SURVEY REPORT ON FINTECH FOR MSMEs ACCESS TO FINANCING (V.2)

SURVEY REPORT

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This survey report is a product of the SME Finance Working Group (SMEFWG) and its members. This publication is an update of the Survey Report on FinTech for MSME Access to Financing, originally published in June 2021.

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A young customer smiles after paying for goods and services through mobile money transfer. Kenya. (Photo by Billy Miaron/Shutterstock)

INTRODUCTION

LACK OF ACCESS TO FINANCE IMPEDES MSMEs' GROWTH

Access to finance for MSMEs remains as one of the main hurdles in many developing countries, noting their significant impact on employment creation, GDP contribution and overall economic growth, it is at the top of the policy agenda in most countries. It is estimated the total MSME credit gap of USD5.2 trillion every year from the estimated total demand of USD8.9 trillion.[1]

The relatively low level of external funding indicates that there is a need to strengthen and expand alternative finance mechanisms for MSMEs. Lack of collateral, high cost of borrowing and no track record are the three main challenges in getting funding identified by SMEFWG members in AFI Alternative SME Finance member survey 2019 (figure1).

One of the most important ways to reduce gender disparity is through MSMEs. In the MSME sector, women entrepreneurs play a crucial role in economic growth and employment creation.[2] Among low- and middle-income countries, women-owned MSME finance gaps account for more than half of the entire finance gap on average. More women have access to bank accounts and loans, which means more women-owned enterprises, according to World Bank research.[3] One of AFI knowledge products indicates, the Maya Declaration and the Denarau Action Plan have made significant progress on gender-inclusive finance, yet there is little attention paid to women-led MSMEs' access to financing by policymakers.[4]

It has been almost two years since COVID-19 brought the world under the pandemic. The COVID-19 pandemic has and will continue to have a negative effect on MSMEs in the developing world.

6.7% In 2020, global GDP declined by 6.7 percent because of the coronavirus (COVID-19) pandemic outbreak.[5]

MSMEs, especially those in the informal sector, which includes the majority of women-led MSMEs, are acutely vulnerable to the impact of the crisis.

1 IFC. 2017. MSME Finance Gap. Assessment of the shortfalls and opportunities in financing micro, small and medium enterprises in emerging markets. Available at: https://www.ifc.org/wps/wcm/connect/03522e90-a13d-4a02-87cd-9ee9a297b311/121264-WP PUBLICMSMEReportFINAL. pdf?MOD=AJPERES&CVID=m5SwAQA.

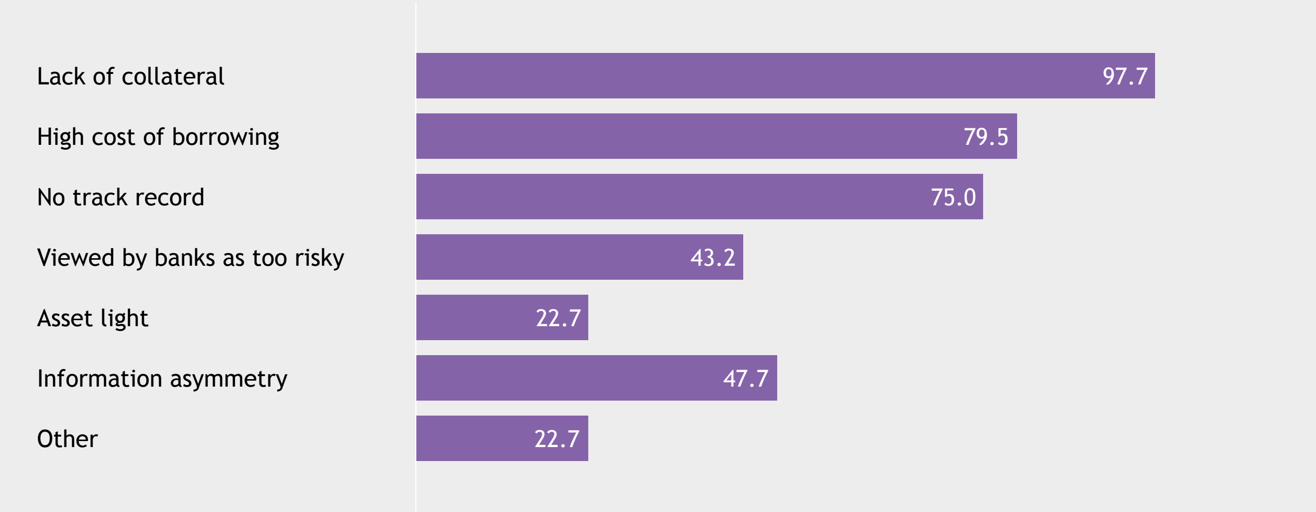
2 WBG (2017), Women's Entrepreneurship Facility

3 GPFI (2020), Promoting Digital And Innovative SME Financing

4 https://www.afi-global.org/wp-content/uploads/2021/01/AFI_SMEFWGBTG_PF_AW2_digital.pdf

5 Published by M. Szmigiera, Jun 1, 2021, https://www.statista.com/statistics/1240594/gdp-loss-covid-19-economy/

FIGURE 1: CHALLENGES FACED BY MSMEs IN GETTING FUNDING, %



Source: AFI Alternative SME Finance member survey 2019. The figures reflect the % of the respondents who identified the challenge as being present in their jurisdiction. Multiple responses were possible

