by Ken Warwick (United Kingdom), Chairman of the Committee on Industry, Innovation and Entrepreneurship (CIIE) and Jacques Augustin (France), Chairman of the WPSMEE, as an input to the *OECD Strategic Response to the Global Crisis,* and its Executive Summary will be part of the background documentation for the upcoming meeting of the OECD Council at Ministerial level (MCM) on 23-24 June 2009.

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# EXECUTIVE SUMMARY

## *Background*

Access to financing continues to be one of the most significant challenges for the creation, survival and growth of SMEs[1] especially innovative ones. The problem is being exacerbated by the most severe financial and economic crises in decades. Financing has been a key area of work for the OECD Working Party on SMEs and Entrepreneurship (WPSMEE) for several years. In June 2004, *Financing Innovative SMEs in a Global Economy* was one of the themes addressed by the 2nd OECD SME Ministerial Meeting in Istanbul. In March 2006, the *OECD Global Conference on Better Financing for Entrepreneurship and SME Growth*, held in Brasilia, assessed the SME financing gap. Further work and research on *Financing Innovative and High- Growth SMEs* was carried out in 2007-2008. In October 2008 the 34th Session of WPSMEE engaged in a preliminary exchange of views on the impact of the global crisis on SME and entrepreneurship financing and discussed strategies so far adopted by governments to deal with the problem.

In order to further the debate on policy responses to the global crisis, a Round Table on the *Impact of the Global Crisis on SME and Entrepreneurship Financing and Policy Responses*[2] was held in Turin on 26-27 March 2009 under the auspices of the OECD WPSMEE and hosted by Intesa Sanpaolo. The Turin Round Table had before it an issues paper which was based on the responses of 29 OECD Members and non-Members, as well as the European Commission and the European Investment Fund, to a questionnaire which covered the supply of financing to SMEs, their demand for financing, the credit conditions, loan approvals and defaults as well as information on equity financing. The responses also described in detail the policy measures taken by governments for SME and entrepreneurship financing. The presentations and discussions of the Turin Round Table have been incorporated into this report. The Round Table was an important milestone in the WPSMEE's commitment to contribute to the OECD Strategic Response to the Financial and Economic Crisis which may have persistent effects on SME and entrepreneurship financing. The outcomes of the Turin Round Table will be further developed for the OECD High-level (possibly Ministerial) Meeting on SMEs and Entrepreneurship, "Bologna + 10", to be held in November 2010.

1 There is no single agreed definition of what constitutes a SME. A variety of definitions are applied among OECD member countries and non member economies, and the number of employees is not the sole defining criterion. Generally speaking, the OECD WPSMEE considers SMEs as non-subsidiary, independent firms which employ less than a given number of employees.

2 The Turin Round Table was attended by more than 100 participants from 37 countries/economies [OECD Members: Australia, Austria, Belgium, Canada, Czech Republic, Denmark, Finland, France, Germany, Greece, Hungary, Ireland, Italy, Japan, Korea, Luxembourg, Mexico, Netherlands, Poland, Portugal, Slovak Republic, Spain, Sweden, Switzerland, Turkey, United Kingdom, United States -- Non OECD Members: Chile, Chinese Taipei, Indonesia, Malaysia, Peru, Philippines, Romania, Russian Federation, South Africa, Thailand], the European Commission (EC), the Business and Industry Advisory Committee to the OECD (BIAC), the Trade Union Advisory Committee to the OECD (TUAC), 4 international financial institutions [the European Association of Mutual Guarantee Societies (AECM), the Bank for international Settlements (BIS), the European Central Bank (ECB), the European Investment Fund (EIF)] and an international organisation [the International Labour Organisation (ILO)].

## Importance of SMEs in "normal times" and in times of crisis

SMEs and entrepreneurs play a significant role in all economies and are the key generators of employment and income, and drivers of innovation and growth. In the OECD area, SMEs employ more than half of the labour force in the private sector. In the European Union, they account for over 99 % of all enterprises. Furthermore, 91 % of these enterprises are micro-firms with less than 10 workers. Given their importance in all economies, they are essential for the economic recovery.

Even in 'normal' economic conditions governments have recognised that, to survive and grow, SMEs need specific policies and programmes – hence the comprehensive range of SME measures currently in place across the OECD members. However, at the present time, SMEs have been especially hard hit by the global crisis. These firms are more vulnerable now for many reasons: not only has the traditional challenge of accessing finance continued to apply, but new, particularly supply-side, difficulties are currently apparent. It is important to stress that SMEs are generally more vulnerable in times of crisis for many reasons among which are:

- it is more difficult for them to downsize as they are already small;
- they are individually less diversified in their economic activities;
- they have a weaker financial structure (i.e. lower capitalisation);
- they have a lower or no credit rating;
- they are heavily dependent on credit and
- they have fewer financing options.

SMEs in global value chains are even more vulnerable as they often bear the brunt of the difficulties of the large firms.

## Impact of the global crisis on SME and entrepreneurship financing

Although there is no internationally agreed definition of small and medium sized enterprises (SMEs), the evidence suggests that these firms are being affected by the financial and economic crisis across economies. There is evidence that SMEs in most countries are confronted with a clear downturn in demand for goods and services if not a demand slump in the fourth quarter of 2008. Many expect a further worsening to come. For SMEs there are two related stress factors: a) increased payment delays on receivables which added - together with an increase in inventories- result in an endemic shortage of working capital and a decrease in liquidity and b) an increase in reported defaults, insolvencies and bankruptcies.

*Extended payment delays on receivables, especially in times of reduced sales, are leading rapidly to a depletion of working capital in many countries*. For example, in Belgium 43 % of surveyed SMEs recently experienced extended delays in their receivables and in the Netherlands 50 % of SMEs have to deal with longer payment terms from their customers. In New Zealand, the share of enterprises waiting over 60 days for payment has risen dramatically from 4.8 % to 29.5 % between February 2007 and 2008. In Denmark, Italy, Ireland, Norway and Spain the surge in corporate insolvencies was higher than 25 %. In Finland, while short-term solvency problems among SMEs normally involve 6-8 % of these firms, in January 2009 more than 17 % of small firms with less than 50 employees declared insolvency problems. In Sweden, according to ALMI (the Swedish state owned Development Bank), bankruptcies increased over 50% in the first two months of 2009 compared to the same period in 2008.

*Increased insolvency rates appear to confirm SMEs' increased inability to obtain short-term financing*. In all countries using the Bankers' Lending Survey method, the tightening of credit conditions by banks[3] was clearly evident for all the banks' clients. The European Central Bank (ECB) data also confirmed the tightening. The ECB attributes the tightening to the banks' ability (or inability) to access capital, the banks' liquidity positions, expectations regarding the recession and higher risk on collateral. Interest rate spreads have risen to unprecedented levels, thereby partially offsetting the effects of the easing of monetary policy. The main factors exacerbating the banks' attitude towards lending to SMEs are: a) the poor SME economic prospects already discussed; b) stagnation in inter-bank lending and increased cost of capital; and c) the desire to rebuild bank balance sheets. In all reporting countries, banks are under pressure and are trying to preserve or strengthen their capital base. As a result, they are seeking fully collateralised transactions. In consequence, by choosing to keep only the strongest clients, banks and other financial institutions are contributing to a polarisation process. For example, Korea reported that lending to blue-chip SMEs has increased whereas lending to SMEs with poorer credit ratings has deteriorated. For many banks this may be a sensible survival strategy and their survival is vital. In some countries it is also a case of returning to "normal" lending practices after a number of years of excessive flexibility and generosity in lending.

*The stagnation in lending is true even of banks in countries where governments have deliberately strengthened banks' balance sheets to allow them to grant additional credit to SMEs and/or where credit guarantee schemes exist*. As it will be seen later in the summary, most countries have not only recapitalised their banks, but also extended the funds and guarantees available for SME financing. But the effects of the incentives to lend to SMEs put in place by governments in some countries (such as the provision of additional capital) have not yet yielded the desired results. Some governments are closely monitoring this situation or have put in place "credit mediators" to ease the flow of credit to SMEs or have enacted binding codes of conduct for SME lending.

3 Loan conditions encompass many aspects among which the most important are the spread between banks cost of funds and their interest rate, their commissions and fees, the difference between the amounts granted and those demanded by enterprises; the level of collateral required, and the duration of loans.

During the Round Table there was much discussion about the fact that large banks have evolved into very complex institutions where loan decision making is centralised and based on automated credit assessment systems. Thus, SMEs often lack face-to-face contact with bank managers who understand their specificities. Inappropriate and indiscriminate use of credit scoring mechanisms can lead even deserving SMEs to be denied credit. To some extent, a proper use of individual assessment through "relationship banking" can counteract this, and it has survived in some countries because the banking sector is composed of many "local" or "regional" banks which have been less affected by the crisis, are liquid, and continue to lend to SMEs (Switzerland and the United States, for example). There are also some large banks that are preserving "relationship banking" at the local level (in Italy, Intesa Sanpaolo is one of them and in Indonesia, the Bank Rakyat).

*Confronted with worsening access to credit, SMEs are exploring alternative sources of finance such as the mobilisation of reserves, self-financing and factoring*. Access to venture capital and private equity also appears to be constrained but there are no official statistical data available covering the fourth quarter of 2008. The financial crisis has had a three-fold impact on venture capital and private equity markets. *First,* exit opportunities are reduced. *Second,* fundraising activities seem to be shrinking. *And thirdly,* invested capital has stagnated or even slowly started to decline, especially investments in new projects.



*Global venture capital fundraising slowed down between 2007 and 2008*. The current economic recession and the global downward pressure on prices are expected to influence the future prospects for fundraising in the markets in the long run. Institutional investors providing funding will simply be less willing to supply new funds with fresh capital. Figures from Canada confirm the global trend as fundraising has decreased by roughly 25 % in 2007 and 2 % in 2008. Similar declines have been registered in Australia and the UK.

Under the influence of these trends, public funds (both direct and indirect investment funds) will be impacted as much as the private funds. In markets with public or semi-public investment funds, which provide capital to funds-of-funds activities, such public funds are likely to witness a more limited possibility for co-investment with private funds, simply because the private funds increasingly reduce their investment activities. As a result, public funds cannot be expected to provide the same leverage effect as before the crisis, unless supplied with more capital.

## *Policy responses of governments*

The participants in the Round Table stressed that the appropriate broader framework conditions are a critical determinant for SME financing. Indeed there is a need for "reliable governance, tax, regulatory and legal frameworks that provide a level playing field for all economic entities irrespective of size" as stated in the *OECD Brasilia Action Statement on SME and Entrepreneurship Financing* (March 2006). In particular, participants noted that any government measures taken to ease SME financing should not impair fair competition and should avoid contributing to a rise in protectionism.

Countries' abilities to deal with the crisis depend to a large extent on the margin provided by their respective fiscal and monetary policies. Many of the reporting countries have recently put in place anti-crisis packages combining in different proportions three lines of action: *stimulation of demand* (consumption packages, infrastructure programmes, tax policies); *credit enhancement* measures, including *recapitalisation of banks* which, in some cases, include explicit provisions or mechanisms to preserve or enhance banks' capacity for financing SMEs such as public credit guarantees; and *labour-market measures* (reduced employment taxes or social security charges and extended temporary unemployment programs).

*The anti-crisis packages and accompanying measures address, in many countries, the financing problems of SMEs*. The measures put in place by countries can be classified in three different groups: (a) measures supporting sales and preventing depletion of SMEs' working capital such as export credit and insurance, factoring for receivables, tax reductions and deferrals, and better payment discipline by governments, (b) measures to enhance SME's access to finance, mainly to credit through bank recapitalisation and expansion of existing loan and credit guarantee schemes; (c) measures aimed at helping SMEs to maintain their investment level and more generally their capacity to respond in the near future to a possible surge in demand through investment grants and credits, accelerated depreciation, and R&D financing.



*Many governments have implemented measures to maintain or increase cash flows*. For instance, they have allowed accelerated depreciation for investments already undertaken. Some countries are also giving tax credits, cuts, deferrals and refunds. In Japan, the Government has reduced the corporate tax rate from 22 % to 18 % for the SMEs with 8 million yen (€61 thousand) or less in annual income in the coming 2 years. In the Netherlands one of the tax brackets has been reduced from 23 % to 20 % for both 2009 and 2010 for amounts up to 200,000 euros and Canada increased the income threshold for which the small business rate applies. The Czech Republic, France and Spain are refunding VAT payments immediately or monthly. The idea was introduced during the Turin Round Table that governments concentrate first on reducing those taxes that are "profit-insensitive", that is, taxes that are paid regardless of whether the SME is making a profit. This would increase the ability of SMEs to finance working capital internally.

*Governments are taking moves to shorten payment delays for public procurement* (Australia, France, Hungary, Italy, the Netherlands, New Zealand, and UK) and enforce payment discipline (France). The European Commission has suggested that public authorities should pay their bills within 30 days. In parallel, the Commission commits itself to speed up payment of goods and services so to fully respect the targets for paying bills. In the case of the UK it has cut government payment times to 10 days. Governments are also easing tendering and procurement procedures and policies (Australia, France, the Netherlands, New Zealand and the United Kingdom). Lastly, in order to maintain employment, some governments are giving wage subsidies to enterprises so that employees can receive full wages while working part time.

*The most widely used policy measure to increase access to finance has been until now the extension of loans and loan guarantees.* These measures vary widely in their design and execution. Although some measures such as new credit guarantee scheme for working capital by Greece, launched in December 2008, are already showing positive results, time is too short to draw conclusions about what are the "best practices" in the field of emergency measures and in the field of loan guarantees. The OECD WPSMEE has, in the past, identified a few schemes in the field of loan guarantees[4] which could lay the groundwork for future comparisons and evaluations.

*In some countries, the governments have found the response of the newly recapitalised banks to the needs of SMEs unsatisfactory or insufficient even though guarantees are available.* These countries have resorted to discipline measures that in some cases complement the incentives, in order to pressure banks to continue lending to enterprises. Belgium and France have appointed a *"credit mediator",* who at regional and central levels, may intervene to ease difficulties and help enterprises obtain bank funding. The US has chosen to strictly monitor, on a monthly basis, the credit activities of banks that have been rescued by public funding. Furthermore, it is requiring all banks to report on a quarterly basis. Ireland has enacted a legally binding code of conduct on SME bank lending. The Belgian Ministry for SMEs is giving pre-fund agreements directly to SMEs which can be taken to the banks to obtain guaranteed loans.



## Proposals for Further Action

The discussions during the Turin Round Table revealed the participants' sense of urgency to alleviate the shortage of working capital SMEs are facing. SMEs are caught in a vicious circle because of the causal connections between the demand shock and the decline in working capital. At the same time the impaired credit markets are not responding to the SMEs' need for liquidity. As was highlighted during the Round Table, "… a downward spiral has been created which is damaging the fabric of many economies". Therefore, governments were urged to review the policy measures already taken with the aim of reinforcing them or complementing them with new measures. The Round Table distinguished between the short-term emergency measures such as tax measures that could be reversed and the long-term measures which need to be undertaken to make structural improvements and institutional changes in the SME financial environment in order to restore growth.

4 Cf. OECD Framework for the Evaluation of SME and Entrepreneurship Policies and Programmes, OECD 2007.

In addition to the policy measures reviewed above, countries may wish to consider the following policy recommendations related to measures which are more institutional or structural in nature to remedy the long-standing deficiencies in the SME financial environment:

- Encourage banking competition across economies and, to alleviate the stagnation in bank lending, consider the *monitoring of SME lending by banks* through timely reporting and the establishment of *a code of conduct for SME lending by banks.*
- To know the real situation of SMEs, policy makers also need more timely and SME specific data on the supply of and demand for financing so that they can determine if their measures are working. Already several OECD countries are improving transparency in bank lending by encouraging the timely public disclosure by banks of the composition of their loan portfolios by size of firm.
- As SMEs often lack face-to-face contact with bank managers due to the current impersonal structure of the modern banking system, banks could consider using their scoring methods for assessing SME credit-worthiness with appropriate discretion so that *adequate room would be left for the specificities of the client, as happens with "relationship banking"*. Appropriately balanced use of any assessment method could help in cases where the circumstances and viability of individual businesses can be accounted for. Consequently, staffing local branches with personnel who have adequate skills in dealing with SME lending becomes important. Banks could also enter partnerships with business service providers to help them reduce the risks in SME lending.
- Evidence was offered that automatic systems of credit evaluation do not always function to the effect that viable companies can obtain credit, which could be addressed with a more appropriate and discriminate use of these methods. Systems are needed to evaluate the credit risk of SMEs on a company basis rather than on a sectoral basis, while being consistent with prudential management practices in terms of sectoral allocation of funds.
- The specific financing needs of micro-enterprises (less than 10 employees in the EU) which dominate the SME sector were considered at the Round Table. Research on start-ups by the Ewing Marion Kauffman Foundation (United States) revealed that they also need modest capital injections and that the most important source was outside credit averaging USD 32,000. This could be provided through micro-finance in countries which do not already have such schemes.
- Improving the means by which SMEs are informed about the availability of SME-related government support measures, especially those that are responses to the current crisis, is crucial for the implementation of government policy

and programmes. It could be facilitated in partnership with business service providers or business associations. As indicated in the OECD Brasilia Action Statement "…*informing SMEs of the range of financing options (e.g., public guarantee programmes, business angels, and bank loans) will ensure greater take-up of schemes*".

- Also competence building should spur the demand for financing among SMEs. The managerial competencies of SMEs—especially in the field of finance—have to be supported. Governments should take the opportunity offered by SME owners' realisation that they did not have all the skills needed to help their firms survive the crisis to encourage participation in general managerial skills development, including mentoring and business advice.
- SMEs should be engaged in the design of relevant finance-related policies and programmes from the outset to ensure that their perspectives and needs are well understood and taken into account. Examples were given of regular communication and consultation with the representatives of SMEs through forums and round tables to raise awareness and to assess the effectiveness of existing measures and programmes to help SMEs to access finance.

