From Laws to Loans: Opportunities and Challenges in Achieving the Promise of Secured Lending Reforms

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FROM LAWS TO LOANS: OPPORTUNITIES AND CHALLENGES IN ACHIEVING THE PROMISE OF SECURED LENDING REFORMS

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Financial systems with institutional depth are core to inclusive economic development. Studies have shown that traditional measures of size of the financial sector and extent of financial intermediation are insufficient indicators of the financial sector's true contribution to economic strength[1]. Rather, it is institutional depth that determines whether financial systems can reduce inequality and levels of poverty, and support broad-based economic growth and resilience.

Small and medium-sized enterprises (SMEs) are the backbone of most economies, accounting for over 95% of firms, 50% of jobs and 35% of GDP across emerging economies globally[2]. Yet despite their importance, in many economies SMEs tend to be underserved by financial institutions and consequently face a disproportionate challenge in accessing finance. In many economies, historical economic, legal and cultural factors cause lenders to depend heavily on fixed assets – namely real estate – as collateral for loans. For SMEs that commonly do not own fixed assets of value sufficient to back their credit needs, this can create a prohibitive barrier to accessing finance.

Movable property lending (MPL) – the use of movable assets such as goods, equipment, inventory, receivables, vehicles, agricultural products and livestock as collateral for loans – offers great promise to broaden access to affordable finance, and thereby drive the creation of inclusive, resilient financial systems. Even if they do not own real estate, almost all SMEs globally own assets ranging from goods to accounts receivable that could serve as the collateral needed to open their access to credit. It is estimated that globally 78% of SMEs' asset base is movable property. The same applies to other commonly marginalized segments, such as women or certain minority groups, who are often legally or culturally inhibited from owning or pledging real estate.

MPL is a norm in most developed economies' financial sectors, and highly integrated with broad and cascading benefits. In countries with advanced systems for security interests, credit to GDP averages 60%, compared to 30-35% in countries without such systems[3]. Beyond expanding the availability of credit, the ability to use movable assets as collateral also reduces the cost of credit. Businesses commonly embed these savings into the price of their goods and services, leading to market benefits and greater prosperity far beyond the financial sector.

Despite the benefits, most developing countries lack the legal, institutional and cultural enablers necessary for MPL. Over the past three decades, governments and international donors have sought to address this disparity by investing in legal reforms and the creation of movable collateral registries to enable the expansion of MPL.

Today, countries are at various stages of implementing MPL-enabling legal and institutional infrastructure: while some are taking initial steps toward system modernization (e.g., Ethiopia),

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[1] World Bank, "Measuring Banking Sector Development," 2005, http://siteresources.worldbank.org/INTTOPACCFINSER/Resources/Banking.pdf

[2] OECD, Meeting of the OECD Council at Ministerial Level, "Enhancing the Contribution of SMEs in a Global and Digitalized Economy," 2017, https://www.oecd.org/mcm/documents/C-MIN-2017-8-EN.pdf

[3] IFC, "Secured Transactions and Collateral Registries": https://www.ifc.org/wps/wcm/connect/793e79804ac10fff9ea69e4220e715ad/Secured+Transactions+and+Collateral+Registries+Brochure-English.pdf?MOD=AJPERES

others have fully implemented a modernized legal framework and web-based collateral registry and are pushing towards broad adoption of MPL practices (e.g., Colombia).

To explore the intersection of MPL and women's access to finance, our team conducted a global survey of industry experts actively implementing MPL policies across over 30 countries. Evidence from the experiences of these countries on the extent and pace with which efforts to enable MPL has increased access to finance shows that the promise of MPL has not yet lived up to expectations. While some countries have seen progress towards success, the overall volume of MPL lending, the diversity of users and the range of assets pledged as collateral has been below the expectations of MPL advocates, regulators and implementers alike. Careful study of the factors that promote or impede adoption of a comprehensive MPL system are needed.

At the core of the challenges may be an issue of market failure in which supply (availability of capable lenders) and demand (potential borrowers) are not coming together. A key lynchpin for the MPL market to function is the willingness of banks and other providers of finance to invest in developing the products and services to take advantage of the opportunity that MPL presents. In many cases, banks and other financial institutions have been slow to make these investments. Countries such as Jamaica, Mexico and Colombia that have implemented full MPL reforms in recent years today are grappling with a common recognition that despite registry activity, banks on the whole have failed to move into new MPL products and categories beyond the leasing and factoring that had occurred prior to reforms.