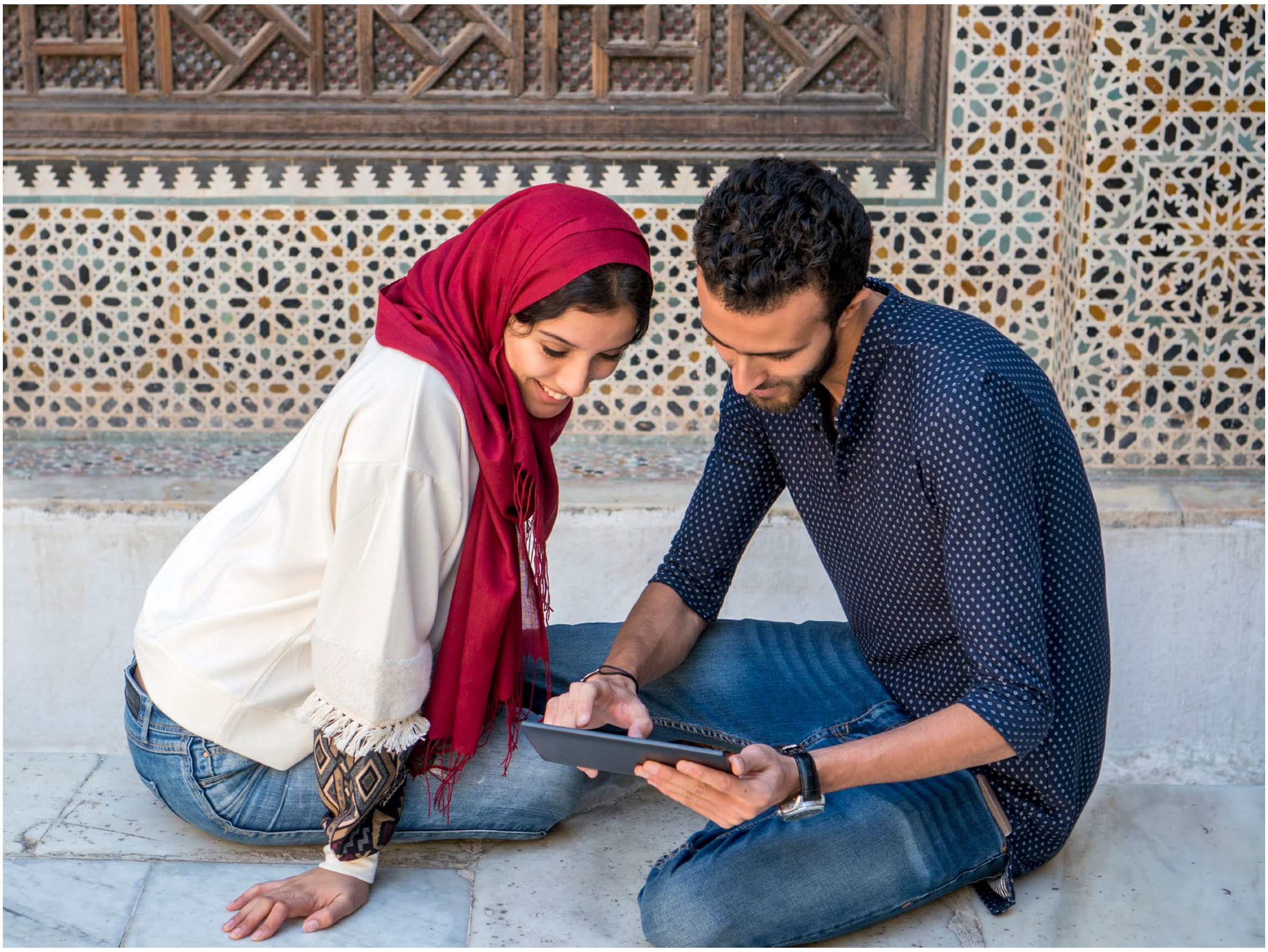
Even in countries where the local impact of the pandemic was less severe, the reduction in international trade is having a disproportionate effect on MSMEs. This reality is highlighted in the findings in the SME Competitiveness Outlook.[6] This places extra stress on already struggling MSMEs, resulting in a worsening of the sector's financial position. In order to fulfil the increased need for MSME financing, new techniques are needed to address the current scenario.

Banks and other financial institutions have grown steadily but have not been able to reduce the MSME finance gap, have not adequately addressed the access to finance problems faced by women and other vulnerable groups, and are unlikely to deal with the anticipated increased demand from MSMEs due to the COVID-19 pandemic.[7] Since the existing traditional financing channels are limited in addressing the credit gap to a significant amount, alterative finance mechanisms are required to complement the MSME finance ecosystem. The types of alternative finance mechanisms considered are digital finance (fintech and digitalized data), the use of the capital market, finance mechanisms from banks and finance houses other than secured loans and grants.[8] From asset-based lending to alternative debt to hybrid instruments and platforms for MSMEs to be publicly listed, the risk associated with each of the approaches varies.

6 International Trade Centre (2020), SME Competitiveness Outlook 2020 – The Great Lockdown And its Impact on Small Business

7 https://www.afi-global.org/wp-content/uploads/2021/01/AFI_MSMEs_survey-report_AW_digital_0.pdf

8 https://www.afi-global.org/wp-content/uploads/2021/01/AFI_MSMEs_survey-report_AW_digital_0.pdf



Young couple using digital technology to make e-payment. Morocco. (Photo by Marko Rupena/iStock)

OBJECTIVE

AFI's SME Finance Working Group conducted a survey in 2020 to establish a baseline of information provided by AFI member institutions in identifying the current financing landscape and how the emergence of FinTech and digitalized data could complement the financing ecosystem, policy implementation and national strategies, particularly from a regulators' perspective and help mitigate the financing gaps.

SME FINANCE WORKING GROUP SURVEY

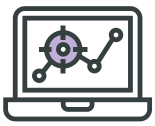
Is it true the emergence of Fintech and bigdata help MSME in gaining more access to finance? Could FinTech address the issue of financing difficulties especially for early stage and smaller MSMEs, as most of them are considered as "thin files", light in assets with limited collateral and not stable. Are they regulatory-based or market-based? Are they local or international players? How would the government support this initiative and most importantly protect the consumers (individual and MSMEs)? These are among the problem questions for the AFI SME Finance Working Group survey to explore on FinTech for MSMEs Financing. This Survey addresses these questions in six different sections highlighted below.

This quantitative single survey was conducted online from 3 to 18 September 2020 via survey monkey. The survey received 22 member responds representing six regions which the highest participation is from the Pacific Islands followed by Sub-Saharan Africa. According to the survey, there are examples and lessons that may be useful to regulatory authorities in advancing fintech and digitalized- based financing mechanisms, such as the need for appropriate and risk-based regulations, alternative regulatory approaches like sandboxes, and the importance of coordinating outreach to inform MSMEs.

This Survey addresses these questions in six different sections namely:

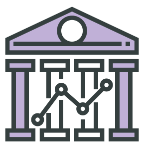
1

Landscape of MSMEs FinTech Financing in SME Finance Working Group Member Countries



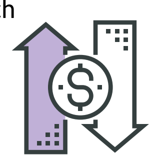
2

FinTech Regulation amongst SME Finance Working Group



3

Government support (financial/non-financial) on the use of FinTech



4

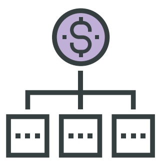
Investment and lending-based crowdfunding

5

Data protection and privacy

6

Credit information sharing



SECTION 1: LANDSCAPE OF MSMEs FINTECH FINANCING IN SME FINANCE WORKING GROUP MEMBER COUNTRIES

FinTech companies are considered new players within the financial ecosystem amongst most of AFI member institutions.