## *Preparing SMEs and entrepreneurs for recovery and innovation-led growth*



It was also noted that the crisis brings certain opportunities to improve the SME legal framework and the business environment. The crisis could accelerate the redeployment of resources to new activities. Emerging firms and those redesigning their processes should be encouraged to focus on sustainability and knowledge-based outcomes.

Both the Istanbul Ministerial Declaration on Fostering the Growth of Innovative and Internationally Competitive SMEs (2004) and the OECD Brasilia Action Statement on SME and Entrepreneurship Financing (2006) acknowledged that SMEs' financing requirements differ at each stage of their development. In particular innovative SMEs need have access to appropriately structured risk capital.

The OECD Brasilia Action Statement highlighted the fact that access to appropriate types of financing structures and facilities are especially required to allow SMEs and entrepreneurs to take advantage of the opportunities provided by innovation.

The Statement proposes actions which could contribute to preparing SMEs and entrepreneurs for recovery and innovation-led growth which are relevant in the current situation.

- *"A lack of appropriate financing notably represents a hindrance to the creation and expansion of innovative SMEs (...). Comprehensive efforts are needed to bolster the early stages (i.e. pre-seed, seed and start-up) of SMEs, which are marked by negative cash flows and untried business models. This can be done by entrepreneurs themselves leveraging the capital lying dormant in their personal assets, or by "business angel networks" or venture capital markets (...). Successful approaches to developing early stage venture capital markets include both tax-based programmes and programmes that use government's ability to leverage private risk capital such as co-investment.*
- *Business incubators, clusters of innovative SMEs, science and technology parks, and development agencies play an important role in facilitating appropriate access to financing for SMEs at local and regional level. Cities and regions can underpin and strengthen this function through partnerships with private financial institutions and universities. Appropriate financial incentives can correct market failures and stimulate equity investment in local enterprises.*
- *There is a need to promote enhanced awareness, educate and communicate more broadly the value of equity financing, including raising the recognition among entrepreneurs of fair value and transparency in valuing investments.*
- *The combined legal, tax and regulatory framework should ensure that risk capital is not discriminated against, including by safeguarding orderly, equitable and transparent exit routes. Taxes should not put SMEs, entrepreneurs or their financial backers at a disadvantage. There should be neutrality between alternative sources of risk capital, such as domestic versus foreign venture capital funds. Maintaining neutrality between debt and equity should also be an aim for tax policies.*
- *There is no venture capital without venture capitalists and business angels greatly enhance the effectiveness of informal finance. Representing an evolving entrepreneurial breed, these actors thrive on their ability and courage to assume risk. Obstacles should be identified and eliminated. Effective role models can also be promoted to spur the dynamism of these actors. Ways should be explored to facilitate the establishment of "business angel networks", which may greatly enhance information and capital flows."*



The review of measures recently implemented by Governments reveals the paucity of measures directed to venture capital. As such, there is some scope to provide additional incentives to encourage investors to participate in venture capital funds or to act as business angels. Governments may want to consider greater support for venture capital such as increasing guarantees for risk capital and/or more co-investment as well as fiscal incentives such as tax credits for venture capital investments, or tax reductions on capital gains from venture capital investments and enhanced efforts to prepare SMEs to be more 'investment-ready'. In sum, governments should not stop with the current short-term measures for SME survival but consider the medium and long-term measures for preparing SMEs and entrepreneurs for recovery and innovation-led growth.

## *Proposed Role for the OECD*

One of the principal recommendations in the *Brasilia Action Statement* was that the OECD consider the development of definitions, indicators, and methodologies for gathering data on the supply of financing available to SMEs and the demand for financing by SMEs. In response to this recommendation, the OECD has already undertaken the following:

- A review of terminology on business financing used by national and international organisations;
- An overview and assessment of some of the main sources of data on both the supply of and demand for financing for SMEs;
- A collection of policies and programmes related to SME and entrepreneurship financing, in particular to financing innovative and high growth SMEs.



In light of the extreme importance of data availability for effective policy responses, as revealed by the current global crisis, the OECD should continue efforts to improve availability and international comparability of data sets on SME and Entrepreneurship Financing. The OECD Working Party on SMEs and Entrepreneurship (WPSMEE), in close cooperation with its parent Committee, the CIIE:

- Could *promote* a *Scoreboard on SME and entrepreneurship financing data and policies* (a pilot project will be carried out in the framework of the 2009-2010 programme of work in view of the "Bologna +10" High level Meeting) ; *and*
- Should *monitor, report on, and discuss SME and entrepreneurship financing trends on a regular basis.*

As a follow-up, the WPSMEE should also carry out, in the framework of its programme of work 2009-2010, an *assessment of the effectiveness of measures* taken to assist SMEs and entrepreneurs in weathering the financial and economic crisis, as reported in the present report.

Finally, the OECD should also continue facilitating the *Tripartite Dialogue between governments, SMEs and the financial institutions,* to periodically review progress in strengthening SME and entrepreneurship financing.

# I. BACKGROUND

SMEs and entrepreneurs play a significant role in all economies and are key agents of employment, innovation and growth. A significant number of entrepreneurs and SMEs could use funds productively if they were available, but are often denied access to financing, thus impeding their creation, survival and growth. Although SMEs form a broad spectrum as far as their relative size, sector of activity, seniority, location and performance are concerned, there is a vital need for innovative solutions for their financing in particular for innovative and high- growth SMEs in a globalised knowledge-based economy.

Financing has always been a key area of work for the OECD Working Party on SMEs (WPSMEE). In June 2004, the theme *Financing Innovative SMEs in a Global Economy* was discussed by Ministers at the 2nd OECD SME Ministerial Meeting in Istanbul. In March 2006, the Brasilia Conference on *Better Financing for Entrepreneurship and SME Growth* assessed the SME "financing (debt and equity) gap". The *OECD Brasilia Action Statement for SME and Entrepreneurship Financing*, which was issued at the end of the Conference, stressed that the financing gaps are not insurmountable and can be mitigated by a series of actions. The WPSMEE has been pursuing research in this area and carried out work in 2007-2008 on *Financing Innovative and High Growth SMEs.* In late October 2008 on the occasion of its 34th Session WPSMEE delegates engaged in a preliminary exchange of views on the impact of the global crisis on SME and entrepreneurship financing, and discussed the strategies so far adopted by governments in dealing with the problem and what should be done next.



It was recognised that in the current context of the most severe financial and economic crisis in decades, various factors such as increased risk aversion, decreased liquidity, bleak prospects for economic growth, etc. are having or are expected to have a highly negative effect on SMEs and entrepreneurs' access to short and long term financing. Small firms are particularly vulnerable because a) it is more difficult for them to downsize since they are already small, b) they are individually less diversified in their activities, c) they have weaker financial structures or lower capitalisation, d) they have lower or no credit ratings, e) they are heavily dependent on credit, and f) they have fewer options for finance, especially in financial markets. With this in view, the measures that most governments are taking or planning to take to counteract the effects of the crisis and stimulate their economies should include easing SME and entrepreneurship access to finance.

To further the debate on policy responses to the crisis, and also to discuss how to ensure that these responses are consistent with the medium and long- term actions taken by governments which can help accelerate the recovery and foster SME growth in the long term, the Turin Round Table on *the Impact of the Global Crisis on SME and Entrepreneurship Financing and Policy Responses* was held on 26-27 March 2009 under the auspices of the WPSMEE and hosted by Intesa Sanpaolo.

The present report is based on an Issues Paper prepared for the Turin Round Table and was subsequently enriched by the presentations and debate at the Round Table and comments received afterward. The report analyses the country responses (OECD members and non-members) to a survey launched in mid-January 2009 covering data on the situation of SME and entrepreneurship financing and information on policy measures, as well as publicly available information. Responses to the questionnaire were provided by 29 governments[5], the European Commission and the European Investment Fund.

This document is divided into i) *background,* ii) *the impact of the global crisis on SME and entrepreneurship financing iii) the policy responses, existing and proposed and iv) preparing SMEs and entrepreneurs for recovery and innovation-led growth and v) the proposed role of the OECD.*

The Executive Summary of the present paper will be part of the background documentation of the OECD Meeting of the Council at Ministerial Level (24-25 June 2009), in the context of the OECD's Strategic Response to the Financial and Economic Crisis.



5 Australia, Austria, Belgium, Canada, Czech Republic, Denmark, Finland, France, Germany, Greece, Hungary, Italy, Japan, Korea, Luxembourg, Mexico, Netherlands, New Zealand, Poland, Spain, Switzerland, United Kingdom, Brazil, Romania, Russia, Slovenia, Thailand, Chile and Estonia.

# II. IMPACT OF THE CRISIS ON SMEs AND ENTREPRENEURSHIP FINANCING

## A. SMEs under stress – the indicators

### The demand shock

The national responses and other publicly available information provide some indications about the effective and expected movements in levels of sales of SMEs. As shown in the Table 1, SMEs in most countries reported a clear downturn in demand for goods and services, if not a demand slump, in Q4-2008 and expect a further worsening to come. The magnitude of the reported shock is severe, but it differs from country to country, in part due to the differences in methods of assessment in each country.

**Table 1: Indications on the magnitude of demand shock**

| Country | Assessment of intensity of experienced or expected demand shock |
|---|---|
| Australia | According to a survey conducted among small enterprises only (firms employing up to 19 employees), more than 1/2 reported either an increase or no change in sales;. In terms of anticipations, almost 2/3 were expecting a recession to occur within the next year. According to another survey covering enterprises with up to 199 employees, business confidence fell during the Q1-2009 to its lowest level, also showing a record low in the sales performance indicator. Only around 31 per cent of enterprises reported facing no problems in their business. Lack of work or sales is the primary concern of SMEs Q1-2009, remaining close to its highest level since May 1998. Medium-sized businesses were more confident than small businesses. |
| Belgium | According to an "Access to Finance" survey, 60% of respondents report falling sales as the main manifestation of the crisis, followed by a worsening of their financial condition (52%) and extension of their clients' payment delays. |
| Canada | According to Business Barometer (Dec 2008) : 29% of SME owners say their performance in 2008 was much stronger than in 2007, while 40% say performance is much worse or somewhat worse. Only 17% expect improvement and 44% anticipates worsening performance. |
| Finland | For a majority of SMEs, orders or pre-orders have been postponed (47%) or cancelled (24%) during the last few months. Demand conditions were worsening further from Q3-2008, when postponed orders affected 34% and cancellations 14% of SMEs. |
| Germany | According to the National Federation of Independent Businesses, in Q4-2008 poor sales were seen as the single most important problem for 25% of businesses, while financial issues were a top concern for about the same proportion of enterprises. |
| Greece | The current economic crisis has affected businesses in different ways: for 58% it has been through insufficient working capital, for 55% by way of insufficient sales. |
| Italy | According to Eurostat, retail trade volume fell by 4.9% in December 2008 compared to December 2007 (new car registrations fell by 17.2%). According to Istat (National Institute of Statistics), exports in 2008 rose by 2% compared to 2007, but fell during the last quarter (5.5% in December 2008 as compared to December 2007. Industrial orders in manufacturing fell by 13.1% in December 2008 compared to the same period of 2007. Business confidence recorded in the ISAE (Institute of Studies and Economic Analysis) surveys has fallen in recent months to all-time lows in all the sectors. |

| Country | Assessment of intensity of experienced or expected demand shock |
|---|---|
| Sweden | During Q4-2008, 29% of respondents to a recent survey reported that the volume of total new orders slumped at a very high rate, 47% of respondents reported a high rate, 15% reported that it was unchanged and 7 % of respondents reported an increase. |
| New Zealand | On a seasonally adjusted basis, a net 44% of firms reported a drop in their own activity Q4-2008, which is the worst result for this measure since at least 1970. In addition, a net 43% of firms expected a drop in their activity for the Q1-2009 quarter. In a survey of mid-February, 60.9% of the 659 surveyed firms reported that their sales/revenue has decreased (somewhat or greatly) in the last three months. |
| United Kingdom | A recent survey found that the volume of total new orders during Q4-2008 slumped at its fastest rate since July 1991. Of the SME manufacturers surveyed, 54% reported a fall of new orders compared to only 13% reporting an increase. SMEs report that demand is by far the biggest factor to constrain output. The British Chambers of Commerce Economic Survey found a similar decline in manufacturing demand, as well as declines for SMEs in the service sector. |
| United States | The rate of owners (seasonally adjusted) reporting higher sales in the previous three months lost 4 points, falling to a net negative 29 %, the worst reading in survey history. The Index of Small Business Optimism fell 2.6 points to 85.2 (1986=100), the second lowest reading in the 35 year history of the survey. |

Source: Country Responses to the OECD WPSMEE Questionnaire on the Impact of the Global Crisis on SMEs and Entrepreneurship Financing and the Policy Responses, launched on 14 January 2009 and publicly available information.

Countries not included in this table, such as Chile, Japan, Korea, Mexico and the Netherlands also report that SMEs have suffered poor sales. In Luxembourg, information from the Chamber of Commerce and the Chamber of Crafts indicate that demand and economic activity are falling in comparison to the last years. Although not yet a demand slump, Luxembourg authorities are concerned by the declines. In Hungary, surveys show that the self-employed have the worst business expectations, while optimism increases with firm size. Although general, the fall in demand hit some sectors or activities with particular force: construction (Finland, Netherlands); automotive supplies and manufacturing (Slovenia, Netherlands, India, Italy); wholesale (Italy); semiconductors (Netherlands); exports (Chile, Denmark, India, Thailand).



The above mentioned evidence suggests that the experienced and expected fall in sales is having a strong impact on SMEs. This is further supported by two additional stress indicators: (a) increased payment delays on receivables which add –together with an increase in inventories - to an endemic shortage of SMEs' working capital and a decrease in liquidity; and (b) an increase in reported defaults, insolvencies, and bankruptcies.

## *Increased payment delays*

Extended payment delays on receivables, especially in times of reduced sales, rapidly leads to a depletion of working capital and may entail frequent liquidity or even insolvency problems. In Belgium, 43 % of surveyed SMEs recently experienced extended delays in their receivables while 14 % reacted by extending their own payment delays. In New Zealand, the share of enterprises waiting over sixty days for payment has risen dramatically from 4.8 % a year ago to 29.5 % in mid-February. In the Netherlands, 50 % of SMEs have to deal with longer payment terms from their customers. In France, payment delays have been identified as a major problem for SMEs. An Observatory of payment delays was set up there in 2006 (see annex 1). Australia, Canada, Italy, Korea, Mexico and the UK also report payment delays as a growing problem. Governments are aware that if SMEs cannot quickly obtain additional funding this will lead to insolvencies and they are taking action to prevent this as will be seen in section III.

*Increase in enterprise insolvencies and bankruptcies*

Reduced demand rapidly depletes working capital in the smallest firms. Insolvency frequently increases if short- term financing cannot be obtained. According to "Insolvencies in Europe 2008/09" (Creditreform), the total number of insolvencies increased by 11 % between 2007 and 2008. In some countries like Denmark, Italy, Ireland, Norway, and Spain the surge in corporate insolvencies was higher than 25 %. The Confederation of Finnish Industries found in its January 2009 survey that among the small firms (less than 50 employees) the incidence of solvency problems was more than 17% compared to the usual 6-8%. Furthermore, 51 % of the sample reported some increase in their clients' insolvency problems. A review by size indicated the most significant increase in insolvency problems was for medium-sized enterprises. These trends have to be interpreted with great caution because legislation on insolvency and bankruptcies differs greatly by country, and so do statistical reporting methodologies – which means that the figures may not capture short-term changes. In order to have a proper reading of such figures, they should be put in longer-term perspective. With regard to corporate liquidations, data from New Zealand shows that company liquidations are increasing and the twelve month moving average is trending upwards, as are receiverships and creditor initiated bankruptcies. At the Round Table Sweden reported that bankruptcies had increased over 50 % in the first two months of 2009 compared to the previous year. Normally viable businesses were going into bankruptcy unnecessarily because of the lack of working capital.



## B. SMEs' reactions

The response of the surviving SMEs to the double pressure of falling sales and extended payment delays in a general context of bleak medium-terms perspectives is – in theory - three fold: (a) cost-cutting to restore profitability and adjustment of production to lower demand levels, measures that materialise mainly in a reduced wage bill; (b) search for additional sources of liquidity (extending own payment delays, reducing or suppressing dividends – if any); (c) postponing of investment and expansion plans, when possible (including M&A activity for the small subset of high- growth SMEs). In the case of entrepreneurship, this could simply mean the postponement or even the cancellation of new business ventures.

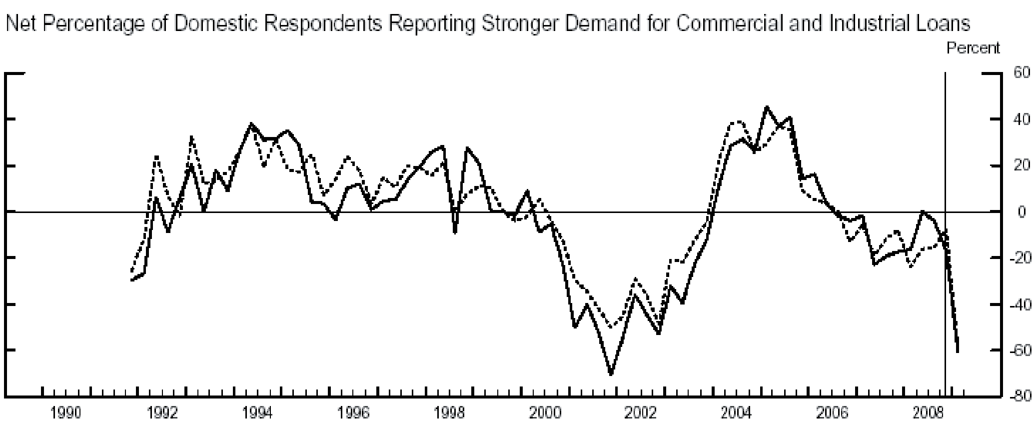
Among the possible SME responses to the demand shock for goods and services, cost-cutting and lay-offs and the subsequent labour market impacts are clearly outside the terms of reference of the present paper which is focused on financial considerations. The next three sections are devoted to identifying how the SMEs' responses have affected their demand for credit, how the lending conditions of banks and other financial intermediaries have changed, and what is the availability of equity and venture capital in the new situation.