COLOMBIA RESEARCH & FINDINGS

Our team conducted a series of interviews and documentary research to survey the status, impacts and lessons of MPL reform efforts in more than 30 countries over the past three decades. Informed by the findings of this survey, we sought to explore the question of MPL implementation further, looking in detail at Colombia as a case study. Having modernized its legal infrastructure in 2013 and implemented a digital collateral registry in 2014, Colombia has among the most advanced MPL infrastructure in Latin America and among developing countries globally.

Nearly four years after these reforms, the results of MPL implementation in Colombia to date exhibit many of the same limitations seen in other countries at comparable stages of MPL development – an early surge of registrations (including existing liens under prior law) has been followed by a slower growth pace of registration. Banks have shown little interest in investment. Initial uptake has largely focused on motor vehicles; of transactions attributed to businesses, accounts receivable lending remains below 3% of transactions, and business equipment represents just 2.6% of assets registered.[4] The same is the case for other countries with modern legislation and collateral registries, such as Mexico. While Colombia has some unique contextual considerations, it has enough in common with the experience of other countries looking to introduce MPL to make Colombia a compelling case from which to draw insights about what may be driving these results, and what might improve them.

Over the course of a multi-month study, our team engaged with over 50 Colombian officials responsible for implementing and regulating MPL, including senior bank executives, financial technology (fintech) leaders, industry executives, SME owners and a variety of other stakeholders in the Colombian financial sector. The research sought to understand the causes of the relatively

[4] Percentages refer to the share of total transactions in which a business is the borrower; it excludes transactions attributed to individuals or "natural persons"

slow pace of banks' investment in broadening their portfolio of MPL products and services, and to develop a formalized understanding of the business case for banks to invest.

Our research found that while a clear market need for MPL exists in Colombia – with unmet demand for credit among formal SMEs with suitable credit estimated at over $6.2 billion – the traditional banking sector has been slow to embrace potential new products in the face of regulatory challenges and market incentives, as well as uncertainties and costs related to market entry investments. The foremost barrier to entry cited by banks is the weakness of related and supporting industries, particularly those that would provide services such as asset valuation, seizure, and liquidation to would-be MPL providers. The relative underdevelopment of these enabling industries limits outsourcing opportunities for banks, requiring additional investment to build them in-house.

Beyond these constraints explicitly cited by banks, a range of other factors impact the scale of demand and the incentives for banks to enter the market for MPL:

- **Business formality:** high levels of informal, non-incorporated business activity limit the prevalence of certain collateral (e.g., invoices)
- **Alternative products:** programs that encourage unsecured lending and inefficient credit products crowd the market for MPL
- **Nature of competition within and among banks:** limited incentives for banks to aggressively capture additional market share limits the attractiveness of MPL
- **Data and product understanding:** banks' poor market and product understanding limits awareness of market potential and how it can be tapped
- **Relationship and reputational concerns:** mistrust between banks and borrowers rooted in recent historical context limit the perceived feasibility of MPL, particularly around seizure of assets
- **Risk assessment practices:** banks' generally limited understanding of how to assess the risk of growth-oriented SMEs prevents them from accessing credit and drives potential MPL customers out of the financial system

These findings point to several opportunities for targeted interventions to promote uptake of MPL in the Colombian context, the majority of which extend beyond the realm of legal and regulatory reform. While Colombia has sought to address both legal and non-legal ecosystem components in its approach to date, focusing on four main areas could help overcome existing constraints that to date have limited bank uptake and broader MPL activity:

1. **<u>Build awareness</u>:** While awareness has already been a significant component of Colombia's approach to date, additional investment is needed to **address gaps in understanding among banking executives and key regulators** of the practical dimensions of MPL implementation who have been the traditional targets of training. In addition, reformers should work to **extend training across staff levels** within these institutions in order to reach customer-facing employees and their manager who are often best positioned to identify opportunities for MPL.
2. **<u>Prove the market:</u>** In particular, reformers and supporting investors should **direct support beyond the traditional banking sector to other categories of lenders that exhibit promise as first movers** (e.g., fintech, financing companies, etc.). These institutions – some of which are already incorporating MPL into their business models – can provide services and play a catalytic role in proving the potential of the MPL market. **Investing in the development of comprehensive, reliable and authoritative data** on

SME credit, disaggregated by sex, would facilitate accurate assessments of the MPL market and targeted deployment of capital.