Most FinTech services in the member respondent countries are either regulated under the relevant banking act or supervised by the Security Commissions/ Ministry/Agency) of Non-Bank Financial Institutions (NBFIs) (Figure 2).

For example, in **Namibia**, **Suriname** and **Armenia** the Fintech services are supervised by formal financial institutions. There are countries that allow FinTech companies to operate without being regulated but have plans to develop a suitable regulatory framework such as the Maldives Monetary Authority (MMA), Central Bank of Solomon Islands (CBSI) and SUGEF (Costa Rica).

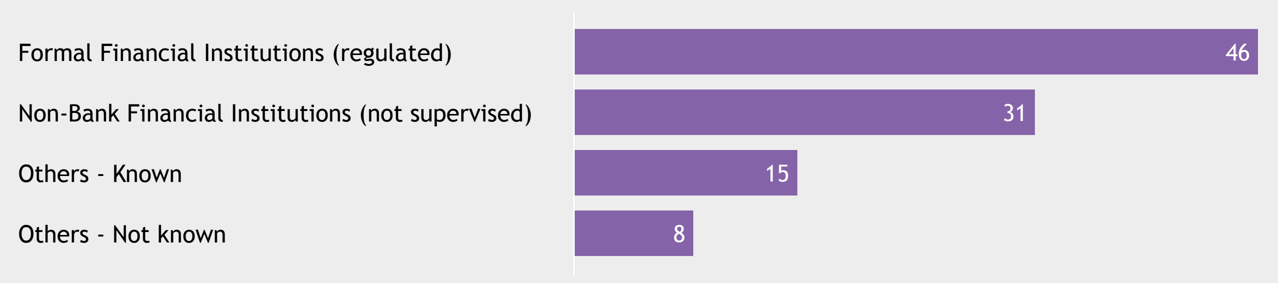
In the **Philippines**, the Financial Sector Forum (FSF) created a Fintech Committee to ensure the alignment of cross regulatory jurisdictions and regulatory responses. Until now, FinTechs and large IT companies have not often applied for banking licenses. However, there are some notable exceptions in both the EU and the US.[9]

62% Although 62 percent of members indicated FinTech companies are not local[10].

However, the **Philippines** shared that they do have homegrown FinTech companies in operation, such as FundKo, which offers online crowdlending that matches the borrower and the lender directly through their platform, and Acudeen, an online platform for receivables discounting. In **Costa Rica**, new FinTech companies offer credit to individuals as well to microenterprises through platforms such as the Emma (Easy Mobile Money Access) App. Amongst the services offered are, merchant and E-Commerce, invoice lending and P2P/marketplace lending are top of the alternative financing options made available by FinTech companies in member countries. Other members offer business sheet business ending, reward/donation-based and equity crowdfunding.

9 https://www.bis.org/fsi/fsipapers17.pdf
10 AFI SMEFWG Survey response: FinTech for MSME Finance (AFI, Sept 2020)

FIGURE 2: TYPE OF INSTITUTIONS THAT PROVIDE FINTECH SERVICES IN AFI MEMBER COUNTRIES, %



THE PHILIPPINES

The Philippines Financial Sector Forum (FSF) created a FinTech Committee (FC) in 2018 to develop a framework for a shared regulatory sandbox for activities that cross regulatory jurisdictions and ensure alignment of regulatory responses to FinTech innovation in the sector. The FSF is composed of four financial regulators in the country, namely the Securities and Exchange Commission (SEC), the Insurance Commission (IC), the Philippine Deposit Insurance Corporation (PDIC) and the Central Bank of the Philippines (BSP).

The objectives of the Philippines FinTech Committee include:

- Establishing a cohesive and consistent approach in the areas of regulation, supervision, and policymaking.
- Building the capacity of Regulatory Authorities (RAs) for enhanced supervision and oversight readiness.
- Creating an enabling regulatory environment for FinTech innovation.
- Ensuring that FinTech innovation fulfills the regulatory goals of maintaining financial stability.
- Upholding consumer protection, cybersecurity, and data privacy.
- Preventing money laundering and other illicit activities and strengthening situational awareness through information sharing, enhancement of surveillance capabilities and continuous monitoring of the developments in the FinTech landscape.

Source: AFI SMEFWG response from Bangko Sentral Ng Pilipinas (September 2020)

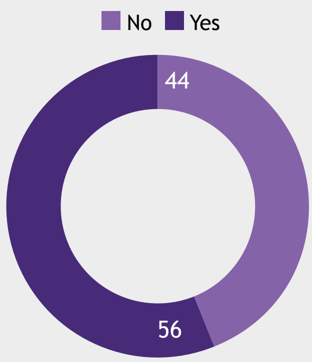
Using digital technology to manage small business, Philippines. (pixfly/Shutterstock

SECTION 2: FINTECH REGULATION AMONGST SME FINANCE WORKING GROUP

Regulatory frameworks in the financial sector typically incorporate both activity-based and entity-based rules. All institutions that provide a particular service must adhere to activity-based rules. In contrast, entity-based restrictions are imposed on organizations that have been granted a license to carry out a specific activity.[11]

More than half SME Finance Working Group members[12] have certain regulations/policy on FinTech companies for oversight and monitoring (Figure 3). In the process of regulating innovation, regulators are often faced with the task of balancing conflicting priorities such as market growth and competition with the integrity, safety and stability of the financial system[13]. With the establishment of appropriate regulatory frameworks, FinTech can contribute positively to the betterment of financial markets, including the economic well-being of the consumers and MSMEs, especially if this is done in a gender-sensitive manner; otherwise, they risk exacerbating the credit gap for MSMEs.

FIGURE 3: MEMBER INSTITUTIONS THAT HAVE FINTECH REGULATIONS, %



Source: AFI SMEFWG Survey response: FinTech for MSME Finance (AFI, Sept 2020)

These examples show the importance of designing and implementing effective regulations, taking into account financial stability, protection of investors, and supporting new financing channels for MSMEs. In addition, new financing models such as crowdfunding, that are increasingly emerging, may engage relatively inexperienced investors.[14] Besides MSME financing, other enablers and services that are currently leveraging on FinTech include risk assessment mechanism, credit guarantor and registry, credit Information bureau, wealth creation, insurance and others (mobile payment service). In **Afghanistan**, two regulations oversee the operation of FinTech companies: (i) Payment Systems Regulation and (ii) EMI Regulation. As for **Maldives**, while mobile payment services are regulated, other emerging FinTech service providers are not. The Maldives Monetary Authority (MMA) is developing a national payments infrastructure to enhance access for new entrants to the market, whilst developing the necessary regulatory framework for a conducive innovative and competitive environment in the industry.