## C. SMEs' demand for bank credit

The assessment of credit demand is difficult from the methodological point of view. Some countries use the Bank Lending Survey (BLS) method to capture changes in demand as perceived by bank officials. These responses are weighted according to the relevant bank's market share and presented as a balance of opinions: the weighted percentage that sees an increase in demand minus the weighted percentage that see a decrease in demand. The evidence from countries applying this methodology (presented in Annex 2) clearly shows (a) the overall slump in credit demand is being experienced in all countries but one in Q4-2008 and is expected to last in Q1-2009 even if its severity varies from country to country; (b) in all countries the reduction of credit demand for investment or acquisition purposes is extremely severe (50% or more of respondents); (c) SMEs' demand for credit in Italy, and to a lesser extent Germany, did not change so dramatically when compared to their French, British and US counterparts.



**Figure 1: Demand for credit in the US**




*Source*: Federal Reserve, Senior Loan Officer Opinion Survey on Bank Lending Practices, released February 2, 2009

In countries either not using or not publishing BLS results, the evidence provided refers to the many SMEs that feel frustrated in accessing credit and not to changes in the level of demand as such. In Australia, almost 50 % of small business feel it is harder to borrow funds now, in comparison to 12 months ago; in the Netherlands, one out of five SMEs was looking for additional funding in 2008. During the Round Table, Canada reported that one out of four SMEs were underfinanced and Spain said that more than 80 % of SMEs have problems in accessing financing. In contrast, in Finland or New Zealand less than 10 % of SMEs were facing major difficulties in obtaining working capital or investment funding.

The overall SME reactions that emerge from the available information suggest that entrepreneurs are not willing to increase their indebtedness despite the fact that sales fall and payment delays increase. Facing an uncertain future, this reaction is fully rational especially when these enterprises are confronted with tightened credit conditions imposed by banks and other creditors.

## *D. Tightened credit conditions*

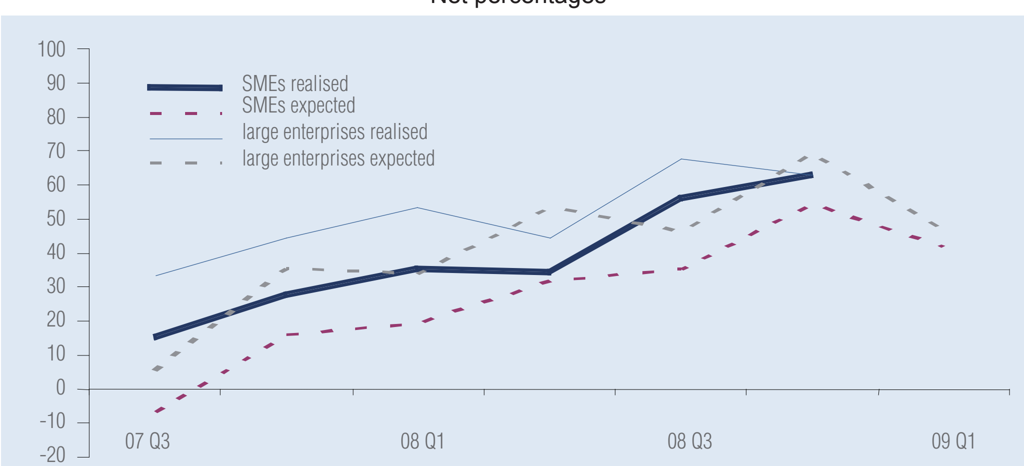
Loan conditions encompass many dimensions among which the most important are the spread between the banks and other financial intermediaries' cost of funds and interest levels, the commissions, the difference between the amounts granted and those demanded by the enterprises, the level of collateral required, the duration of the loans, and processing delays. In all countries using the BLS methodology, the tightening of SME credit conditions by banks is clearly visible for all the banks' clients. This being said (see Annex 3), in some countries – Germany and France - SMEs seem to have been slightly less affected than larger enterprises, while the reverse is true in the US.

Figure 2 shows the tightening of credit standards for enterprise loans as calculated by the European Central Bank. There has been an increased tightening since mid-2008 due to the banks' inability to access capital, the banks' liquidity position, expectations regarding the recession and higher risk on collateral.



**Figure 2: Tightening of credit standards for loans to enterprises, SMEs and large enterprises**

Net percentages

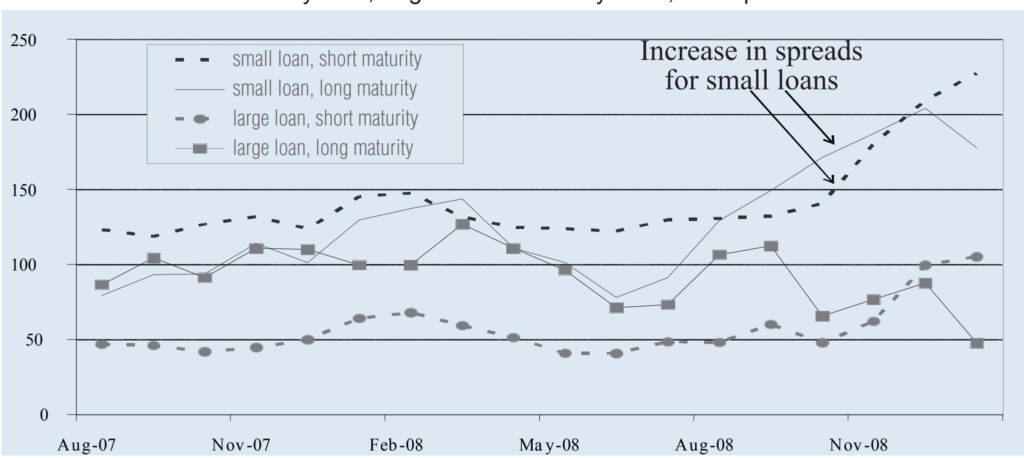



*Source*: European Central Bank

The above mentioned evidence suggests that (1) SMEs (and enterprises in general) have strongly reduced their investment projects financed by credit; (2) SMEs demand for working capital and short-term loans has been reduced in some countries but not as dramatically as for investment purposes; (3) banks have tightened their lending policies in terms of security guarantees and amounts, but not exclusively towards SMEs; (4) in some countries banks and other financial intermediaries have substantially increased the cost (and spread) of credit to all their clients, which may appear paradoxical in a situation of a general fall in interest rates. The European Central Bank reported a dramatic increase in bank spreads in the late 2008 for small loans. The Round Table participants were struck by the fact that interest rate spreads had risen to exceptionally high levels, thereby partially offsetting the effects of the easing of monetary policy.

**Figure 3: Bank spreads on small and large loans to non-financial corporations**

Monthly data, August 2007-January 2009, basis points




*Source*: European Central Bank



In consequence, this evidence suggests that in addition to the demand shock described above, conditions under which SMEs can access credit have significantly worsened in some reporting countries. If this is true, then the enterprises in general and SMEs in particular are, de facto, exposed to two different shocks reinforcing each other: a demand slump or downturn and a financial shock due to banks and other financial intermediaries' reluctance to lend.

*Banks and other financial intermediaries' strategy and constraints*

Three factors may have exacerbated the banks and other financial intermediaries' attitude towards lending to SMEs: (a) poor SME economic prospects (already discussed), (b) the stagnation in inter-bank lending and the increased cost of capital and (c) balance sheet constraints. In all reporting countries, banks and other financial intermediaries are under pressure and are trying to preserve or strengthen their capital base. As part of this strategy they are seeking fully collateralised transactions that minimise the use of their economic (as opposed to regulatory) capital. In consequence, by choosing to keep only the strongest among their existing clients, banks and other financial intermediaries are contributing to a polarisation process. For example, Korea reported that lending to blue-chip SMEs has increased whereas lending to SMEs with poorer credit ratings has deteriorated. In some countries, banks have reduced lending not just because risk has gone up, but also because they are having difficulty raising new funds overseas and are directly affected by the substantially reduced access to short term inter-bank funding at other than very expensive rates resulting from a significant deterioration in banks' confidence in the banking sector's general level of solvency and credit rating.

**Table 2: *Experienced or expected* impacts of the crisis on SME and entrepreneurship financing**

| | Impacts on SMEs (Cf. Table 1) | | | SME demand for credit (Cf. Annex 2) | | |
|---|---|---|---|---|---|---|
| | Demand | Working capital & Payment delays | Exits (Insolvencies and bankruptcies) | Total | Short-term | Long-term |
| **OECD** | | | | | | |
| Australia | | + | | | | |
| Austria | | | = | | | |
| Belgium | - - - | + + | + | - | | - |
| Canada | - - | + | - | + | | |
| Czech Republic | | | = | | | |
| Denmark | | | + + | | | |
| Finland | - - | + + | + | | | |
| France | | + | + | - - - | | |
| Germany | - | | = | - | | - - |
| Greece | - - - | + | = | | | |
| Hungary | | | + | | + | - |
| Ireland | | | + + + | | | |
| Italy | - | + | + + | - | = | - |
| Japan | - | + | | | | |
| Korea | - | + | | | + | - |
| Luxembourg | - | + | + | - | | |
| Mexico | - | + | | | | |
| Netherlands | - | + | - - | | | |
| New Zealand | - - | + + | + | | | - - |
| Poland | - | | | + | | |
| Spain | | | + + + | | | |
| Switzerland | | | = | | | |
| UK | - - | + | + | - - | + | - - - |
| USA | - - | | | - - - | + | - - - |
| EC | | | | - - | - - | - - - |
| **Non OECD** | | | | | | |
| Chile | - | | | | | |
| Estonia | | | = | | | |
| Romania | | | | | | |
| Russia | + | + | | | | |
| Slovenia | | | = | | | |
| Thailand | | | | | | |

Note: One or more "+" signs (depending on the intensity) indicate that the information points out to an experienced or expected increase on the impacts for the indicators in each column. A "=" sign indicates no change, and one or more "-" signs indicate an expected or experienced decrease.

Source: Country Reponses to the 14 January 2009 OECD WPSMEE Questionnaire on the Impact of the Global Crisis on SMEs and Entrepreneurship Financing and publicly available information, including Creditreform (2009) Insolvencies in Europe 2008/09 and Opora Russia.

During the Round Table there was much discussion about the fact that large banks have evolved into very complex institutions where loan decision making is centralised and based on automated credit assessment systems. Thus, SMEs often lack face-to-face contact with bank managers who understand their business. It is the large, troubled banks which are now refusing to lend working capital to SMEs. Under local branch banking these SMEs might have been judged as viable. There are a few countries where the banking sector is composed of many "local" and "regional" banks which have been less affected by the crisis, are liquid and continue to lend to SMEs. It was reported that in the United States, for example, there are approximately 8,000 small commercial banks (in addition to non-bank lenders) whose capital has not been impaired by the credit market collapse. These banks compete with each other to provide lending and other services to consumers and small businesses, and as a result in the US small businesses had not reported in 2008 a sudden freezing up of capital flows. Similarly, Switzerland, due to the duality of its banking system (two big banks which have a significant share of the market, and suffered from the consequences of the crisis) is not suffering from a credit crunch: *regional banks* provide 75% of the credit demanded by SMEs and they currently have strong liquidity. There are also some large banks that are aiming at preserving "relationship banking" at the local level:  in Italy, Intesa Sanpaolo is one of them and in Indonesia, the Bank Rakyat has joined forces with other institutions (NGOs, microfinance institutions, etc.) to reach SMEs in remote areas.



Already before the financial crisis structural changes within the banking sector had put additional constraints on SME lending for financial intermediaries. One tool to mitigate these constraints and to improve the access to finance for SMEs is SME loan securitisation [in both forms: synthetic (mainly for capital relief purposes; only the risk of the portfolio is transferred) and true sale (mainly for funding purposes; originator sells a homogenous set of assets)]. This rather young market segment is now suffering from contagion effects from the general adverse securitisation environment, including uncertainties stemming from methodological adjustments by the rating agencies. Although exaggerations in the securitisation industry have caused the financial crisis, this market in general played and plays an important economic role but is currently severely affected. For the SME loan securitisation as a niche market segment, the investor base is now limited to specialised investors and the number of new transactions that came to the market in Europe in 2008 and so far in 2009 has significantly decreased. The new synthetic SME loan balance sheet transactions in some countries are driven by Basel II and only the mezzanine tranche(s) are offered, whereas the other tranches are retained by the originators. The majority of true sale securitisations are retained by banks mostly for the purpose of accessing central bank liquidity.

The stagnation in lending is true even of banks in countries where governments have deliberately strengthened banks' balance sheets to allow them to grant additional credit to SMEs and/or where credit guarantee schemes exist. As will be seen in the next section most countries have not only recapitalised their banks but also extended the funds and guarantees available for SME financing. But the effects of the incentives to lend to SMEs put in place by governments in some countries (such as the provision of additional capital) have not yet yielded the desired results. Some governments are closely monitoring this situation or have put in place "credit mediators" to ease the flow of credit to SMEs. Such actions will be further described in section III.

Some question whether the current regulatory framework under Basel II has caused deterioration in SMEs' access to credit. As the box below explains there is no evidence of this. In fact under Basel II there is preferential treatment for SME lending. SMEs can be treated as "retail" if certain conditions are met and this results in a reduced risk weighting. However, if Basel II is revised in the wake of the financial crisis, governments could assess the possible effects on SME lending (see Box 1).

**Box 1: SMEs and the regulatory framework of Basel II**

Many of the revisions of Basel II since the first draft of 2001 have been intended to render the rules more flexible. Amongst the beneficiaries of these revisions are SMEs.

These revisions have included a downward adjustment in the weighting for credit risk of SMEs in the Internal Ratings-based Approach of Basel II, a downward shift in the curve relating probability of default to the regulatory capital requirements, and a flattening of its slope. The downward shift is expected to increase the number of firms for which minimum regulatory capital requirements under Basel II would not be greater than under Basel 1. The flattening of the curve would reduce the procyclical impact on bank lending of Basel II's weightings for credit risk by slowing the rise in capital requirements in response to the rise of the probability of default. Small SMEs could also be the beneficiaries of lower risk weights for retail exposures.



A number of estimates of the quantitative impact of these revisions suggest that they will have the desired effect of reducing the risk weights and thus the minimum regulatory capital requirement for SMEs, thus avoiding adverse effects on SMEs' access to bank finance. However, there is still concern over the potential impact of the introduction of Basel II on lending to SMEs. Reasons for this concern include continuing uncertainty over its pro-cyclicality, despite the revisions of the rules already described, and the way in which changes in the legal framework for banking linked to Basel II and changes in banks' risk management and internal controls are actually introduced at country level.

The introduction of Basel II is intended to be accompanied by more rigorous risk management on the part of banks. However beneficial on other grounds, such risk management can conflict with the relationship-based banking that is closely associated with much lending to SMEs and capable of sustaining lending during economic downturns.

Continuing concern over pro-cyclical effects on bank lending is already evident in information concerning the introduction of special rules directed at mitigating the pro-cyclicality of Basel II in some countries. Unsurprisingly these include developing countries particularly concerned to protect from adverse consequences a category of institutions (SMEs) considered to be an engine of economic development.

Ultimately only experience can show whether Basel II – as implemented today - will result in higher borrowing costs for SMEs or even in some cases their exclusion from borrowing from banks. Governments have considerable flexibility concerning the way in which Basel II is incorporated in their regulatory frameworks (though to a somewhat lesser extent for EU countries for which the rules of Basel II are implemented through the Capital Requirements Directive). Banks in their turn have flexibility over the way in which Basel II is incorporated in their practices as to access to, and pricing of, loans. So long as the authorities remain alert to the possible adverse effects of Basel II, they should be able to take offsetting action without violating the letter or the spirit of the Basel II framework.

## E. Supply of equity, venture capital and alternative sources of financing

Confronted with worsening access to credit, SMEs are exploring alternative sources of finance such as mobilisation of reserves and self-financing (Euro-area, Canada, Thailand); self-financing and factoring (Slovenia) (see Annex 4). Although private equity and venture capital markets have not contributed to the global financial crisis, the extent of the impact the crisis has and will have on entrepreneurs, entrepreneurial firms and SMEs' access to equity financing around the world remains uncertain.



### *Global trends in private equity*

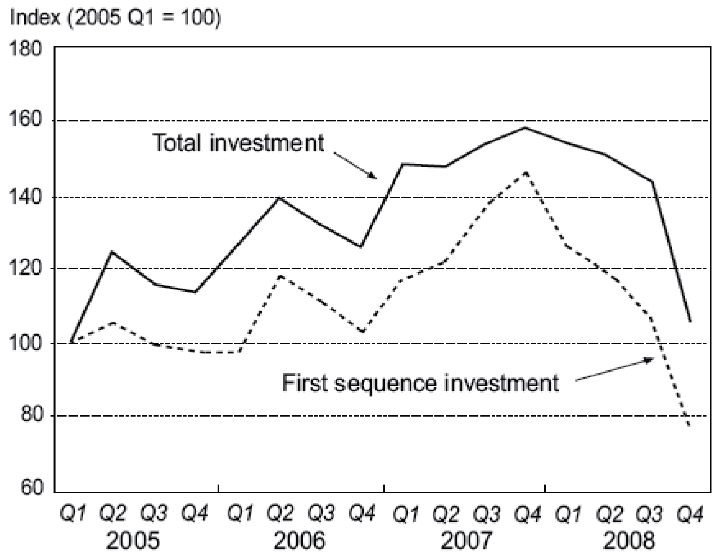
In terms of venture capital and private equity, the information provided is largely anecdotal and for many countries there are no official statistical data available covering 2008. However, new anecdotal information indicates that entrepreneurs, entrepreneurial firms and SMEs find it increasingly difficult to access financing for new projects.

In order to better understand the impact of the financial crisis on the equity markets, some global trends on the private equity market are discussed. Whenever possible, the newest available venture capital and/or private equity data is used to underline these trends.

As is explained in more detail below, the financial crisis has had a three- fold impact on venture capital and private equity markets. First, exit opportunities are reduced. Second, fundraising activities seem to be shrinking. And thirdly, invested capital has stagnated or even slowly started to decline, especially investments in new projects. It is expected that invested capital will see further declines in the coming period. It should be noted that the venture capital market has experienced similar declines after the 2001 economic downturn.

According to data by VentureXpert (a private information source), invested venture capital did not decline between 2007 and 2008. The reason for this apparently steady level of investment was that many of the existing funds raised sufficient capital *before* the crisis. Their mandate is to invest and this short-term obligation to maintain investment levels could very well be a reason for the stable investment level. However, there is a need to understand the apparent flat level of VC investment around the globe, especially when the US, the biggest VC market in the world, experienced an 8 % drop in its VC investment in 2008 compared to 2007 and 26 % drop in the last Q4 2008 compared to Q4 2007. It is also worth mentioning that the financial credit crunch effect varies across countries with some countries like Canada experiencing steep declines. More serious drops in invested capital across the globe are expected in the coming period as a reaction to worsened exit opportunities and difficulties in raising new funds.

**Figure 4: Recent investment trends in the US**




Source: PricewaterhouseCoopers and National Venture Capital Association

## *National trends in venture capital*

According to the Italian private equity and venture capital data from the first semester 2008, 170 new deals were recorded (+11 %) for a total value of €2,772 million (+45 % on first semester 2007 figures). The market dynamism in the first semester is confirmed by the increase in the amounts invested in start ups (+35 % on first semester 2007 figures). However, as the crisis did not really unfold until the last quarter of 2008, it is expected that data from this quarter would show a decrease in investment.

In Australia, the supply of venture capital from 'business angels' to companies participating in the COMET programme (a government programme providing financial assistance and business development advice to very young companies to enable them to grow and become more attractive to private sector investors) has decreased in the period from June 2008 to January 2009 in comparison to the period June 2007 to January 2008. From June 2008 to January 2009, there was AUD $19 million (€10.3 million) invested by business angels compared to AUD $29 million (€15.8 million) in the period June 2007 to January 2008. Indicators for the investment funds for exit and fundraising data show a similar downward trend.

Due to the financial crisis, exit opportunities also seem severely hit. According to the National Venture Capital Association (NVCA), the most significant impact of the US financial crisis on the venture capital industry has clearly taken place in the exit markets. Falling prices on the world's stock markets have made investors turn to more safe investments, which consequently makes it almost impossible to exit a venture capital investment through either an IPO (initial public offering) or a merger or acquisition. In the US, the number of exits and IPOs were historically low in 2008. 2008 brought just six IPO exits, the fewest annual venture-backed offerings since 1977, when there were also six IPO exits. According to the latest figures from the NVCA, IPO profits in 2008 reached USD 470.2 million, the lowest value since 1979 with USD 339.7 million.

As a result, the time it takes from when an investment is made until it can be exited has increased. In 2000, the period before exit would average four years. In 2008, the average period has increased to seven years although it varies between sectors. And this period has gone up between 2007-2008. Because investors find it harder to exit their investment, they are forced to hold on to it longer. As a result, they must provide more follow-up capital to their portfolio firms in order to ensure the survival and development of the firms. New companies/projects are therefore likely to feel the consequences of the crisis first, as investors will be more reluctant to make new investments.



According to the Korean Venture Capital Association, the largest venture capital investors are the Korean Government and corporations. The number of new companies funded by venture capital has been declining as a trend between 2000-2009. The number of exits usually via IPOs on the KOSDAQ has also declined as a trend over time from 171 (2000) to 38 (2008).The Government is increasing the size of the Korean Fund of Funds so that it can take a much larger share in venture funds launched in 2009.

### *Global trends in fundraising activity*

The global fundraising activity has also slowed down between 2007-2008. The current economic recession and the global downward pressure on prices are expected to influence the future prospects for fundraising in the markets in the long run. Institutional investors providing funding will simply be less willing to supply new funds with fresh capital. Figures from Canada confirm the global trend, as fundraising has decreased by roughly 25 % in 2007 and by 2 % in 2008. As a result, the number of new venture capital funds could be lower than expected before the crisis.

In Australia, the Minister for Innovation, Industry, Science and Research consulted with venture capital industry stakeholders in December 2008 and identified that venture capital fund managers were generally unable to raise new capital; the supply of follow-on funding was drying up; institutional investors were seeking to reduce their exposure to risky investments; and, pension funds were seeking to rebalance their investment portfolios and to reduce their exposure to venture capital assets.

Similar trends were found in the United Kingdom. Other than yearly data up to 2007 provided by the British Venture Capital Association, there are no up to date published data on the provision of equity finance during the economic downturn. However, there is anecdotal evidence that VC funds are delaying making investments, and are also having problems raising funds themselves. Exit routes through IPOs are also restricted due to liquidity issues, which may cause investors to hold onto their investments for longer, reducing the flow of capital for new investments.

If the private venture capital and private equity funds do not raise sufficient capital, they will have to reduce the number of investment managers. For many markets this will mean a significant setback in investment and have a negative impact on the development of investment expertise in the markets, and thus make it even harder for entrepreneurial firms and SMEs to survive and grow – in the longer run as well.

### *Possible impacts and policy implications*



Under the influence of these trends, public funds (both direct and indirect investment funds) will be impacted as much as the private funds. In markets with public or semi-public investment funds, which provide capital to funds-of-funds activities, such public funds are likely to witness a more limited possibility for co-investment with private funds, simply because the private funds increasingly reduce their investment activities. As a result, public funds cannot be expected to provide the same leverage effect as before the crisis, unless supplied with more capital.

# III. POLICY RESPONSES OF GOVERNMENTS

## A. Existing measures

Countries' abilities to deal with the crisis depend to a large extent on the margin provided by their respective fiscal and monetary policies. Many of the reporting countries have recently put in place anti-crisis packages combining in different proportions three lines of action: *stimulation of demand* (consumption packages, infrastructure programmes, tax policies); *credit enhancement* measures, including *recapitalisation of banks* which, in some cases, include explicit provisions or mechanisms to preserve or enhance banks' capacity for financing SMEs such as public credit guarantees; and *labour-market measures* (reduced employment taxes or social security charges and extended temporary unemployment programs).

The anti-crisis packages and accompanying measures address, in many countries, more specifically the financing problem of SMEs. According to the preceding analysis, the measures put in place by countries can be classified in three different groups depending on the aspect of the SME financing problem to which they are geared. Three main groups of measures can be distinguished: (a) measures supporting sales, cash flows, and working capital; (b) measures to enhance SME's access to liquidity, mainly to bank lending; (c) measures aimed at helping SMEs to maintain their investment level and more generally to build their capacity to respond in the near future to a possible surge in demand.



### 1. Short-term measures supporting sales, cash flows and working capital

The stimulus packages are intended to revive demand either through consumption or investment spending. Some of the packages include spending on health, education, technology and infrastructure. SMEs in these sectors could benefit either directly or indirectly. More direct are the measures to increase cash flow, thereby contributing to working capital. A robust cash- flow is a condition sine qua non for business development and growth. Many governments have implemented measures to maintain or increase cash flows. For instance, they have allowed accelerated depreciation for investments already undertaken. France and Germany have introduced accelerated depreciation either on all categories of assets or on specific ones as in Germany where depreciation thresholds are targeted to SMEs thereby reducing taxable income. Some countries are also giving tax credits, cuts, deferrals and refunds. In Japan, the Government has reduced the corporate tax rate from 22 % to 18 % for the SMEs with 8 million yen (€61 thousand) or less in annual income in the coming 2 years. In the Netherlands one of the tax brackets has been reduced from 23 % to 20 % for both 2009 and 2010 for amounts up to 200,000 euros and Canada increased the income threshold for which the small business rate applies. The Czech Republic, France and Spain are refunding VAT payments immediately or monthly.

The idea was introduced during the Turin Round Table that governments give preference to reducing those taxes that are "profit-insensitive", that is, taxes that are paid regardless of whether the SME is making a profit. This would increase the ability of SMEs to finance working capital internally. Lastly, in order to maintain employment, some governments are giving wage subsidies to enterprises so that employees can receive full wages while working part time.

To address the depletion of SMEs' working capital, some countries have implemented specific measures that, without involving additional credit lines, are aimed at easing SMEs' liquidity. As mentioned in Annex 5, two main types of instruments are used; either legal moves to shorten payment delays and enforce payment discipline (France) or reduction of government payment delays (Australia, France, Hungary, Italy, the Netherlands, New Zealand, UK). In the case of the UK it has cut government payment delays to 10 days. Governments are also easing tendering and procurement procedures and policies.

Some of the responding countries are highly internationalised economies, and thus depend on export markets. SMEs are among the exporters, either directly, or indirectly through their participation in Global Value Chains. In order to alleviate the sales shock on export markets and strengthen enterprises' liquidity in case of extended international payment delays, many countries have put in place or reinforced existing export financing or guarantee facilities. Annex 5 provides additional details on measures adopted which range from dedicated export credit lines (Canada, Chile, Czech Republic, Denmark, Mexico, Slovenia), credit insurance mechanisms, (Germany, Luxembourg, New Zealand and the Netherlands), investment credit for exporting SMEs (Mexico), and general support for internationalisation and competitiveness of SMEs (Austria, Italy, Spain). These measures either strengthen existing ones or are ex novo creations.



## 2. *Enhancing SMEs' access to liquidity, especially to bank lending*

Despite the fact that in many of the responses, some of the largest banks have been recapitalised with public funds, the evidence from previous sections of this paper suggests that banks have significantly tightened their credit policies. In order to alleviate the effects on SMEs of the twin shock of falling sales and more difficult access to funding, governments are using two different approaches to increase availability of credit to SMEs: (a) on the incentive side, the creation and extension of guarantee schemes for loans to SMEs, or when that fails direct public lending; (b) on the discipline or sanction side, setting targets for SME lending for banks that have been recapitalised by public monies, putting them under administrative monitoring or putting in place specific procedures to solve problems between individual SMEs and banks.

*Incentives: the loan guarantee schemes*

Extension and diversification of public guarantee schemes or, in some cases, even direct lending by public institutions, are among measures being widely used by reporting countries. These policy measures deal with one of the key reasons that may explain banks' reluctance to lend to SMEs that is, their constraint in terms of their capital requirements ratio. According to Basel II methodology, for banks operating under the "standardised approach", the level of capital requirement for a publicly guaranteed credit line is very low or even nil, depending on the extent and the exact modalities of the public guarantee. For banks operating under the "internal rating-based approach", the regulatory capital requirement is very low, if any, and in the last analysis depends on the internal risk model. For this reason, public guarantee schemes for SME credit are expected to be an incentive for bank lending to this segment of clients. It is also worth mentioning that even for guarantee structures without regulatory capital relief, loan guarantee schemes can improve the access to finance for SMEs through economic capital relief as an incentive for banks. For European Union member countries, the potential leverage effect of public guarantees on SME bank lending has been further extended by the decision of the European Commission to temporarily authorise Member States to ease access to finance for companies through subsidised guarantees and loan subsidies for investments. In France, for instance, this easing of rules makes it possible for the guarantee schemes to cover up to 90 % of the risks related to a loan as compared with 50 to 60 % on average before. The United Kingdom guarantees 75 % of the loan and Korea, 100 %. Japan, in principle, guarantees 80 % of the loan but there are some exceptional cases of 100 % coverage. Almost all reporting countries have enhanced, or put in place, a credit guarantee scheme either focused on SMEs or a general one. For example, Greece introduced new credit guarantee scheme, which recorded €2.2 billion credit guarantee provision for SME working capital for its first three months (see Box 2). Exceptions are Australia and New Zealand, which do not have a credit guarantee scheme in the first place as well as Denmark, which has been maintaining its credit guarantee scheme as it was before the crisis.

**Box 2: New credit guarantee scheme for working capital in Greece**

Greece has introduced a new credit guarantee scheme for working capital which is a public-private risk sharing scheme where the Government covers 80% of the risks. The scheme offers fixed interest rate loans for SMEs which have recorded profits in the last three years.

The Credit Guarantee Fund of Small and Very Small Enterprises (TEMPME S.A.) launched in December 2008, the programme "Loan Guarantee and Interest Rate Subsidy for the Working Capital of Small and Micro Enterprises". In this programme, TEMPME S.A. guarantees part of the loans contracted among Small/Micro Enterprises and financial auxiliaries in a way that the entrepreneurial risk is shared. The allocated budget, for the first phase, amounts to 100 million Euros for the interest rate subsidies and to 2.5 billion Euros for the allocation of guarantees. In brief, the programme includes the working capital loan guarantees and full subsidy of interest rates.

The duration of the loan, and thus the duration of guarantee and subsidy, is three years (without a grace period)

- The loans are guaranteed by TEMPME S.A. up to 80%.
- For the remaining 20% that is not guaranteed by TEMPME S.A, the bank does not ask enterprises for any other collateral.
- The interest rate which is covered by TEMPME S.A has been negotiated between TEMPME and the banking sector and has been agreed at EURIBOR +210 base units (2.10%).
- The loan cannot exceed 30% of the average turnover of the last three accounting years and also cannot exceed 350 000 Euros.

The number of the applications approved reached 20,000 and the amount guaranteed reached 2.2 billion Euros in loans for the first three months.



There are also a number of private guarantee schemes. The Association Europeenne de Cautionement Mutuel AECM), which is composed of non-profit organisations giving SME credit guarantees, has provided 55 billion euros for 1.6 million SMEs (roughly 8 % of total SMEs in the EU). AECM members have knowledge of the local context and the SME sector and therefore they can undertake a reliable individual risk analysis of each loan. They also provide additional information to both the bank and the SME partner and act as an interface. From the perspective of the AECM, EU counter-guarantees are extremely useful and value-adding but the Competition and Innovation Programme was suffering from implementation delays and only a few

AECM member organisations have been able to sign their bilateral agreements with the European Investment Fund so far. At the Turin Round Table it was suggested that during the crisis, governments should be more flexible with their counter-guarantee mechanisms and widen their scope to include working capital and widen their terms to include short-term guarantee commitments. The AECM also proposed that banks accepting private guarantees have the respective loans exempted from reserve requirements.

During the Turin Round Table direct lending to SMEs by public institutions such as France's Organisation for SME Support (OSEO), the Belgium Ministry for SMEs, Spain's Instituto de Crédito Oficial (ICO), the Japan Finance Corporation and the Business Development Bank of Canada (BDC) were put forward as another means to provide liquidity in the face of private banks' reluctance to lend to SMEs even with guarantees. In Belgium the Ministry for SMEs provides SMEs with pre-fund agreements which they can take to the banks to obtain a guaranteed loan. Sweden also increased the lending capacity of ALMI's subsidiary SME banks by 50 % and lending demand doubled.

*Mediation and monitoring*



In some countries, the governments have found the response of the newly recapitalised banks to the needs of SMEs unsatisfactory or insufficient. These countries have resorted to discipline measures that in some cases complement the incentives, in order to pressure banks to continue lending to enterprises. Belgium and France have appointed a credit mediator, who at regional and central levels, may intervene to ease difficulties and help solve divergences between enterprises and banks (see Box 3). The UK has established the SME Lending Monitoring Panel. In the US, the Government has chosen to strictly monitor, on a monthly basis, the credit activities of banks that have been rescued by public funding. The first such report has been released in January 2009 under the title "Treasury Department Monthly Lending and Intermediation Snapshot". The purpose of the document is "to provide the Treasury Department and the public with regular insight into the lending trends and intermediation activities – including underwriting, buying and selling of securities, and other activities in capital markets – of the banks that received the most funding via the Capital Purchase Program (CPP). This snapshot seeks to gather information to help answer the question asked by many during this crisis: "Are banks doing what they are supposed to do, providing credit to borrowers in a safe and sound manner?" Furthermore, the US has also required *all* banks to provide information on SME lending in their quarterly reports. Ireland has instituted a legally binding code of conduct for banks' SME lending.

**Box 3: Credit Mediation in France**

Credit mediation was set up in November 2008 in order to assist SMEs to resolve their liquidity problems by maintaining or obtaining credit. To start the process the enterprise must establish a "mediation file" on the website of the Credit Mediator who has been appointed at the national level to coordinate and act as a final "referee". He is assisted by departmental mediators who are the regional directors of the Bank of France. After the file is received, the banks are notified by mail and they have five business days to reply to the enterprise. After this, the departmental mediator has five business days to review the file and indicate how the file should be treated. When the mediator has identified solutions, the enterprise is notified by mail. If the enterprise is not satisfied, it may appeal to the national mediator.

Between November 2008 and February 2009:

- 8 000 enterprises have been seen by credit mediators;
- 90 % are SMEs with less than 50 employees;
- The main cause of referral to the mediator is the need for short-term credit (69 % of referrals);
- The rate of successful mediation within 15 days is 66 %;
- 60 000 jobs have been preserved.