23%

This finding is in line with AFI SURVEY REPORT ON ALTERNATIVE FINANCE FOR MSMEs which indicates 23 percent give positive response on 'enablers' leveraging big data in facilitating financing to MSMEs which includes responses relate to both existing infrastructure (credit information systems) and alternative sources of data, e.g. payments data and the use of mobile technology.[15]

It was found that four main areas of focus were identified by AFI network regulators, FinTech associations, and accelerator/incubator leaders for a comprehensive Fintech Ecosystem: (i) organizational structure; (ii) capacity building and upskilled involvement; (iii) regulatory framework and (iv) incentives.[16]

11 https://www.bis.org/fsi/fsipapers17.pdf
12 AFI SMEFWG Survey response: FinTech for MSME Finance. Results is 50 percent of a total 22 responses was used as a proxy to gauge the results of the AFI SME Finance Working Group as a whole. There are a total of 59 member institutions in the Working Group as of 28 April 2021.
13 https://documents1.worldbank.org/curated/en/579101587660589857/pdf/How-Regulators-Respond-To-FinTech-Evaluating-the-Different-Approaches-Sandboxes-and-Beyond.pdf
14 GPFI (2018).For details on measures to encourage innovation while minimizing risks, see "G20 High Level Principle of Digital Financial Inclusion," 2018.
15 https://www.afi-global.org/wp-content/uploads/2021/01/AFI_MSMEs_survey-report_AW_digital_0.pdf
16 AFI (Special Report) 2020. CREATING ENABLING FINTECH ECOSYSTEMS: THE ROLE OF REGULATORS

MEXICO

Mexico is the first country in Latin America to introduce a framework covering a wide scope of FinTech activities in legislation, the Mexico FinTech Law, enacted in 2018. The Law was prompted by the rapid growth of these activities in recent years, for example, the alternative finance industry in Mexico (including balance-sheet lending and crowdfunding models) increased by more than 7x from 2015 to 2016, and P2P consumer lending market volumes expanded by 90 percent in 2017. The Law now provides more opportunities for non-banks to enter the sector with more legal clarity, encouraging new products and links between banks, telcos and FinTech providers. The Law supports innovative FinTech activities by:

- Giving legal recognition to and setting supervisory frameworks for financial technology institutions (FTIs), which can perform the following activities: crowdfunding (debt, equity, co-ownership or royalties) and e-money (including e-wallets). The Law also mandates that entities currently offering crowdfunding or e-money services must request authorization by September 2019.
- Allowing FTIs and banks to make transactions using cryptocurrencies, subject to special authorization and rules issued by the central bank.
- Creating an obligation for financial services providers to share financial data with other providers and third parties specializing in technology through standard APIs (Open Banking).
- Introducing a regulatory sandbox for both nonregulated and regulated entities. For the former, the Law allows financial authorities to grant legal and regulatory exemptions to test products or services before becoming a regulated entity. For the latter, exemptions to the secondary regulation are granted to test innovative models. In both cases, eligibility criteria for testing apply.

The FinTech Law gives the Comisión Nacional Bancaria y de Valores (CNBV) and other financial authorities the power to supervise FTIs and innovative model institutions. New organizational structures within the CNBV have also been established to support the supervision of the new sector. The CNBV now houses a FinTech Supervision Department to oversee crowdfunding and e-money, and a Sandbox Team that works with both regulated and non-regulated entities seeking to test new innovations.

Source: AFI Special Report (2020). Creating Enabling Fintech Ecosystems

Shop assistant using digital technology to take e-payment. Mexico. (aldomurillo/iStock)

In pursuit of maintaining financial stability and protecting consumers, FinTech regulations would have to cross borders to have sufficient oversight on all the risk factors. Regulators need to have better international cooperation, as only 25 percent (Figure 4) of the survey respondents admitted to having some form of regulatory arrangements with another country to mitigate FinTech legal issues. Solomon Islands engages regionally and internationally with the governments of supportive and neighboring countries, international standards bodies, aid partners, and others via the National Information and Communications Technology Policy (National ICT Policy) by the Ministry of Communications and Aviation.

Market stability and consumer protection are among the main elements for regulators to consider in this new field.

75%

75 percent (Figure 5) of members indicate the availability of customer redress mechanism for FinTech related complaints, fraud occurrences or incidences regarding MSMEs.

For example, the **Central Bank of Russia Federation** has a hotline number for complaints about financial sector services even though it is not specifically for MSMEs. In **Ecuador**, MSMEs can go to the Superintendency of Popular and Solidarity Economy (SEPS) where FinTech companies are registered, or they can present their claims to the judiciary, where there are also agents specialized in combating financial crimes. There is a special department within the Bank of Mozambique that is responsible for consumer protection where all complaints regarding the offer of financial products and services by the providers of these services are directed, however there is still no space for complaints about the services provided by FinTech, since they are not yet operating autonomously.

Engagement between regulators and FinTech association(s) is needed to understand the perspectives and concerns from both ends, to gauge the likely impact of emerging products on consumers and the regulatory framework, thus ensuring careful alternative financing options for consumers and MSMEs. The majority of member institutions, about 70 percent, have FinTech associations to bridge the gap between industry and government.

To keep up with technological developments, the public sector has developed learning modules on FinTech literacy, cybersecurity in the design of businesses, online platform operations, personal and business data protection for FinTech financing, and operating model of FinTech lenders, to create awareness and educate central bank staffs on FinTech opportunities and risk management. In the **Philippines**, as part of the BSP's capacity building initiatives, the Financial Technology Subsector was established and comprises a Technology Risk and Innovation Supervision Department (TRISD). TRISD is primarily responsible for conducting onsite and offsite IT supervision of BSFIs to ensure safety and soundness of technology risk management processes, as well as establishing and maintaining a comprehensive, relevant, and flexible regulatory and supervisory framework relating to IT supervision. It is also charged with cybersecurity surveillance and oversight while promoting digital or FinTech innovation through BSP's regulatory sandbox.