## 3. *Strengthening pro investment measures*

In the context of bleak medium-term prospects amid falling sales, many SMEs have reduced or withheld their investment plans. In consequence, their demand for long- term lending has significantly fallen, as discussed earlier. In order to prevent SMEs from losing their competitive edge in the medium term, and help them to remain ready for the upturn, some governments have put into place measures to strengthen their capital base or to develop their productive capacities, or both. These measures are either tax incentives (US), or provision of specific funding possibilities such as grants (Germany) or credit (Austria, Czech Republic, Germany, Hungary, Spain). On the top of this, the existence of Structural Funds within the European Union gives to new-member countries a margin of maneuvre to support SMEs investment projects in specific technologies, sectors or regions (Romania and the Czech Republic). Annex 6 provides more information on specific instruments used by each country.

## 4. *Strengthening the capital base, private equity and venture capital*

Some countries have addressed the venture capital and equity market within the rescue plan. However, it is uncertain to what extent the list of government interventions have actually been designed as responses to the crisis or were already planned interventions that have been adjusted accordingly. Annex 7 provides some information about the means put in place to strengthen the equity base of SMEs. These range from private-public partnerships (Finland) to ad hoc programmes (Austria, Chile, Hungary, Mexico) and international projects like the Japanese-Hungarian Venture Capital Fund. The UK is setting up the Capital for Enterprise Fund with 75 million pounds (€85 million) in equity and quasi-equity. It is a mix of government and private sector funds. Korea is improving exit opportunities by activating a M&A market and enhancing the KOSDAQ.

Various policy measures are implemented via the European Investment Bank Group's European Investment Fund (EIF)[6]. The EIF provides long term equity financing and guarantees on SME loan portfolios/securitisations to enhance access to finance for SMEs. It has provided 3.5 billion euros in net equity (venture and growth capital portfolio) commitments and 12.3 billion euros in outstanding guarantees and securitisation commitments at the end of 2008. During the Round Table it was mentioned that in its Private Equity Business, the EIF –as a Fund of Funds – sees a severe slowdown in fundraising and problems especially but, not only, for young VC . With regard to the SME loan securitisation, this small, but important market for SME financing, is negatively affected by contagion effects from the general securitisation market. It was noted that the EIF's products cover mainly long term SME financing and that there is little it can do to ease the situation in terms of working capital even for innovative start-ups.



The Australian Government has established the Innovation Investment Follow On Fund to assist high potential young innovative companies to be sustainable through the financial crisis. The capital provided by the Government will be allocated on a competitive basis to selected venture capital fund managers to provide follow-on funding to early-stage innovative companies in their portfolio that have already received funding under specified government programs. Up to AUD 83 million (€45.2 million) will be available over a three year period. Improving SMEs' and entrepreneurs' readiness to receive capital is also very important. In New Zealand, in order to inform small firms of the capital raising process and therefore to make them *"investment ready",* the Government has been providing specialised training assistance to small firms.

6 For details regarding the main policy measures by the EIB/EIF see annexes 4 and 6.

**Box 4: New Zealand's Investment Ready Training**

Investment Ready Training helps businesses learn about the type of finance they require to expand, diversify or commercialise a new concept, and how to access equity funding from investors. It is offered in a series of free workshops as part of Enterprise Training programme which is provided by New Zealand's national economic development agency, New Zealand Trade and Enterprise (NZTE). Investment Ready Training consists of seven modules that are delivered across two half-day workshops.

Owners or managers of small businesses employing fewer than 50 full-time staff are eligible for this training, which is divided into the following modules:

- 1. ***Understanding the capital raising process*** (The alternatives / angel investors and venture capitalists – what are they and how do they work? / What type of funding is appropriate at each stage of business?)
- 2. ***Understanding what investors look for*** (Why do small businesses miss out on venture capital? / What do investors look for?)
- 3. ***Preparing your business case - business plan*** (Six key things investors look for / Starting your own business plan / What kind of deal can you offer?)
- 4. ***Preparing your business case - what is your business worth?*** (The principles of valuation and the key steps in valuing your business / The drivers of value in your business)
- 5. ***Legal implications of raising funds*** (The Securities Act and the exemptions / Background on public issues / Guidelines on private debt legal documentation)
- 6. ***Finding an investor*** (Deal process and timetable /What to provide investors / Critiquing potential investors and identifying/targeting investors / The importance of "the pitch")
- 7. ***Doing the deal*** (Due diligence - what to expect / The negotiation process and key negotiating strategies How and when to use the earn in formula / Legal agreements required)

New Zealand set up this training programme in November 2003: it succeeded a similar programme evaluated in 2005 which reported high rates of repeat attendance.

## Table 3: Policy responses

| | A. Measures supporting sales, cashflows and working capital (Annex 5) | | | | B. Enhancing SME access to liquidity, especially to bank lending (Annex 6) | | C. Strengthening proinvestment measures (Annex 6) | D. Strengthening capital base and private equity and venture capital (Annex 7) |
|---|---|---|---|---|---|---|---|---|
| | Alleviating working capital shortage in the economy | Reducing and easing tax payments | Export facilitation | Easing procurement payment procedures | Creation and extension of loan & guarantee schemes | Mediation and monitoring | | |
| **OECD** | | | | | | | | |
| Australia | | ✔ | | ✔ | | | | ✔ |
| Austria | | | ✔ | | ✔ | | ✔ | ✔ |
| Belgium | | ✔ | | | ✔ | Mediator | | |
| Canada | ✔ | ✔ | ✔ | | ✔ | | | |
| Czech Republic | | | ✔ | | ✔ | | ✔ | |
| Denmark | | ✔ | ✔ | | | | | ✔ |
| Finland | | | | | ✔ | | | ✔ |
| France | ✔ | ✔ | | ✔ | ✔ | Mediator | ✔ | |
| Germany | | | ✔ | | ✔ | | ✔ | |
| Greece | | | | | ✔ | | | |
| Hungary | | | | | ✔ | | ✔ | ✔ |
| Italy | ✔ | ✔ | ✔ | | ✔ | Monitoring | ✔ | |
| Japan | | | | | ✔ | | ✔ | |
| Korea | | | | | ✔ | | | |
| Luxembourg | | | ✔ | | ✔ | | | |
| Mexico | | ✔ | ✔ | | ✔ | | | ✔ |
| Netherlands | ✔ | ✔ | ✔ | ✔ | ✔ | | | |
| New Zealand | | ✔ | ✔ | ✔ | | | | |
| Spain | | | ✔ | | ✔ | | ✔ | |
| Switzerland | | | ✔ | | | | ✔ | |
| UK | | | | ✔ | ✔ | | | ✔ |
| USA | | | | | ✔ | Monitoring | ✔ | |
| EC | | | | | ✔ | | ✔ | |
| **Non-OECD** | | | | | | | | |
| Brazil | | ✔ | ✔ | | ✔ | | | |
| Chile | ✔ | | ✔ | | ✔ | | | ✔ |
| Estonia | | | | | ✔ | | | |
| Romania | | | | | ✔ | | | |
| Russia | | | | | ✔ | | | |
| Slovenia | | | ✔ | | ✔ | | | ✔ |
| Thailand | | | | | ✔ | | | |
| **International Financial Institutions** | | | | | | | | |
| EIB/EIF | | | | | ✔ | | ✔ | ✔ |

Source: Country Reponses to the 14 January 2009 OECD WPSMEE Questionnaire on the Impact of the Global Crisis on SMEs and Entrepreneurship Financing and publicly available information.

## 5. Conclusions on existing measures

Most of the measures described in this paper are very recent and thus have not been evaluated. In consequence it is impossible to identify best practices. This being said, extension of existing credit guarantee schemes is the most widely adopted measure (24 countries). It has to be stressed that these measures help SMEs by solving their immediate liquidity problem, but if the macroeconomic situation continues to worsen, they may only postpone an insolvency problem. In some countries, measures aimed at solving the long-term problem of insufficient own capital base are being taken. They address the issue either by helping enterprises to strengthen their cash-flow and self-financing or by putting in place additional sources of equity capital.

Although the present paper is based on an impressive volume of information from the country responses, a number of questions remain unanswered. Indeed, the evidence provided by reporting countries derives from a variety of surveys with different methodologies which make general conclusions difficult. First, the crisis has been unfolding in many countries with different sequence and timing before hitting the "real" economy; second the reporting methods and indicators used work with different lags. This being said, the convergence of otherwise heterogeneous information is striking on two main points: *the demand shock and the tightened bank lending conditions.* Clearly, SMEs experience additional difficulties today in achieving adequate levels of liquidity, but it is still unclear to what extent they are willing to borrow, on what terms and to what extent they are credit constrained. Indeed, increased borrowing today may result – in case of prolonged poor sales - in over indebtedness tomorrow. In such a situation the current liquidity problem would be transformed in the medium-term into an insolvency one.



Obviously, the banks' attitude towards lending is an important aspect of the issues addressed in this paper. Compelled to revise their business models and lines of activities, most banks are constrained by their poor capital base and sensitive to the fact that investors are putting a premium on the shares of financial institutions that are better capitalised. It is unclear, for the time being, if the evident tightening of lending conditions is linked to the revisions in the financial institutions' strategy, or to their – pro-cyclical - regulatory environment (Basel II), or to the general bleak economic perspectives or to the financial market scepticism towards poorly capitalised banks.

The most widely used policy measure to increase access to finance has been until now the extension of loans and loan guarantees. These measures are also very heterogeneous in their modalities, in their cost and also target groups. Time is too short to draw conclusions about what are the "best practices" in the field of emergency measures and in the field of loan guarantees. The OECD Working Party on SMEs and Entrepreneurship (WPSMEE) has, in the past, identified examples of best practices in the field of loan guarantees[7]

7 Cf. OECD Framework for the Evaluation of SME and Entrepreneurship Policies and Programmes, OECD 2007

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which could lay the groundwork for future comparisons and evaluations. The second most widely used measures are those which improve cash flows such as tax cuts and deferrals, and the adoption of prompter payment schedules for government procurement.

In terms of venture capital and private equity markets, worsened exit opportunities and declining fundraising activities are slowly resulting in lower investment levels. It is expected that investment levels – in particular new investment – will decline further in the coming period. In terms of policy interventions on the venture capital markets, it is uncertain whether the newly introduced policy instruments have been designed following the crisis or planned prior to crisis and since adapted to the new situation.

## B. Proposals for further action

The discussions during the Turin Round Table revealed the participants' sense of urgency to alleviate the shortage of working capital SMEs are facing. SMEs are caught in a vicious circle because of the causal connections between the demand shock, the decline in working capital and the increase in insolvencies. At the same time the impaired credit markets are not responding to the SMEs need for liquidity. Hence a downward spiral has been created which is destroying the backbone of many economies. Therefore, governments were urged to review the policy measures already taken with the aim of reinforcing them or complementing them with new measures. The Round Table distinguished between the short-term emergency measures such as tax measures that could be reversed and the long-term measures which need to be undertaken to make structural improvements and institutional changes in the SME financial environment in order to restore growth.



### 1. Resolving the problem of insufficient working capital

Almost all participants acknowledged that there is an increased problem of insufficient working capital which is threatening the survival of SMEs. Several speakers noted that the situation regarding working capital had deteriorated rapidly at the end of 2008 and worsened in the first quarter of 2009. There is evidence that if steps are not taken to resolve the liquidity crisis, SME exits will increase in the near future.

A number of examples of good practices were put forward to resolve this problem of insufficient working capital.

*Making guarantees effective*

- The most widely used measure has been the extension of SME loans and loan guarantees. What was learned from previous crises was that in order to encourage financial institutions to increase lending, it may also be necessary to utilise government guarantees in tandem with capital injection schemes. In countries where SMEs are export-oriented, governments are also expanding export credit guarantees. However, some banks are still reluctant to take up loan guarantees.

- Participants described the additional measures being taken by their governments such as the creation of *"credit mediators";* the *monitoring of SME lending by banks* through timely reporting and the establishment of a *code of conduct for SME lending by banks*. Another policy response which attracted interest is where the government gives pre-fund agreements directly to the SMEs which then can be taken to the banks to obtain guaranteed loans.

*Dealing with cash flow problems*

- To deal with cash flow problems, countries reported a number of *temporary tax measures* they had undertaken such as tax cuts and deferrals. It was suggested that governments give priority to reducing taxes that are "profit insensitive" that is, taxes which are paid regardless of whether the SME is making a profit (e.g. payroll taxes). Some governments are also *deferring social contributions* by SMEs.
- *SMEs in supply chains* are particularly vulnerable and some governments are *guaranteeing their accounts receivable.* In a number of countries fiscal stimulus packages allocate a percentage of government procurement to SMEs. Another major problem noted by a number of speakers is the increase in *payment delays*. To alleviate cash flow problems some governments are leading the way in paying their SME suppliers within 30 days or less. Furthermore, the European Commission is revising the directive on payment delays in view of improving the payment behaviour.



## 2. Assisting innovative start-ups and high -growth SMEs

There was a general consensus that it is necessary to ensure that innovative start-ups and high- growth SMEs have access to adequate funding in times of economic recession.

- Some governments are stimulating the provision of private risk capital through *co-investment.* They are in line with OECD Brasilia Action Statement which emphasises that "with appropriate incentives for management, public equity funds can operate so as to help catalyse and leverage the provision of private risk capital."
- Some governments are also *reducing or eliminating taxes on capital gains for investment in SMEs by venture capital funds*.

## 3. Improving the SME and entrepreneurship financial environment

In addition to the policy measures reviewed above, measures which are more institutional or structural in nature were proposed during the Round Table that could remedy the long-standing deficiencies in the SME financial environment.

- As SMEs often lack face-to-face contact with bank managers due to the current impersonal structure of the modern banking system, banks could consider balancing their scoring methods for assessing SME credit-worthiness with *adequate room being left for "relationship banking"*. Returning, to some extent, decision making on SME loans to local branches could help in cases where the circumstances and viability of individual businesses need to be better accounted for. Consequently, staffing local branches with personnel who have adequate skills in dealing with SME lending becomes important. Banks could also enter partnerships with business service providers to help them reduce the risks in SME lending. Overall, it needs to be stressed that banks and the financial community are part and parcel of any solution to the SME and entrepreneurs' financing problem. SMEs have to do their part to improve the transparency of their economic and financial conditions, as well as in improving the quality of their credit demand.
- Issues have been raised regarding SMEs and the regulatory framework of Basel II and its pro-cyclical potential effects; when Basel II is revised in response to the financial crisis, governments should assess the possible effects on SME lending.
- Automatic systems of credit evaluation do not always function to the effect that viable companies can obtain credit, which could be addressed with a more appropriate and discriminate use of these methods. Systems are needed to evaluate the credit risk of SMEs on a company basis rather than on a sectoral basis, while being consistent with prudential management practices in terms of sectoral allocation of funds.
- SME loan securitisation is an important element to support the SME financing environment. In order to enable the market to fulfil its function, over regulation as a reaction to the financial crisis should be avoided. However, measures with proper incentive structures are preferable in order to prevent moral hazard and to ensure less complexity/more transparency.
- The specific financing needs of micro-enterprises (less than 10 employees) which dominate the SME sector were considered. Small firms often require modest financing to conduct their business. Research on start-ups by the Kauffman Foundation revealed that they also need modest capital injections and that the most important source was outside credit averaging USD 32,000. This could be provided through micro-finance in countries which do not already have such schemes.

*Improving SME and entrepreneurs' information and competencies*

- Improving the provision of general information on SME-related government measures is crucial for the implementation of government policy and programmes. It could be facilitated in partnership with business service providers or business associations. As indicated in the OECD Brasilia Action statement "…informing SMEs of the range of financing options (e.g., public guarantee programmes, business angels, and bank loans) will ensure greater take-up of schemes".
- Also competence building should spur the demand for financing among SMEs. The managerial competencies of SMEs - especially in the field of finance - have to be supported. In order to improve the level of financial knowledge among SMEs, governments could support business development services and training programmes.

*Facilitating dialogue and consultation between governments, SMEs and financial institutions*

- SMEs should be engaged in the design of relevant finance-related policies and programmes from the outset to ensure that their perspectives and needs are well understood and taken into account. Examples were given of regular communication and consultation with the representatives of SMEs through forums and round tables to raise awareness and to assess the effectiveness of existing measures and programmes to help SMEs to access finance.



*Improving knowledge of the situation of SME and entrepreneurs' financing*

- There is a need for more timely and SME specific data on the supply of and demand for financing so that the real situation of SMEs is known and so that policy makers can determine if their measures are working. Several OECD countries are improving transparency in bank lending by encouraging the timely public disclosure by banks of the composition of their loan portfolios by size of firm.

# IV. PREPARING SMEs AND ENTREPRENEURS FOR RECOVERY AND INNOVATION-LED GROWTH

As many have said the crisis brings certain opportunities. Crises are always moments when change accelerates and new possibilities arise. The crisis could accelerate the redeployment of resources to new activities so that growth is greener and knowledge-based. The current stimulus packages and the normal public procurement programmes could be further tailored to promote innovation and a restructuring of the economy toward the provision of more energy-efficient and greener goods and services. Governments should ensure they are utilising their SMEs as suppliers and could consider procurement targets ensuring SMEs receive purchase orders from government. SMEs should be put in the position to offer these goods and services.

Both the Istanbul Ministerial Declaration and the OECD Brasilia Action Statement acknowledged that SMEs' financing requirements differ at each stage of their development. In particular innovative SMEs have to have access to appropriately structured risk capital at all stages of their development. As discussed earlier, venture capital and private equity have been in short supply since 2001 and with the current crisis are on the verge of collapse. If SMEs are to be the drivers of innovation-led growth, then governments must redouble their efforts to promote private sector risk capital. The European Business Angel Network (EBAN) reported that there is "an unexpected flow of capital demands to business angel networks across Europe which clearly demonstrates the current lack of access to bank credit. This is creating some important challenges for early stage investors but also opportunities which policy makers should help to tackle and leverage."



The OECD Brasilia Action Statement dealt extensively with this issue. It highlighted the fact the access to appropriate types of financing structures and facilities are especially required to allow SMEs and entrepreneurs to take advantage of the opportunities provided by innovation, notably through the diffusion of information and communications technologies (ICTs). They are also needed for SMEs with new business models and high-growth prospects. The OECD Brasilia Action Statement contained a number of proposed actions which could prepare SMEs and entrepreneurs for recovery and innovation-led growth:

- *"A lack of appropriate financing notably represents a hindrance to the creation and expansion of innovative SMEs (...). Comprehensive efforts are needed to bolster the early stages (i.e. pre-seed, seed and start-up) of SMEs, which are marked by negative cash flows and untried business models. This can be done by entrepreneurs themselves leveraging the capital lying dormant in their personal assets, or by "business angel networks" or venture capital markets (...). Successful approaches to developing early stage venture capital markets* *include both tax-based programmes and programmes that use government's ability to leverage private risk capital such as co-investment.*

- *Business incubators, clusters of innovative SMEs, science and technology parks, and development agencies play an important role in facilitating appropriate access to financing for SMEs at local and regional levels. Cities and regions can underpin and strengthen this function through partnerships with private financial institutions and universities. Appropriate financial incentives can correct market failures and stimulate equity investment in local enterprises.*

- *There is a need to promote enhanced awareness, educate and communicate more broadly the value of equity financing, including raising the recognition among entrepreneurs of fair value (this is being rolled back) and transparency in valuing investments.*

- *The combined legal, tax and regulatory framework should ensure that risk capital is not discriminated against, including by safeguarding orderly, equitable and transparent exit routes. Taxes should not put SMEs, entrepreneurs or their financial backers at a disadvantage. There should be neutrality between alternative sources of risk capital, such as domestic versus foreign venture capital funds. Maintaining neutrality between debt and equity should also be an aim for tax policies.*

- *There is no venture capital without venture capitalists and business angels greatly enhance the effectiveness of informal finance. Representing an evolving entrepreneurial breed, these actors thrive on their ability and courage to assume risk. Obstacles should be identified and eliminated. Effective role models can also be promoted to spur the dynamism of these actors. Ways should be explored to facilitate the establishment of "business angel networks", which may greatly enhance information and capital flows."*



The review of measures recently implemented by governments reveals the paucity of measures directed to venture capital. As such, there is some scope to provide additional incentives to encourage investors to participate in venture capital funds or to act as business angel, if venture capital is to play a role in the road to recovery and to stimulate innovation-led growths. EBAN reported that "…there are great opportunities at attractive values on the market… but angel funding for newly formed early stage businesses will not come easy in the next 12 to 24 months…". Government actions could include guarantees for risk capital and/or more co-investment and fiscal incentives such as tax credits for venture capital investments, or tax reductions on capital gains from venture capital investments—whatever is appropriate and for however long it is necessary to re-start venture capital. Incentives must be given to the SMEs as well to encourage them to invest both in upgrading technology as well as shifting toward greener goods and services. These incentives have already been discussed such as accelerated depreciation and tax credits for investments.

# V. PROPOSED ROLE FOR THE OECD

One of the principal recommendations in the *Brasilia Action Statement* was that the OECD considered the development of definitions, indicators, and methodologies for gathering data on the supply of financing available to SMEs and the demand for financing by SMEs. In response to this recommendation, the OECD has undertaken in particular:

- *A review of terminology on business financing* used by national and international organisations. This work has resulted in a proposed common set of definitions for all relevant terms. These definitions and other relevant material on measuring access to finance for SMEs and Entrepreneurship will form a section on "Measuring Access to Finance" in the OECD Entrepreneurship Measurement Manual to be published in 2009.
- An overview and assessment of some of the main sources of data on both the supply of and demand for financing for SMEs. This work highlighted that:
  - Few truly comparable datasets exist across countries. This applies generally to information both on the demand side and the supply side. In one area, i.e. the supply of equity financing, internationally comparable information can be compiled, although many differences exist in the data published by the venture capital and private equity organisations. A temporary database, the Entrepreneurship Financing Database (EFD), has been developed by gathering the available data on the supply of equity financing with a view of enhancing comparability.
  - Available information on the supply of debt financing does not allow one to separate amounts for firms of different sizes and it is therefore impossible to identify the supply of debt financing for SMEs. Proxies are used for firm sizes, e.g. borrowing limits size of loans. In the case of the supply of equity financing, data are classified by stage of firm development and by industry sector.
- *A collection of policies and programmes related to SME and entrepreneurship financing* in particular financing innovative and high growth SMEs. A systematic database of these programmes will be established in the framework of the 2009-2010 programme of work of the OECD Working Party on SMEs and Entrepreneurship (WPSMEE).

In light of the extreme importance of data availability for effective policy responses, as revealed by the current global crisis, the OECD should continue efforts to improve the availability and international comparability of data sets on SME and Entrepreneurship Financing. The WPSMEE, in close cooperation with its parent Committee, the Committee on Industry, Innovation and Entrepreneurship (CIIE):

- Could *promote* a *Scoreboard on SME and entrepreneurship financing data and policies* (a pilot project will be carried out in the framework of the 2009-2010 programme of work in view of the "Bologna +10" High level Meeting) ; *and*
- *Should monitor, report on, and discuss SME and entrepreneurship financing trends on a regular basis.*

As a follow-up, the WPSMEE should also carry out, in the framework of its programme of work 2009-2010, an *assessment of the effectiveness of measures* taken to assist SMEs and entrepreneurs in weathering the financial and economic crisis, as reported in the present report.

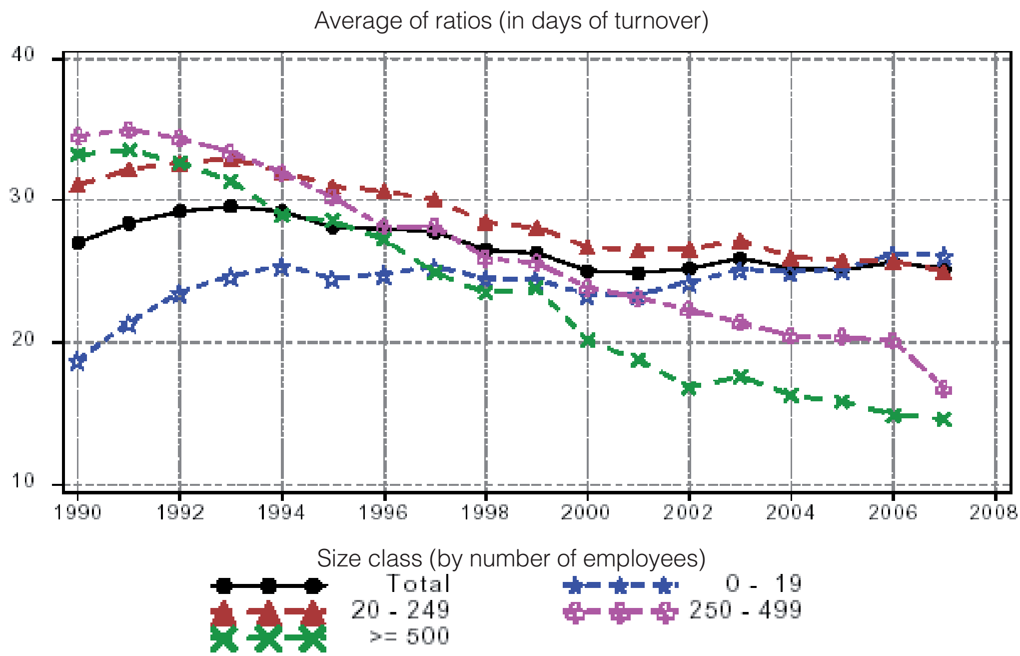
Finally, the OECD should also continue facilitating the *tripartite dialogue between governments, SMEs and the financial institutions,* to periodically review progress in strengthening SME and entrepreneurship financing.

# ANNEXES

## *Annex 1.* *"Short term financial balance" – the French example*

The notion of "short term financial balance" is defined as a difference between a firm's receivables and its own trade debts. The Observatory of Payment delays (set up in 2006) expresses the outstanding balance in terms of an average daily turnover. The graph below represents the evolution of this "balance" for different size classes of enterprises in French industry. Expressed in days of turnover, the SME situation is most problematic relative (25 working days) to large enterprises.

**Figure 6: Net balance (receivables – commercial debt) expressed in average days of turnover in France, by enterprise size**




Source: Bank of France – Fiben, Economic sectors: Food industry (EB); consumer goods (EC); automobile (ED); capital goods (EE); intermediate goods (EF).

# Annex 2.
# Evidence on credit demand

| Based on Bank Lending Surveys methodology | |
|---|---|
| **OECD** | |
| France | In Q4-2008 the overall enterprise demand for credit dramatically decreased, according to 78% of respondents, while for the Q1-2009 a further decrease is expected by 73%; as far as SMEs are concerned, in Q4-2008, 90% of respondents reported a fall in demand (66% for large enterprises) while 73% expect a further fall in Q1-2009 (as opposed to 34% for large enterprises). |
| Germany | In Q4-2008 the overall enterprise demand for credit decreased, according to 7% of the respondents, while for the Q1-2009 a slight overall increase is expected by 4%; as far as SMEs are concerned, for Q4-2008, 19% of respondents reported a fall (8% for large enterprises) while for Q1-2009 the situation is expected to remain stable for SME while large enterprise demand is expected to raise by 4%. The overall demand behaviour is explained by a drastic fall in fixed investment financing demand (-4 4% in Q1-2009 and -12% in Q4-2008) and M&A financing demand (-14% in Q1-2009 and -10% in Q4-2008). |
| Italy | The overall enterprise demand for credit was stable in Q4-2008, while for Q1-2009 an increase is expected by 12% of respondents; the same figure applies for SMEs, while demand by large enterprises is expected to drop by 25% of bank officials. While demand for short term credit is expected to rise by 12% of respondents, the demand for investment credits is expected to fall also by a net 12.5%. |
| Switzerland | Since the beginning of 2008, the Swiss National Bank has been conducting a qualitative survey with twenty banks which make up the bulk of the domestic loan market. The survey carried out in January 2009 shows that some banks have tightened their lending conditions slightly. Moreover, a growing number of banks are expecting to do the same in the near future. While statistics confirm lower growth in overall lending, they do not show an actual decline. |
| United Kingdom | Demand for new credit facilities by medium-sized and large non-financial enterprises is reported to have experienced a fall superior to that anticipated in Q4-2008, while drawdowns on existing committed credit lines are reported to have increased. For Q1-2009, lenders expected further declines in demand for new credit. Drawdowns on committed credit lines were expected to rise. When small enterprises are concerned, in Q4-2008, 53% of lenders report a fall in demand for unsecured credits, and 34% for secured ones. The situation is rather similar for medium and large enterprises when Q4-2008 is concerned (35% reported a fall), while prospects for Q1-2009 differ as 37% of respondents expect a further fall in demand from medium sized enterprises, and only 17% from the larger ones. Sharp fall in capital investment, real estate and M&A activity in medium and large enterprises are the main explanations of the stalled demand in the two quarters under review (-37% to – 66%). Inventory financing and balance sheet restructuring are the two reasons that have contributed to maintain demand (11% to 36% of respondents). |

| Based on Bank Lending Surveys methodology | |
|---|---|
| United States | In the US about 60% of respondents expect for Q1-2009 a very strong fall in credit demand, with a slightly higher value for large enterprises (above 50 million USD turnover) than for small enterprises; in Q4-2008 only 7% of respondents report a fall in demand for small enterprises and 17% for larger ones. While enterprises falling credit demand is explained mainly by reduction in investment and M&A projects, the only reasons mentioned that motivate an increase in demand is growth in enterprises' inventories and receivables. No alternative source of funding is mentioned as a possible explanation of the fall. |
| **Other** | |
| Euro Zone | "Net demand for loans by enterprises declined considerably and remained negative in the Q4-2008, standing at -40%, after -26% in the Q3-2008. The negative net demand was driven by a decline in the financing needs for fixed investment (to -60%, from -36% in Q3-2008) and by a further drop in the demand stemming from M&A activity and corporate restructuring (-44%). In terms of borrower size, while net loan demand, in contrast to preceding quarters, was negative for both large firms and SMEs, the decline was somewhat more pronounced for SMEs in the fourth quarter of 2008. Regarding the maturity spectrum, net demand decreased particularly markedly in the case of long-term loans." |
| **Derived from other methodologies** | |
| **OECD** | |
| Australia | Almost 50% of small businesses feel it is harder to borrow funds now, in comparison to 12 months ago. A forthcoming report by MYOB also shows that 31% of small businesses are currently funded by loans or borrowings, compared to 45% in September 2006. |
| Belgium | The demand for loans is expected to decline together with the investments put on hold by many SMEs. |
| Hungary | In order to measure banks' expectations related to SMEs' demand for credit and its' changes, the Ministry for National Development and Economy, the Bank Association and the National Federation of Savings Co-operatives make a monthly survey among Hungarian financial institutions in 2009. According to it, the financial resources that can be provided to SMEs by financial institutions will decrease in the near future. Financial institutions expect that SMEs' credit risk will grow in the following three months especially related to micro and small enterprises. Although there was a smaller increase in the credit stock of SMEs in Q4-2008 financial institutions expect that the demand for credit will decrease, especially among small enterprises. For the question that according to their opinion how the demand for investment credit and short term loans will change in the future the financial institutions answered that the demand for investment credit will decrease and for short term loans will increase.<br><br>In Hungary 2/3 of SME credit was short term loan in 2008. In the new financial situation caused by the crisis the biggest risk of the banks is to renew short term loans of SMEs that they need for their continuing operation.<br><br>The investment credits of SMEs have always been very low (5% of the total SME credit in 2008). The business expectation of SMEs is very pessimistic which makes them to postpone their investment. |
| Netherlands | Approximately one out of five SMEs was in 2008 looking for additional funding. This is particularly strong among small businesses with 10-49 employees. |

| Derived from other methodologies | |
|---|---|
| New Zealand | In 2007 the Business Operations Survey shows that 29% of firms with more than 6 employees sought debt financing, with 93% of them being able to access finance on acceptable terms. In the same year, 11% of firms sought equity finance and 81% of those firms received financing on acceptable terms. In a survey conducted in mid-February 2009, 62% of firms applying for finance in the previous three months had it granted as requested and 24% with amended terms. In the same survey, of predominantly small firms, 48.5% of respondents answered that their business had not been affected at all by the availability of finance. Of those that had been affected the most common effect was to have put expansion plans on hold (22.6%). The next most cited effect was to put reinvestment/refurbishment plans on hold (17.6%). In relation to employment 15.2% said they are laying off staff, 15% have implemented a hiring freeze and 11.8% have put staff on reduced hours. |
| Switzerland | Since the beginning of 2008, the Swiss National Bank has been conducting a qualitative survey with twenty banks which make up the bulk of the domestic loan market. The survey carried out in January 2009 shows that some banks have tightened their lending conditions slightly. Moreover, a growing number of banks are expecting to do the same in the near future. While the statistics confirm lower growth in overall lending, they do not show an actual decline. |
| **Non-OECD** | |
| Thailand | SMEs face severe credit constraints, finding it very difficult to obtain loans from commercial banks or to raise funds from capital markets. |