FIGURE 4: ARRANGEMENTS WITH OTHER COUNTRIES ON CROSS BORDER LEGAL ISSUES, %

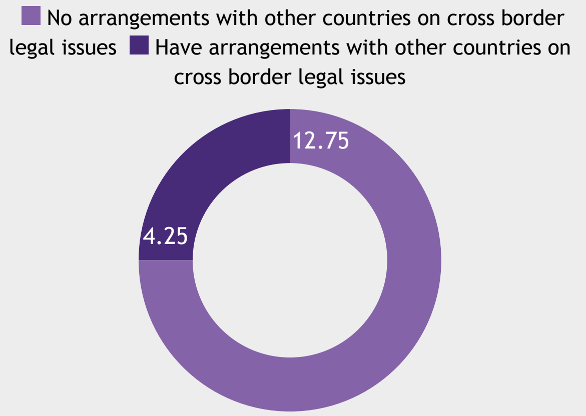
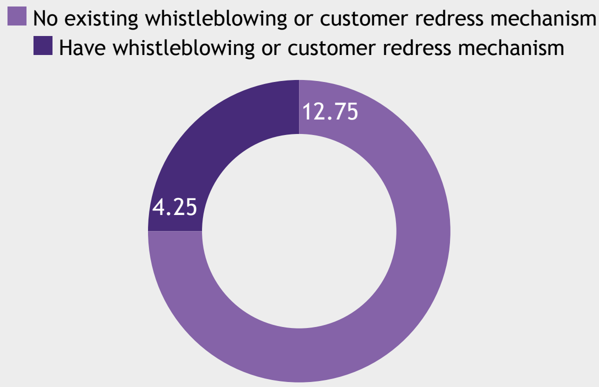


FIGURE 5: WHISTLEBLOWING OR CUSTOMER REDRESS MECHANISM FOR FINTECH RELATED ISSUES, %



EXAMPLES OF AFI MEMBER COUNTRIES FINTECH ASSOCIATION CHAMBERS

MOZAMBIQUE	PAPUA NEW GUINEA	ECUADOR	COSTA RICA	PHILIPPINES
> Financial Sector Deepening Mozambique (FSDMoç) > Mozambican FinTech Association	> Papua New Guinea Digital Commerce Association > YuTru (a private sector led digital trust framework)	> Chamber of E-Commerce	> FinTech Association Central America and the Caribbean	> FinTech Alliance encourages collaboration and cooperation among digital finance sector participants in the Philippines. > FinTech Philippines Association: independent industry association

DFS also has benefits for financial providers; they can diversify their loan risk across many smaller accounts and thus, making a run on a financial institution less likely, especially as women have lower levels of non-performing loans than men.

Additionally, DFS can also enhance financial stability and allow alternative ways to assess client risk, through big data and social media, ecommerce transactions, utility bill payments, and etc., to lower transactions costs and expand their reach and profits.

However, the rise of DFS and FinTech products also present new risks and threats, such as those stemming from opaque data privacy/data protection practices or systemic vulnerabilities from cybersecurity threats. These practices and vulnerabilities could undermine public confidence and trust in the financial system if it is not adequately protected/addressed. These concerns would be amplified in women, as it is widely understood that women's confidence and trust in the use of formal financial services are not on the same level as those of men.

Regulatory Technology (RegTech) and Supervisory Technology (SupTech) are considerable solutions for the integration and regulation of FinTech into a country's financial ecosystem and requires additional effort on the part of a central bank of financial regulatory body.

RegTech is any application or platform that makes regulatory compliance more efficient through automated processes and at lower costs. SupTech is the use of innovative technology to support supervision, helping supervisory agencies digitize reporting and regulatory processes, resulting in a more efficient and proactive monitoring of risk and compliance.[17] These elements will be important in creating a safe environment for the usage and implementation of FinTech for MSME financing.

From **AFI Survey Report on Alternative Finance for MSMEs**, Regulatory Sandboxes, RegTech and innovation office among the top three approaches used by the authorities to inform regulation for alternative finance.[18]

> View here

To keep up with the rapidly changing FinTech trends, innovation in regulation must be instilled across the regulatory ecosystem to ensure regulators can carry out their primary mandate for financial stability, integrity, and consumer protection. Regulators should also be up to date on recommendations and guidance set forth by the global Standard-Setting Bodies (SSBs) on new developments such as virtual assets. Key gender considerations also need to be integrated into the regulation at the outset and during any review of existing regulations and guidelines.

17 BANK FOR INTERNATIONAL SETTLEMENTS (2018). FSI Insights on policy implementation No 9 (July 2018). "Innovative technology in financial supervision (SupTech) - the experience of early users"., available at https://www.bis.org/fsi/publ/insights9.pdf).

18 https://www.afi-global.org/wp-content/uploads/2021/01/AFI_MSMEs_survey-report_AW_digital_0.pdf

SECTION 3: GOVERNMENT SUPPORT (FINANCIAL/NON-FINANCIAL) ON THE USE OF FINTECH

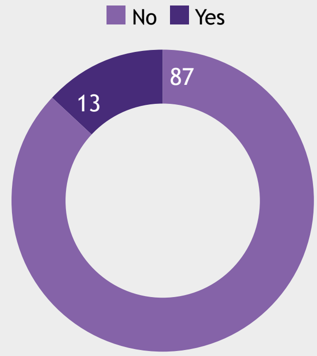
As much as we see opportunities emerge out of FinTech, the majority of respondents, at 87 percent (Figure 6), indicated that there is no government support available on the use of FinTech. However, some members have taken the initiative to support this industry.

In the Philippines, BSP pushes for an increasingly digital financial landscape, not just in the MSME environment, but have always been supportive in allowing a wide range of providers, including FinTech players, to enter the market and catalyze the development of financial products and services. In Solomon Island and Ecuador, the governments have allocated expenses (CAPEX/OPEX) for FinTech, while Costa Rica and the Seychelles provide government grants and investment for FinTech companies. These examples show Government acceptance and encouragement of the usage of FinTech within the financial ecosystem.

Both traditional alternative financing and FinTech-based financial providers may have different levels and approaches to financing terms across jurisdictions. **Ecuador, Timor-Leste** and **Mozambique** find FinTech providers easier to fund compared to traditional alternative financing services, whereas **Papua New Guinea** and **Seychelles** have opposing views. **Costa Rica, Solomon Islands** and **Suriname** indicate both FinTech providers and traditional alternative financing services are equally easy to fund. The mixed perspectives of financial regulators towards this new technology are indicative of its instability and risk, and despite the benefits it can bring to MSMEs and individual users, it leaves much to be fully comprehended by many regulators in the developing world.