# Annex 3.
# Evidence on credit conditions

| Based on Bank Lending Surveys methodology | |
|---|---|
| **OECD** | |
| Canada | The Senior Loan Officer Survey focused on changes to business-lending practices in the Q4-2008. Survey respondents reported a further widespread tightening in lending conditions attributed mainly to concerns about the general and industry economic outlook. For the second consecutive quarter, the balance of opinion on tightening was the highest recorded since the survey began in 1999. While tightening applied to both pricing and non-pricing aspects of lending. Credit conditions for businesses in general have deteriorated considerably since the summer of 2007. From an average 0.12 % points between January 2000 and July 2007, the spread has increased to an average 0.86 % points between August 2007 and December 2008. In September 2008, it reached 1.55, its highest level since late 1974.<br><br>The Bank of Canada's Business Outlook Survey (Dec 2008) indicates that credit has been getting tighter since the third quarter of 2007 and that the net proportion of businesses reporting tighter credit conditions has reached, in the fourth quarter of 2008, its highest point since this survey exists, at 58%.<br><br>Traditional lenders such as banks have increased lending by 13.2% in December 2008 compared to a year earlier. This increase in lending does not, however, appears to fully meet the increased demand. |
| France | The credit standards are reported to be tighter in Q4-2008 by 37% of respondents and are expected to tighten further by 21% in Q1-2009, while SMEs credits are expected to have stricter conditions by 17% of respondents. Lending banks have significantly increased their margins on risky loans (smaller increases for average risk levels); somehow reduced the loan amounts but not their maturity while not increasing the level of required security. |
| Germany | The tightening in credits conditions for large enterprises is, and is expected to be, stronger than for the SMEs: 52% in Q4-2008 and expected 44% for Q1-2009 as opposed to "only" 19% for Q4-2008 and expected 37%, for SMEs. The main factors explaining this situation are above all related to the economic perspectives (macro, sector and borrower specific) and to the banks' balance sheet constraints, i.e. cost of capital and access to debt financing. While lending to enterprises banks have and will continue to increase their margins. However, in Germany the situation of SMEs is slightly better than of large corporations: for Q1-2009, 48% of respondents expect a margin increase on average SME loans (50% do so on the riskier SME loan) while 65% expect that the margin on average large enterprise loan will rise (59% on riskier ones). |

| Based on Bank Lending Surveys methodology | |
|---|---|
| Italy | During Q4-2008 the change in credit standards was dramatic: 100% of the respondents report tightening (87% in case of SMEs). In Q1-2009 loans to large companies are expected to fall by 25%. The tightening concerned the totality of long-term credits and only a proportion of short-term ones. The stress on long term financing is expected to continue. The main factors justifying – in the eyes of responding banks – this evolution are related to the expectations concerning the level of general, and industry specific, activity. Considerations related to banks' cost of capital or balance sheet constraints play clearly a secondary role as compared with France and Germany. In Italy, tightening of credit conditions meant above all higher margins (according to 100% of respondents on riskier loans and 62% on average ones) and reduced size of loan (88%).<br><br>According to the report of the Bank of Italy (Economic Bulletin n.55, January 2009) borrowing by enterprises and households, especially by SMEs, slowed down in the last quarter of 2008.Moreover, borrowing costs rose significantly, especially for riskier loans. A moderate tightening of credit conditions occurred since October 2008, as seen from lending fees, size, contractual clauses and maturity. The percentage of firms that did not receive a favourable answer to their loan request also rose significantly. |
| United Kingdom | A net balance of lenders reported that they had reduced overall corporate credit availability in Q4-2008. As in Q3, lenders reported a larger than anticipated reduction in credit availability to the commercial real estate sector. A further reduction in overall credit availability is expected for Q1-2009. The reduction in the availability of credit is associated with a reduction in maximum credit lines, increasing collateral requirements, and declining loan approval rates. During Q1-2009, UK lenders expected further tightening in these factors. The changing cost and availability of funds to banks is reported to have been a key factor contributing to the decline in credit available to enterprises (-55% expected at –21% in Q1-2009). In addition, concerns about the economic outlook, changing sector-specific risks (expected at – 40% and –33% in Q1-2009) and a reduction in lenders' appetite for risk had also contributed to the tightening of standards. |
| United States | Respondents expect for Q1-2009 an increase in spreads between the loan rates and banks' cost of capital to continue, as during Q4-2008 (almost 90%) and affect to a similar extent both small and large borrowers. When it comes to the broader notion of "standards" the surge initiated in Q2-2008 is supposed to continue but at a slightly lower pace than in Q4-2008. Small enterprises will be more affected than large and medium ones (69% v. 64%). Among factors explaining the changing attitude of banks, the uncertain economic outlook comes first (100%) closely followed by a reduced tolerance for risk (85%); factors related to banks' financial structure or environment do not belong to the most important factors.. |

| Based on Bank Lending Surveys methodology | |
|---|---|
| **Other** | |
| Euro Zone | "In contrast to the previous survey rounds, the net tightening of credit standards reported for large enterprises (63%, after 68% Q3-2008) was equal to that given for SMEs (63%, after 56% in Q3-2008. While there was a certain degree of stabilisation in the case of large enterprises, net tightening for SMEs increased further in Q4-2008. With regard to the factors underlying the changes in credit standards, for both large enterprises and SMEs, expectations regarding general economic activity and the industry or firm specific outlook continued to be the most important contributors. At the same time, banks' cost of funds and balance sheet constraints played a somewhat more important role in the net tightening for large firms than for SMEs, and they seem even to have gained in importance, especially for lending to SMEs. Moreover, competition from other banks contributed for the first time, albeit to a limited extent (8%), to the net tightening of credit standards for both SMEs and large firms. With respect to the terms and conditions for credit, net tightening of credit standards continued to be reflected most in net increases in banks' margins on both average and riskier loans to both large firms and SMEs. Regarding non-price terms and conditions, the net tightening for both large firms and SMEs remained broadly at the same high levels as in the previous quarter". |
| **OECD** | |
| Czech Republic | According to a recent survey taking into account 833 enterprises: more than 2/3 feels a more difficult access to financing. Besides the tightening of credit conditions, credit also has become more expensive according to 22 % of respondents. Loans for M&A are being discontinued by banks almost completely, investment loans being largely reduced and access to short-term financing having become to some extent more difficult. |
| Finland | SMEs surveyed reported that access to financing is worrying compared to the normal situation. About 25% of responding SMEs considered that access to financing had become more difficult, at least to some extent, during the last months. Access to investment funding, for instance, had become significantly more difficult for 14 per cent of industrial enterprises. |
| Korea | Most of the loans were provided to blue-chip SMEs, and financial status of SMEs with low credit rating has deteriorated, which means polarisation of SME financing. |
| New Zealand | In a survey of 659 firms (two-thirds of which had fewer than 20 employees) conducted in mid-February 71.7% of respondents answered that their overdraft/ credit facilities had stayed the same and four times as many (21.5%) reported that theirs has been increased compared to those who reported a decrease |
| Spain | In Q4-2008, 80% of SMEs seeking a bank credit have had problems in obtaining one. The amounts offered by banks in 59% of the cases were lower than requested by their clients, and in 26% credit horizon has been reduced by the bank. In more than 70% of cases, credit conditions have been tightened. |
| Sweden | In Q-1 2009, credit standards are reported to be much tighter by 50 % of respondents, tighter by 38%, unchanged by 15% and eased by 2 % of respondents. |
| **Non-OECD** | |
| Slovenia and Romania | SMEs have difficulties in accessing credit from commercial banks because of restrictive guarantee requirements and increased commissions charges. In Slovenia banks have increased their interest charges and are also more careful when approving new credits (especially long-term credits),as they demand further guarantee even for short-term loans. |

# *Annex 4. Alternative financing sources for SMEs*

| | |
|---|---|
| Canada | In 2006 and 2007 SMEs started to tap the leasing market with a 9.3% increase in the value of outstanding leases. Lease financing also appears to be gathering an increasing share in SME financing, representing 15.0% of the outstanding amount of SME credit (debt and leasing) in 2007 compared to 9.2% in 2000. The leasing market has been significantly impacted during the credit crisis and this source of financing has been more difficult to obtain, which had led to a greater demand for traditional debt financing. This increased demand does not appear to be fully met |
| New Zealand and Switzerland | In New Zealand as in Switzerland, private equity and alternative sources such as mezzanine capital have only played a negligible role in providing SMEs with funds. A survey of New Zealand firms in mid-February 2009 showed 73.7% of respondents have made no changes to their pre-crisis sources of finance and 23% had looked into alternative methods of raising finance. |
| Euro Zone | Bank Lending Surveys reports a more important use of self-financing possibilities by SMEs as a substitute to more difficult access to bank financing. |
| **Non-OECD** | |
| Slovenia | Banks are reported to start proposing new products such as leasing and factoring. |
| Thailand | In 2008, SMEs used more extensively their own savings to run their businesses and were more likely to turn to alternative financial sources such as factoring credit to address the working capital shortage and enhance the business liquidity. Government also turned to joint venture to support SME projects at an initial stage. |
| **International Financial Institutions** | |
| EIB/EIF | The European Investment Bank will put an additional €1 billion at the disposal of the European Investment Fund for a mezzanine finance facility. |

# Annex 5.
# Policy measures supporting sales and preventing depletion of SMEs' working capital

| Export financing and guarantees | |
|---|---|
| **OECD** | |
| Austria | A program to promote export competitiveness has been extended until the end of 2010 and endowed with a yearly budget of €25 million. |
| Canada | In order to address emerging stresses and financial gaps in Canada's export sector, most notably in auto-related and other manufacturing enterprises, the government is injecting $350 million (€218.7 million) for Export Development Canada supporting up to about $1.5 billion (€937.3 million) in increased credit capacity for the exporters most affected by the financial crisis. |
| Czech Republic | The government will increase the availability of state advantageous loans to exporting SMEs. In consequence, the basic capital of the Czech Export Bank will be increased by an additional CZK 1 billion (€37.2 million), which should provide for state assistance to exports in the amount of CZK 20-25 billion (€744-€930 million). |
| Denmark | An export lending scheme will be set up under the auspices of Eksport Kredit Fonden to secure funding for the export activities of Danish businesses. The lending scheme will run for a period of three years and will have a limit of DKK 20 billion (€2.7 billion).<br><br>In addition to loans to fund export activities involving long-term credits, the Eksport Kredit Fonden will also support export activities involving short-term credits, including components, semi-manufactures, comsumer non-durables and food. This will take place by the Eksport Kredit Fonden reinsuring the private credit insurers (debtor insurance). Such reinsurance will contribute to alleviating the problems businesses may be experiencing in terms of obtaining bank loans to fund their export activities. The reinsurance scheme will have a limit of DKK 10 billion (€1.3 billion). |
| Germany | Various products of the Federal Government's "Hermes" export credit guarantees have been improved and extended until the end of 2010. Thus, supplementary flexibility in export financing has been created. |
| Italy | An anti-crisis export promotion plan has been introduced, with an overall allocation of €185 million in 2009, managed by the Institute for Foreign Trade (ICE). Internationalisation support services provided by ICE to Italian companies will benefit from up to a 50% discount on fees, and special payment conditions aimed at small companies will be made available. |
| Luxembourg | To facilitate export activities the funds available for credit insurance on export are raised from €20 million to €35 million. The "Office du Ducroire" handles this mission for the Luxembourg State. |
| Mexico | The financing of exports will be expanded, through BANCOMEXT, to provide credit for working capital to the exporting enterprises, as well as to provide them with the necessary equipment. Also, a Productive Chains Program is put in place to prevent Mexican enterprises from being dropped because of financial weakness from Global Value Chains. In this way the flow of Mexican exports is being protected. |

| Export financing and guarantees | |
|---|---|
| Netherlands | The Dutch credit insurance facility is expanded so as to cover through public funds risks for markets where commercial insurances are not possible any more (especially in Eastern Europe) and by doing so enable trade. In order to provide support for large transactions the government will guarantee their payment. |
| New Zealand | The Export Credit Scheme has been expanded so as to provide short-term trade credit insurance on export contracts with payment terms of less than 360 days. |
| Spain | Two new programs: "Internacionalización" and "Proinmed" run by the Instituto de Credito Oficial are aimed at helping SMEs in their internationalisation projects and programs. |
| Switzerland | Increase available funding (+ CHF 10 million -€6.6 million) allocated to the agency responsible for promoting export activities and broaden the scope of export insurance to include products that private insurance companies do not offer. |
| **Non-OECD** | |
| Chile | Extension of COFORO is aimed at reducing further liquidity problems that exporters are facing. In consequence, the turnover limit of eligibility has been increased from US$ 20 to US$ 30 million. |
| Slovenia | The government is endowing the Slovene Export and Development Bank with additional resources to enhance export financing, credit and insurance. In 2009 the bank will receive additional funds specifically aimed for exporting SMEs. |
| **Alleviating working capital shortage in the economy** | |
| **OECD** | |
| Canada | A $100 million (€62.4 million) capital injection to the Business Development Bank of Canada will support the implementation of a new program for working capital guarantee. |
| France | Starting from January 2009, payment delays are capped to 45 days, moratory interests are doubled and other legal deterrents are put in place. These measures are supposed to provide SMEs with an extra €4 billon of working capital. |
| Netherlands | The government intends to shorten terms for payments from 45 to 30 days |
| United Kingdom | A Prompt Payment program is put in place reducing official institutions' payment delays to 10 days. |
| **Easing of tax and procurement payment procedures** | |
| **OECD** | |
| Belgium | The government has made possible for firms facing financial difficulties to postpone payments of VAT and tax advances and has granted payment facilities in terms of social security contributions.<br><br>The Federal Government has also committed to accelerate payments on public procurements and has created a new product aimed at transferring unpaid debts hold by SMEs on public authorities to the Participation Fund, which will execute the payments more rapidly. |

| Easing of tax and procurement payment procedures | |
|---|---|
| Canada | The Government increased the amount of small business income eligible for the reduced federal tax rate. |
| Denmark | To ease liquidity in companies, the Danish government has temporarily prolonged the payment of tax and value added tax. |
| France | The Ministry of Defence will immediately balance its arrears towards its suppliers, and many tax credits will be reimbursed in cash; VAT payments and refunds will be made on a monthly basis, and advance payments on public procurements will be increased. |
| Italy | New tax benefits were granted to enterprises, with an allocation amounting to ca. €2,900 million for the 2009-2011 period. The benefits include:<br>• Tax exemption for productivity contracts aimed at boosting labour productivity ;<br>• Deduction of 10% of the regional tax from company income tax and personal income tax<br>• Payment of VAT at the time of actual receipt of sale payment. |
| Japan | The Government has reduced the corporation tax rate from 22% to 18% for the SMEs with 8 million yen (€61 thousand) or less annual income in coming 2 years. |
| Mexico | A governmental purchases program has been initiated according to which at least 20% of the total of annual purchases of the Federal Government and its dependences will be bought from SMEs. |
| New Zealand | A suite of tax changes that will ease cash-flow for SMEs including lowering of interest rates used in case of unpaid or late business taxes. |

# *Annex 6.*
# *Policy measures enhancing SMEs' access to liquidity, especially to bank lending*

| Creation and extension of loans and guarantee schemes for SMEs | |
|---|---|
| **OECD** | |
| Austria | Available total public guarantee have been increased from €3 to €5.3 billion and a further increase of about €400 million guarantees per year is expected. Austria has also increased its low interest loans programme (EPR) to €600 million for 2009 from the present €200 million and put in place a new micro-loan program (up to €30,000) endowed with a total of €50 million. |
| Belgium | The government launched a second "Starters Fund", which is an obligation loan of €300 million providing additional means for the Participation Fund to finance starters.<br><br>A product ("Initio") is a subordinated loan that can be requested immediately at the Participation Fund by SMEs to finance any kind of investment (also working capital) before they go to the banks. |
| Canada | Made improvements to the Canada Small Business Financing Program (loan guarantee) that will increase the eligible loan amount and increase individual financial institutions' cap on claim reimbursement for losses. These changes should encourage access to credit specifically targeted at SMEs and could increase lending under the program by some $300 million per year (€187.4 million).<br><br>Has established Canadian Lenders Assurance Facility which may indirectly encourage lenders on the wholesale market to lend to federally-regulated deposit-taking institutions that may lend in turn to SMEs. It is a temporary program that will ensure that financial institutions in Canada are not put at a competitive disadvantage when raising funds in wholesale markets given similar actions recently announced by other countries. |
| Czech Republic | At the end of 2008 the Ministry of Industry and Trade transferred CZK 1 billion (€37.2 million) to the turnover fund of the Czech-Moravian Guarantee and Development Bank as guarantee for loans provided by commercial banks. In February the Ministry of Industry and Trade will announce another section in the program Guarantee, which will allow entrepreneurs to gain a guarantee for bank loans from commercial banks. In total the Ministry of Industry and Trade is counting with CZK 1.650 billion (€61.4 million) for the programme Guarantee. |
| Finland | The government has increased the ceiling of guarantees and loans for the Government-owned SME-bank between November 2008 and January 2009 by €1.6 billion. |
| France | The government has increased the guarantee programmes run by OSEO so as to allow it to cover up to €4 billion of new loans, to large extent targeted to SMEs, including an important portion linked to short-term credits; |
| Germany | The Kreditanstalt für Wiederaufbau (KfW) (public bank) has created an additional financing instrument with a volume of up to €15 billion, temporarily in place until the end of 2010, through which the supply of credit from the private banks to SMEs will be enhanced. This measure is part of a general effort to implement a €115 billion programme of loans and credit guarantees by expanding existing measures and creating new instruments. |

| Creation and extension of loans and guarantee schemes for SMEs | |
|---|---|
| Greece | A new programme for the enhancement of liquidity of Small and Micro enterprises has been launched by the Credit Guarantee Fund of Small and Very Small Enterprises (TEMPME S.A.). Since December 2008, TEMPME S.A has launched, the programme "Loan Guarantee and Interest Rate Subsidy for the working capital of small and micro enterprises" (Endowed with €100 million for interest subsidies, and €2.5 billion of guarantees). |
| Hungary | In Hungary, the New Hungary Portfolio Guarantee Programme has been put place further to the financial crisis. Within the portfolio guarantee program, Venture Finance Hungary Plc. provides direct guarantee for the financial claims (backing SME credits) of the financial intermediaries (mostly commercial banks) based on pre-determined risk sharing, thus improving the SMEs' bank finance options. For a given credit, the amount of collateral to be secured by Venture Finance Hungary Plc is a maximum of 80% of the bank claim – the rest constitutes the bank's own risk. The guarantee programme offers credits amounting to a maximum of HUF 100 million (€ 344 thousand). The resources to be invested for this purpose total to HUF 28.2 billion (€97 million).<br><br>In Hungary the total public guarantee that is provided by Garantiqa Credit guarantee Co. Ltd. to banks against loans to SMEs have been increased from HUF 450 million (€1.5 million) to HUF 900 million (€3 million euro). |
| Italy | In January 2009 a re-financing of the Central Guarantee Fund for SMEs has been put in place, and a State guarantee as a last-resort guarantee has been provided to this Fund. A total of 70% of the resources will be allocated directly to guarantees to banks against bank loans to SMEs, while 30% will be devoted to back guarantee to the Loan Guarantee Consortiums (Confidi –Allocations for the 2009-2011 3-year period total €450 million). The resources for the Central Guarantee Fund may be further increased. |
| Japan | Additional 21 trillion yen (€160.6 billion) have been targeted for emergency guarantee schemes and loans provided by government-affiliated financial institutions. An Emergency Guarantee System has been set up and between October 31, 2008-December 31, 2008 it has approved 0.17 million loans for a total amount of 3.9 trillion (€9.8 billion) yen; in addition a Safety Net Loan was in operation and in Q4-2008 between the approved number of 49.5 thousand loans for a total amount of 564.8 billion yen (€4.3 billion). |
| Korea | The government will increase SME lending by $35.7 billion in 2009 by expanding guarantees for guarantee organisations as well as bank capitalisation and increasing SME lending by state-run banks. New guarantees volume increased from $9.6 billion in 2008 to $18 billion in 2009. Collateralised Bond Obligation worth $1.4 billion will be issued in early 2009. State banks including Korea Development Bank and Industrial Bank of Korea increased their SME loans from $21.4 billion in 2008 to $31.4 billion in 2009. In order to have access to these funds SMEs with liquidity shortages will be classified into A, B, C, and D categories. |
| Luxembourg | A guarantee scheme was put into place in compliance to the Communication 2009/C16/01 of the European Commission. The total volume of credit the Luxembourg State will cover by its guarantee is limited to €500 million |