Regarding the benefits, we asked SME Finance Working Group members on existing use cases. Members indicate that aside from MSMEs financing, credit information bureau, credit guarantee and registry and wealth creation for savings and investment are among the top enablers that leverage on FinTech in their operations. FinTech usage in the **Maldives** is seen in mobile payment services whilst the **Philippines** utilize it for e-KYC, digital-centric banking, sustained adoption of e-money, and use of virtual currency exchange. **Timor-Leste** use FinTech mostly for cash in, cash out and transfer fund, and **Mozambique** is in the midst of undergoing tests of the FinTech products with the resolution of regulatory aspects. Although sparse, these examples share that there are potential opportunities when regulators and financial supervisors can collaborate with FinTech players and, perhaps, a "test and learn" methodology can be considered via the adoption of regulatory sandbox, drawing on the good practices and learnings from the implementation of sandboxes across over 30 member jurisdictions.[19]

FIGURE 6: GOVERNMENT FINANCING OF FINTECH FOR MSMEs, %



Private-public dialogue becomes more pressing especially as we are amidst COVID-19, which has forced most of the world to transact digitally. As seen in AFI's Member Policy Response Dashboard, new digital financing initiatives are implemented at the same rate as national economic stimuli and, where the country case examples will illustrate, are complementary to the delivery of such stimuli. While MSME is one of the segments that were badly affected due to COVID-19, some MSMEs with digital footprint and leverage on FinTech and DFS experience new opportunity amid the pandemic.

19 Alliance for Financial Inclusion, (2020). Special Report on "Creating Enabling Fintech Ecosystems: The Role of Regulators" (https://www.afi-global.org/sites/default/files/publications/2020-01/AFI_FinTech_SR_AW_digital_0.pdf)

MALAYSIA

In June 2020, Malaysia issued its fourth economic stimulus package, named the Pelan Jana Semula Ekonomi Negara (PENJANA) or National Economic Recovery Plan, which is primarily aimed at helping businesses recover from the impact of the coronavirus pandemic. Some of the measures issued in PENJANA include new tax incentives, financial assistance for small and medium-sized businesses (SMEs), and job protection initiatives.

For the rural community, the package will provide MYR108 million (US$25 million) to help the most vulnerable members of society. A one-off MYR300 (US$70) payment are provided for:

- 190,000 registered disabled persons
- 150,000 single mothers who are below the poverty line
- 2,000 volunteer home help services

The Malaysian government has utilized e-wallets for the disbursement of MYR750 million (USD180 million) for G2P payments. A new Mastercard study shows about 40 percent of Malaysians surveyed are using mobile/e-wallets more, followed by debit cards (26 percent) and contactless credit cards (22 percent). Malaysia leads other countries in Southeast Asia in the usage of mobile/digital wallets at 40 percent, ahead of the Philippines (36 percent), Thailand (27 percent) and Singapore (26 percent).

Source: Ministry of Finance Malaysia, 2020 (https://penjana.treasury.gov.my/pdf/ePENJANA-FAQ-EN.pdf) and Mastercard, 2020 (https://newsroom.mastercard.com/asia-pacific/files/2020/06/Mastercard-AP-Consumer-Retail-Barometer_June-20204.pdf).

Using digital technology to make a contactless payment in a restaurant. Malaysia. (Photo by JimmyFam/iStock)

SECTION 4: INVESTMENT AND LENDING-BASED CROWDFUNDING

Six survey respondents namely the Costa Rica, Haiti, Mozambique, Papua New Guinea, Philippines, and Suriname have P2P financing platforms that are able to service households and MSMEs in economic activities including agriculture and farming, energy and green technology, and ICT.

We also found most respondents do not know the default rate of lending-based crowdfunding platforms available in their countries. In **Ecuador**, the Superintendencia de Economía Popular y Solidaria (SEPS) shared their default rate of less than 2 percent and in **Papua New Guinea**, it is between 2 percent - 3.5 percent.

For loan disbursement, **Ecuador, Haiti, Mozambique** and **Suriname** indicate P2P financing or lending platform take more than 14 days to disburse credit loans. The range of loans disbursed by P2P lending platforms ranges from USD1,000 to USD40,000 amongst respondents.

The low response rate towards P2P lending platform and other crowdfunding services could indicate the infancy of these services in the market. Respondents indicate that amongst the challenges towards adopting these services as alternative financing for MSMEs are the absence of government incentive to use lending-based financing platform, lack of awareness, and lack of understanding on its potential risks. The survey also found that most MSMEs are keen to explore newer technologies for financing due to its quick attainment rate. However, they do not necessarily take the step to engage these new services as penalty rates are not attractive enough. Overall, investment and lending-based crowdfunding platforms do not have high visibility/activity amongst the SME Finance Working Group member institutions. In their view, most MSMEs prefer traditional banking platforms as a source of funding.

A young customer smiles after paying for goods and services through mobile money transfer. (Billy Miaron/Shutterstock)

SECTION 5: DATA PROTECTION AND PRIVACY

Diversity of financial product and player helps to boost supply, cut costs, and promote financial inclusion.

However, there is a chance that it will generate risks for the stability and adequate functioning of the financial system.[20] The emergence of big data and artificial intelligence has amplified concerns around data privacy. Members are aware of threats to consumer protection experienced by MSMEs when accessing alternative finance options with newer technology.

The new regulatory categories for Fintechs do not always aim to control the specific risks they pose, but rather sometimes seek to promote increased competition or financial inclusion by imposing (temporarily) lighter requirements.[21] Most institutions do not have regulations to inform consumers of the ability of FinTech companies to access private data, those who are within the areas of commercial transactions, electronic communication platforms, and social media.

70%

However, about 70 percent of respondent (Afghanistan, the Philippines, Ecuador, Suriname, Papua New Guinea, Samoa, Solomon Islands and Mozambique) indicate there are government agencies that are tasked at implementing cybersecurity on a national level.

In the Philippines, the BSP has a comprehensive set of regulations in response to the increasing propensity and sophistication of cyber-attacks involving fund transfers, payments and other transactions via online channels.

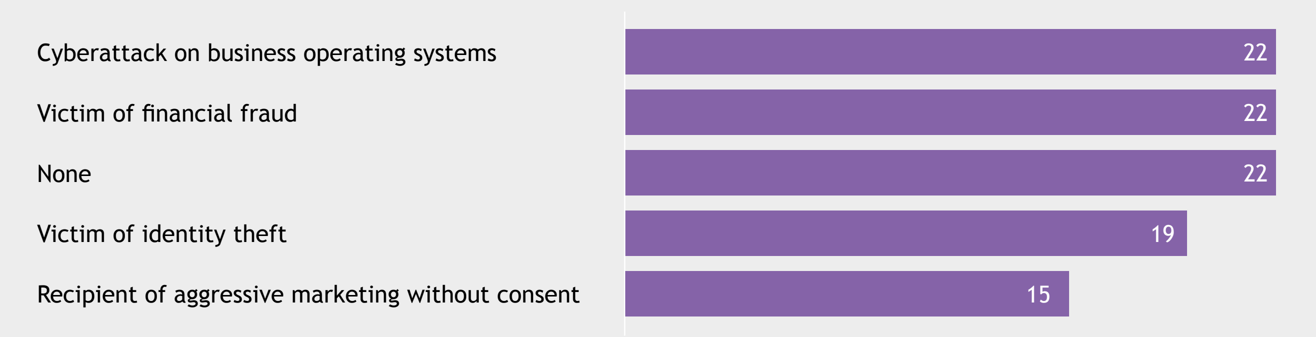
Most survey respondents indicate they do not have any initiative or program to inform MSMEs of the risks pertaining to data and consumer protection due to a lack of demand, as MSME business operations are not impeded by issues in this area. This is due to the fact that many of the MSMEs are made up of micro-enterprises, which operate in the informal sector and due to their unregulated nature, such issues may not be reported to financial regulators or central banks. Existing programs focus on FinTech literacy and are very rudimentary in nature without going into the details of risks of engaging alternative financing FinTech platforms. This is in line to the finding in the AFI SURVEY REPORT ON ALTERNATIVE FINANCE FOR MSMEs that confirms lack of awareness depicts the main reason of low take-up of alternative finance.[22]

20 See Carstens (2018) and FSB (2019).

21 This is the case in Singapore or Hong Kong SAR, where digital banks are allowed to operate temporarily with more flexible requirements until they reach sufficient scale. In the United States, the Office of the Comptroller of the Currency (OCC) attempted to reduce the barrier to entry in 2018 by creating Special Purpose National Bank Charters for FinTechs, allowing them to circumvent the complex state-by-state licensing method. State banking regulators, specifically the Conference of State Bank Supervisors (CSBS), challenged the legality of these new charters. However, in October 2020 the CSBS issued a new single set of supervisory rules - called CSBS Vision 2020 - that are intended to ease compliance burdens.

22 https://www.afi-global.org/wp-content/uploads/2021/01/AFI_MSMEs_survey-report_AW_digital_0.pdf

FIGURE 7: DATA PROTECTION & PRIVACY RELATED INCIDENTS EXPERIENCED BY AFI MEMBERS, %



SECTION 6: CREDIT INFORMATION SHARING

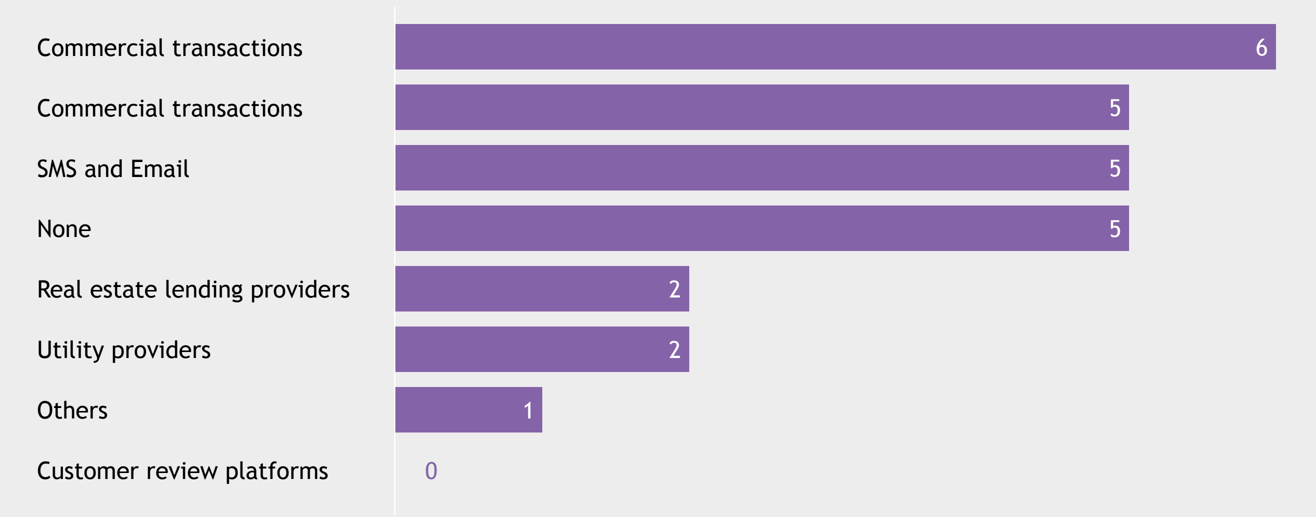
Having acknowledged that many MSMEs, especially microenterprises, lack the capacity or resources to produce formal financial statements and documentation that enable financial institutions assess their repayment capacity and default risk, FinTech companies deploy technologies to get an accurate understanding of MSME liquidity position.

Unlike the practices by traditional banks, the use of Big Data can allow MSMEs to be assessed beyond their traditional credit profile. The emergence of alternative data such as metadata and psychometric data help FSPs to assess MSMEs unconventionally that set for better credit worthiness and access for MSME financing. Powering better credit decisions with FinTech by expanding to new market segments, such as the New-to-Credit (NTC), new-to-bank, thin file, millennials and self-employed, lower the cost of risk by leveraging the predictive capability of AI and Machine Learning to consistently improve digital scorecards while lowering the cost of risk and deriving faster decisions, shortens the time-to-yes from days to less than 1 minute, with scores delivered in real time. Similarly, the survey found (figure 8) most institutions believe that FinTech companies use commercial transaction data to evaluate the risk level of MSMEs. Additionally, institutions are aware that data from social media platforms and communication tools, such as SMS and email are used for risk assessment by FinTech companies.

Information credibility and transparency is another vital element in assessing the data. Most respondents indicate they do not know the status of MSMEs data transparency that is used by FinTech companies to evaluate MSMEs credit rating, nor do they know if there is any regulation that bounds them for the data and ensures the accountability of the personal data use. This would also allude to the lack of knowledge on transparency requirements or laws on this matter.