| Creation and extension of loans and guarantee schemes for SMEs | |
|---|---|
| Mexico | The National Guarantee System strategy aims at enlarging the supply of affordable financial resources for all categories of SMEs; the National Financial Extension Program aimed at increasing SME access to finance and helping SMEs enter into credit relationship through the upgrading of their organisational and managerial faculties. The Development Bank of Mexico has increased significantly its lending to SMEs, to the rural sector and to infrastructure and housing projects. The bank is also offering guarantees to financial intermediaries and solvent businesses hit by the lack of international liquidity. |
| Netherlands | Amounts eligible for guarantees has been increased from €1 million to 1.5 million per company. The guarantee of start-ups has been expanded from €100 to €200 thousand euro. About €80 million have been put aside for financing the extended guarantee scheme. |
| Spain | The Instituto de Credito Oficial has put in place a programme for SMEs whereby SMEs are allowed to use up to 40% of the loan to finance working capital under the condition that he remaining 60% are financing investment in productive assets. Also in Spain la Compañía Española de Refinanziamiento (CERSA) provides the second tier of national second level guarantee fund to loans granted by mutual guarantee companies to SMEs that require additional guarantees to get access to finance. Priority goes to innovative investments and projects, as well as to micro enterprises and new or early-stage business ventures. |
| Switzerland | In the event of an intensification of the crisis, the government envisages the possibility of strengthening the loan guarantee scheme for SMEs, particularly by raising the guarantee limit from CHF 500,000 (€330 thousand) to CHF 1 million (€660 thousand) per enterprise. The guarantee scheme was restructured in 2007 but has remained a marginal measure because its funding totals CHF 150 million only (€99.3 million). |
| United Kingdom | Through the Enterprise Finance Guarantee Scheme, the government will guarantee lending by High Street Banks to viable businesses to ensure that they can get the working capital and investment that they need. This £1.3 billion (€1.5 billion) scheme will support bank lending, from 3 months to 10 year maturity, to UK businesses with a turnover of up to £25 million (€28.3 million) which are currently not in a position to easily access the finance they need. It will enable them to secure loans of between £1,000 and £1 million (€1.1 thousand and €1.1 million). The scheme will remain in operations up to 31 March 2010. In addition UK set up a Working Capital Scheme in direct response to the constraint on bank lending to ordinary-risk businesses with a turnover of up to £500 million (€623.5 million) a year. The Government will provide banks with guarantees covering 50 per cent of the risk on existing and new working capital portfolios worth up to £20 billion (€22.7 billion). Finally, a Regional Loan Transition Fund has been set up in England only with £25 million (€28.3 million) to help businesses at a regional level up to the end of June 2009. The loan fund is primarily aimed at supporting small and medium sized businesses which are suffering from short term liquidity problems caused by the current economic climate. The loan fund will operate in conjunction with existing or new founders to assist with immediate liquidity problems. |
| **E.C.** | The European Commission has temporarily made it easier for its Member States to help access to finance for companies through subsidised guarantees and loan subsidies for investments. Member States are also urged to reduce administrative burdens on business, and to promote their cash flow and help more people to become entrepreneurs. For example, in France, the easing of rules makes it possible for the guarantee schemes to cover up to 90% of the risks related to a loan as compared with 50 to 60 % on average before. |

| Creation and extension of loans and guarantee schemes for SMEs | |
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| **Non-OECD** | |
| Chile | The Guarantee Fund for SMEs (FOGAPE) has been endowed with additional US$ 130 million, bringing its present resources to US$ 200 million. These resources allow guaranteeing loans for more than US$ 2 billion. FOGAPE will expand its coverage to include about 20 thousand medium-sized companies in the country, so they can have access to financing for working capital. Said guarantee will account to up to 50% of the loan. The maximum limit for loan coverage will be raised from US$ 104 thousand to US$ 3.5 million per company. |
| Estonia | A newly introduced permanent measure is aimed at providing public mezzanine financing for enterprises, which are not able to achieve self-financing ratio that banks expect before granting credit. |
| Romania | A guarantee fund will be established with the Romanian Savings Bank to ease SMEs access to credit. |
| Russia | A governmental loan scheme is put into place aimed at supporting SME and entrepreneurship financing through the strengthening of the capital base of banks that usually lend to SMEs and entrepreneurs. |
| Slovenia | In 2009 an additional €50.6 million will be made available for the guarantees and subventions of interest rates in order to help SMEs implement the development projects. |

| Creation and extension of loans and guarantee schemes for SMEs | |
|---|---|
| **International Financial Institutions** | |
| EIB/EIF | The European Investment Bank put together a package of €30 billion for loans to SMEs, an increase of €10 billion over its usual lending in this sector; and it will also reinforce by €1 billon a year its lending to mid-sized corporations. This allows some Member countries to use a second level guarantee scheme provided by EIB. This is the case for Belgium both at central and regional government levels; the UK government has facilitated discussion between UK banks and EIB that opened the way to EIB credit lines of more than £1 billion (€1.1 billion) which are coming on-stream now to provide SME lending.<br><br>Jeremie, Joint European Resources for Micro to Medium Enterprises: Jeremie uses European Regional Development Funds for enhancing SME access to finance in New Member States and in Regional Development areas. This instrument was designed before the crisis but main elements are customised and calibrated as reaction to the crisis. Instruments: equity, funded risk sharing, guarantees, quasi equity and tech transfer. EIF has so far signed 7 funding agreements with €613 million).<br><br>CIP, Competitiveness and Innovation Programme by the EC (managed by the EIF) with an envelope for Guarantees of €550m (covering 2007-2013) and of €550 million for VC. The products have been designed before the crisis but the implementation considers necessary reactions to the crisis.<br><br>Micro Finance Facility/pilot project Jasmine – Joint Action to Support Micro-finance Institutions in Europe, a joint initiative between the European Commission, the EIB, the European Parliament, and the EIF as manager. Support and development of microfinance sector in Europe via debt and equity products (initial resources: €30 million). |
| **Mediation and monitoring measures** | |
| **OECD** | |
| Belgium | The credit mediator in Belgium is a contact point for SMEs and entrepreneurs that have problems with their funding at the bank. The motto used: “No entrepreneur should stand alone with his financial problems”. |
| France | The credit mediator can intervene at regional and central levels, to ease difficulties and help solve divergences between enterprises that are seeking bank funding and the banks. 5 331 have used this facility, 892 enterprises in two weeks with an increasing success rate of 66%. |
| USA | The government has chosen to strictly monitor, on a monthly basis, the credit activities of banks that have been rescued by public funding. First, such a report has been released in January 2009 under the title “Treasury Department Monthly Lending and Intermediation Snapshot”. The purpose of the document is “to provide the Treasury Department (Treasury) and the public with regular insight into the lending trends and intermediation activities – including underwriting, buying and selling of securities, and other activities in capital markets -- of the banks that received the most funding via the Capital Purchase Program (CPP). |

| Strengthening SME's cash-flow, capital base and pro-investment measures | |
|---|---|
| **OECD** | |
| Austria | The service agency for enterprises can contact international financing institutions like EIB and KfW for refinancing of SME projects especially related to R&D and the environment (plus €300 million). |
| Belgium | The government is collaborating with the European Investment Bank in order to liberate supplementary means for investment credits. It is also accelerating several public investment programs and stimulation of green investments and has reduced VAT in the construction sector (to 6% from 21%). |
| Canada | Has provided financial assistance for innovative SMEs by allocating $200 million (€125 million) over two years to the Industrial Research Assistance Programme. These non-refundable contributions will act as a source of fund for innovative SMEs to offset difficulty accessing financing to undertake innovative business strategies and technology-related projects. |
| Czech Republic | The Ministry of Industry and Trade will also announce a new call in the programme Progress, from which entrepreneurs can also gain a loan for development projects which are more demanding in terms of investment. In the calls which will be announced the Ministry will release CZK 2.5 billion (€93 million). |
| France, Germany and Italy | Have introduced accelerated depreciation possibilities either on all categories of assets or on specific ones as in Germany where specific depreciation thresholds are targeted to SMEs thereby reducing taxable income. |
| Germany | The funding available to support SMEs' R&D projects will be increased by an additional €450 million per year for 2009 and 2010. |
| Hungary | Commercial banks received new refinancing credit from the Hungarian Development Bank in order to maintain and increase their investment credit offer to SMEs (HUF 50 billion - €172 million) with a capped interest rate. Due to this credit line, SMEs can obtain preferential credits of between HUF 10-100 million (€34 thousand-€340 thousand).<br><br>The New Hungary Enterprise Development Credit Programme (total resources of HUF 160 billion, €550 million) operate through the National Development Bank and its intermediaries and offer SMEs a long term preferential investment credits with interest rates based on 3 monthly EURIBOR rate with a 4-6% spread. The SMEs can obtain credit between HUF 1 million-3 billion (€3.5 thousand - €10.3 million).<br><br>The New Hungary Microcredit Programme started to operate in order to provide credit for micro enterprises. The total resources of the programme are HUF 58.5 billion (€201 million).<br><br>A new Working Capital Credit is put in place through which SMEs can obtain working capital credit with preferential conditions between of HUF 10-200 million (€34 thousand - €688 thousand). 80% of the Working Capital Credit is guaranteed by the Garantia Credit guarantee Co. Ltd |
| Spain | The Instituto de Credito Oficial grants credits on preferential terms to self-employed and entrepreneurs to launch new businesses and may finance up to 90% of investments in new productive assets. The same institution also supports extension projects of SMEs by financing up to 80% of new productive assets - the programme is endowed with €600 million. |

| Strengthening SME's cash-flow, capital base and pro-investment measures | |
|---|---|
| USA | The Stimulus Package enables SMEs to expense up to $250,000 in property purchased in the 2008 tax year, and it grants 50% bonus depreciation allowance for 2008 capital asset purchases acquired in 2008. Other temporary tax incentives are also put into place to encourage investment job creation; |
| **E.C.** | Within the European Union, the Structural Funds of the European cohesion policy give the Member States and their regions considerable margin of manoeuvre to support SMEs, including through investment projects in specific technologies or sectors. Many Member States are using these opportunities, including Romania and the Czech Republic. |
| **International Financial Institutions** | |
| EIB/EIF | The European Investment Bank will put an additional €1 billion at the disposal of the European Investment Fund for a mezzanine finance facility. |

# Annex 7.
# Private equity and venture capital markets

| | |
|---|---|
| **OECD** | |
| Australia | The Australian Government announced on 18 March 2009 that up to AUD83 million (€45.2 million) over a three year period to assist high potential young innovative companies to be sustainable through the financial crisis. |
| Austria | €1 billion to support small and medium sized companies:- Participation-Fund for SMEs: €40 million per annum for 2009 and 2010. |
| Finland | The government will set up a risk capital fund that will act as a minority investor in Venture Capital or MBO –funds or directly in companies on equal terms with private investors. |
| Hungary | A) The New Hungary Venture Capital Programme has been designed to improve the financial status of Hungarian SMEs by providing early-stage equity financing. The Hungarian capital market is relatively underdeveloped in this field; larger transactions are dominant – only a few market players are involved in financing SMEs in their seed and start-up stages. Under the Program, Venture Finance Hungary Plc. – as the fund manager of a Fund of Funds (FoF) – relays resources to venture capital funds. A total of HUF 35 billion (€120.3 million) is being allocated to the Program, 85% of which is going to be financed by the European Union. The partners of Venture Finance Hungary Plc. will be venture capital fund management firms, who are tasked with raising a fixed proportion of additional private funding to the resources committed by Venture Finance Hungary Plc. The abovementioned partners will be selected by open tender. The amount of the investment may have a transaction size of an annual €1.5 million. Potential target enterprises: SMEs in the early (seed or start-up) or growth stage, which were founded no more than five years prior to the investment decision and have a net annual turnover not exceeding HUF 1.5 billion (€5.2 million) in any business year.<br><br>B) A Japanese-Hungarian Venture Capital Fund (SBI Europe Fund) has also been announced in December 2008 with effect from first quarter 2009. This is the first private equity fund established by a public bank and a private investor in the Central and Eastern European region, focusing on the SME sector. The Fund plans investments in the range between €1 million and €20 million, of around €5 to €7 Million on average in exchange for majority if possible, but in exceptional cases, minority equity interest will be considered. ELAN SBI will be the Fund Manager for the SBI Europe Fund and will target investments in promising companies with high growth potential, with no sector preference. Ideal investment targets will be companies with established management teams, existing revenues and fast growing profits. The Fund will seek to realise exits within 3 to 4 years. The committed amount is €100 million (60 % by the SBIH Group and 40% MFB) |
| Mexico | The Capital for Development Schemes seek to increase the supply of venture capital (Seed Capital Program and Fund of Productive and Infrastructural Development Projects FOPRODE). |
| UK | The Capital for Enterprise Fund will provide £75 million (€85 million) of equity, made up of £50 million (€56.7 million) of Government funds and an additional £25 million (€28.4 million) from Barclays, HSBC, Lloyds TSB and RBS to provide equity and quasi equity of between £250,000 to £2 million (€283 thousand and €2.3 million) for companies with a turnover of up to €50 million who have viable business models and growth potential in need of long term capital. |

| Non-OECD | |
|---|---|
| Chile | CORFO Venture Capital for Innovative SMEs will contribute to investment funds that back the creation or expansion of SMEs with innovative projects and high growth potential. |
| Slovenia | The first public venture capital company (PDTK) will start to operate in 2009 with a budget of €35 million. PDTK will complement private investments in “start-up» and innovative companies with the high-growth potential. |

# ANNEX 8.

## OECD WORKING PARTY ON SMEs AND ENTREPRENEURSHIP

## STEERING GROUP ON SME AND ENTREPRENEURSHIP FINANCING

## LIST OF MEMBERS

### *CHAIR*

**Mr. Salvatore Zecchini**, President, Institute for Industrial Promotion (IPI), Italy.

### *PARTICIPATING COUNTRIES and ORGANISATIONS*

#### *Belgium*

- **Mr. Frédéric Lernoux,** Vice president of the scientific steering group of the Belgian Knowledge Centre for SME financing **(**BeCeFi), Representative of the Ministry of SMEs, Freelancers, Agriculture and Scientific Policies.
- **Mr. Pierre-François Michiels**, Attaché, Federal Public Service (FPS) Economy, SME, Middle Classes, Energy.

#### *Brazil*



- **Mr. João Carlos Parkinson de Castro**, Counsellor, Embassy of Brazil in Ireland.

#### *Canada*

- **Mr. Denis Martel**, Director, Research and Analysis Division, Small Business and Tourism Branch, Industry Canada.
- **Ms. Adele Deschamps**, Policy Analyst, Industry Canada.
- **Mr. Jérôme Nycz**, Vice President, Strategy and Planning, Business Development Bank of Canada (BDC).

#### *Finland*

- **Mr. Pertti Valtonen**, Ministry of Employment and the Economy.

#### *France*

- **Mr. Jacques Augustin**, Deputy Director for Tourism, General Directorate for Competitiveness, Industry and Services, Ministry of Economy, Industry and Employment, and Chairman of the OECD Working Party on SMEs and Entrepreneurship (WPSMEE).
- **Mr. Henry Savajol**, Director, SME Observatory (OSEO).
- **Mme Nadine Levratto**, Researcher, Université de Paris Ouest Nanterre, National Council of Scientific Research (CNRS).

## Greece

- **Mr. Nicolas Tritaris**, Managing Director, Credit Guarantee Fund of Small and Very Small Enterprises, and Vice-Chair of the OECD WPSMEE.

## Italy

- **Mr. Massimo Deandreis**, Head of Management Board Chairman Office, Banca Intesa Sanpaolo.
- **Mr. Mario Calderini**, President, Finpiemonte.

## Japan

- **Mr. Hiromichi Moriyama**, First Secretary, Japanese Permanent Delegation to the OECD, Paris, and Vice-Chair of the OECD WPSMEE.

## Luxembourg

- **Mr. Gilles Scholtus**, Government Attaché, Tourism and Housing, Ministry of Middle Classes.

## Netherlands

- **Mr. Dinand Maas**, Senior Policy Advisor, Department for Entrepreneurship and Innovation, Directorate for Entrepreneurship cluster Corporate Finance, Ministry of Economic Affairs.

## New Zealand

- **Mr. Roger Wigglesworth**, Director, SMEs Industry and Regional Development Branch, Ministry of Economic Development.

## Sweden

- **Mr. Mattias Moberg**, Deputy Director, Energy and Communications, Ministry of Enterprise.
- **Ms. Petra Gråberg**, Desk Officer, Energy and Communications, Ministry of Enterprise.

## Switzerland

- **Mr. Philippe Jeanneret**, Head of SME Policy, State Secretariat for Economic Affairs (SECO).
- **Mr. Christian Weber**, Head, State Secretariat for Economic Affairs (SECO), and Vice-Chair of the OECD WPSMEE.

## European Commission

- **Mr. Vesa Vanhanen**, Department of Enterprise and Industry.

## European Investment Fund (EIF)

- **Mr. Helmut Krämer-Eis**, Head of Research and Market Analysis.

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