In the nutshell, alternative data may not replace the formal credit sourcing system, but it can be an effective equalizer for the unserved and underserved market. When used responsibly, alternative data can contribute to greater financial inclusion and banks that leverage it will have a competitive edge over those relying strictly on traditional credit metrics.

FIGURE 8: KNOWN DATA SOURCES USED BY ALTERNATIVE FINANCING COMPANIES THAT USE FINTECH FOR ASSESSMENT



SURVEY OBSERVATIONS & RECOMMENDATIONS

Although FinTech is pioneered by the developed countries, FinTech is now well recognized and utilized as an alternative source of financing for MSMEs in the developing and emerging countries.

MSMEs are more attracted towards FinTech solutions for accessing financing due to higher efficiency at lower costs, mitigate information asymmetry and more diverse sources of funding. It complements the landscape of MSME access to financing as one of financial service providers. From the responses of the various SME Finance Working Group Members, it can be concluded that FinTech not only refers to digital payments but also acts as an additional source of credit, alternative capital and financial enabler within the MSMEs financing ecosystem. Investment and lending-based crowdfunding are prominent among members, particularly via crowdfunding platforms and Peer-to-Peer (P2P) lending.

The dynamism of financial ecosystems also been seen in the success of mobile money applications, leverage on digital footprint and digitalized data as part of the alternative credit scoring, showcasing their fast-paced advancements. Alternative data, such as periodical utility payments, payments to e-commerce platforms, psychometric data or other financial transactions made digitally, can create new sources of important financial information, reduce information asymmetry in the MSMEs credit market and overcome the barrier in providing risk assessment tools to formal financial institutions. Removing a key constraint on entry into the formal financial sector will not only encourage lending to MSMEs, but also permit those who are motivated to shift their economic activities from the informal sector to the formal sector. All of these factors can come together and be of particular benefit to women MSMEs.

Technology platforms increase the efficiency of transactions with the use of alternative data for customers, such as women and youth, who lack formal credit histories. Members identified that DFS and FinTech can enhance financial stability and can also allow alternative ways to assess client risk through big data, however, DFS and Fintech also present new risks and threats to data privacy or systemic vulnerabilities from cybersecurity threats. On data protection and privacy, majority of the respondents have government agencies that are tasked with implementing cybersecurity on a national level. However, from the public perspective, there is lower perceived risk of data and consumer protection, as MSMEs business operations are mostly informal with little effect for these concerns.

RegTech and SupTech are considerable solutions for the integration and regulation of FinTech into a country's financial ecosystem and requires additional effort on the part of a central bank of a financial regulatory body. Regulators need to find a balance in designing and implementing effective regulations that considers financial stability, protection of investors, cross-thematic topics and vulnerable groups such as women MSMEs, and also supports new financing channels for MSMEs without stifling the market.

Multi ethnic business team in office developing new crowdfunded project, Malaysia. (aldomurillo/iStock)

RECOMMENDATIONS

1 **FinTech associations and incubators need to discuss with regulators to understand the perspectives,** concerns and identify focus areas that require government intervention for a market-based, well-functioning and comprehensive FinTech ecosystem. FinTech and alternative data allow financial services to serve viable unserved or underserved customers. Private-public dialogue has become more pressing, especially amidst COVID-19, which has forced most of the world to transact digitally.

2 **Diversify Fintech based financial products beyond financial usage** as alternative data may also offer valuable granularity on customer preferences and behaviors that can be used to design innovative financial products and services that meet the unique needs of women and men. However, bigdata can suffer from algorithmic bias at the development stage and unless disaggregation of gender and age are actively built into systems.

3 **Adopt a "test and learn" methodology** and implement proportionate regulatory approaches similar to many AFI member countries, such as Kenya, Tanzania and the Philippines, to regulate innovative market deployments and as part of the precursors to the "regulatory sandbox" for FinTech that more than 30 jurisdictions globally have now implemented.[23]

4 **Despite of promoting growth and facilitating financing to MSMEs**, government and regulators have to ensure financial stability and apply a balanced macro mechanism approach to FinTech credit providers.

5 **Regulators should also be up to date on recommendations and guidance** set forth by the global Standard Setting Bodies (SSBs) on new developments such as virtual assets. Key gender considerations also need to be integrated into the regulation at the outset.

6 **Create more platforms for public awareness** and financial intermediary staffs on FinTech literacy, cybersecurity, online platform operations, personal and business data protection for FinTech financing, and operating model of FinTech lenders.

7 **Digital financial literacy campaigns should, therefore, focus on building trust** through the dissemination of accurate and unbiased information on different types of FinTech products and services, including their benefits and risks.

23 Alliance for Financial Inclusion (2018), "FinTech for Financial Inclusion", available at https://www.afi-global.org/thematic-areas/inclusive-fintech/

Women examining their organic farm growth with digital tablet. Malaysia. (Photo by chee gin tan/iStock)

ACRONYMS AND ABBREVIATIONS

AFI	Alliance for Financial Inclusion
AML	Anti-Money Laundering
API	Application Programming Interfaces
BOT	Bank of Thailand
BSFI	BSP-Supervised Financial Institutions
BSP	Central Bank of the Philippines
CFT	Countering Financing of Terrorism
CNBV	Comisión Nacional Bancaria y de Valores (Mexico) / National Banking and Securities Commission (Mexico)
DFS	Digital Financial Services
ECF	Equity Crowdfunding
FC	FinTech Committee
FI	Financial Institutions
FinTech	Financial Technology
FSF	Financial Sector Forum
FTI	Financial Technology Institution
G2P	Government-to-Persons
GFI	General Financial Insight
IC	Insurance Commission
ICT	Information and Communications Technology
IFC	International Finance Committee
KYC	Know Your Customer
MFI	Microfinance Institutions
MMA	Maldives Monetary Authority
MSMEs	Micro, Small and Medium Enterprises
NBFI	Non-Banking Financial Institution
NFES	National Strategy for Financial Education
NFIS	National Financial Inclusion Strategy
NTC	New-to-Credit
OECD	Organisation for Economic Co-operation and Development
P2P	Peer-to-Peer
PDIC	Philippine Deposit Insurance Corporation
RA	Regulatory Authority
RegTech	Regulatory Technology
SEC	Securities and Exchange Commission
SEPS	Superintendencia de la Economía Popular y Solidaria (Ecuador) / Superintendency of Popular and Solidarity Economy (Ecuador)
SME	Small and Medium-sized Enterprises
SMEFWG	SME Finance Working Group
SSB	Standard-Setting Body
SupTech	Supervisory Technology
TRISD	Technology Risk and Innovation Supervision Department

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