3. **Reduce barriers to entry:** MPL advocates should **investigate the role that current guarantee programs (e.g, Fondo National des Garantias) are playing on banks' incentives to develop MPL offerings**, and consider ways in which a new generation of guarantees could be structured to promote uptake of these new lending opportunities. **Encouraging specialization** around select categories of MPL (e.g., retail inventory financing, supply chain invoice financing) not only at the business level but also at the economy level could also help jumpstart MPL in areas where there is most promise.
4. **Adapt regulation:** Legislators and regulators should consider **adapting provisioning standards to reduce focus on valuation for highly rated credits**, while keeping terms in line with international standards. **Enhancing cross-government coordination on enabling business growth** across various stages of development, particularly at transition hurdles, could also help reduce redundancies or competing programs that slow MPL uptake.

Based on our prior global scan, we believe many of these findings and recommendations may have broad applicability.

GLOBAL IMPLICATIONS

At the highest level, these findings affirm a hypothesis that is increasingly gaining traction: that **the movable property lending market depends not purely on legal reform and a digital registry, but also on a complex "ecosystem" of factors** that together enable a market for MPL. Some of these factors can be developed and influenced, while others are fixed either for the medium-long term or indefinitely and must be adapted to. This has particular implications for countries currently facing challenges with MPL uptake among banks, as barriers may exist beyond traditional focus on capacity building and awareness.

In addition to adopting an ecosystem approach, the Colombia case points to five dimensions that can lead to improved outcomes for secured transactions reform with global applications:

- **Continuous education and training**: keeping up with natural employment cycles that may take place over the course of MPL implementation and reaching across staff levels, with an emphasis on practical implementation
- **Anticipate policy consequences and adapt:** crafting policies that both comply with international standards and reflect local contexts that may affect the behaviors that policies induce, together with putting monitoring and evaluation tools in place to indicate when policies may need to be adapted, particularly in early stages
- **Focus on strategic first movers:** looking beyond traditional banks to the priority first movers in the MPL market and directing support accordingly, while recognizing the important role for banks as part of the MPL system in the long term
- **Cultivate MPL as a product:** supporting lenders to develop not only a specific set of capabilities to conduct processes such as valuation and seizure, but also a tailored approach to risk assessment, pricing, customer selection, marketing, client management, and sales, among others
- **Careful use of incentive structures:** where required to stimulate the market, structuring incentives such as guarantees to stimulate market activities without encouraging long-term dependency

Research findings also point to an explicit **set of factors that influence the potential for MPL to have a tangible impact on access to finance, both broadly and in particular for women**. While in most cases MPL opens up channels for finance that offer opportunities for new or underserved borrowers over the long term, the extent of impact on reducing existing financing gaps in the short term depends more on the pipeline and profile of SME owners and the specific nature of the barriers they currently face in accessing finance than on the kind of collateral they own and its value.

Similarly, findings surface a **set of factors that influence the rate at which banks can be expected to invest in and take up MPL**. In the case of Colombia, factors dampening the competition between banks may weaken the incentive for investing in MPL without regulator or development interventions. In their absence, these factors may position alternative lenders such as fintech enterprises, leasing companies or equipment manufacturers to be more agile first market entrants.

IN SUMMARY

MPL is an essential and beneficial element to deepening a country's financial sector, with consequent benefits for financial resilience, inclusion and economic growth. Around the globe, mature MPL systems help SMEs to large multinationals access affordable credit suited to their business needs that enables them to grow and innovate, with far-reaching economic benefits.

There are limits to MPL's applications; MPL fills financing gaps but does not replace unsecured or traditional fixed property lending. In particular, unsecured lending will continue to play a critical role, both in Colombia and globally, in enabling access to finance for much of the population and business community, particularly those tied to regions, populations and business categories (e.g., micro-business, informal sector) that have traditionally been marginalized from the financial sector. Regulators and financial services providers should view MPL as one of a series of tools that together can work to ensure that individuals and businesses are able to access affordable credit to meet their needs.

While the benefits of MPL are clear, we have found that the pace and extent with which those benefits can be realized depends on the complex interplay of many contextual dependencies, ranging from existing cultural norms related to lending, asset ownership and access to finance, to aspects of banking regulation and financial industry structure. Even as law reforms take time to produce results and convert traditional ways of thinking, many of these variables are susceptible to tested development and regulatory interventions, presenting opportunities to both enable and accelerate implementation.

The secured transactions community today is at an inflection point as country experiences increasingly demonstrate the limitations of traditional approaches to MPL implementation focused on legal reform and digital registries. Moving towards an approach that intentionally takes into consideration the full ecosystem of factors that influence MPL is the first step towards better structured, better resourced and ultimately more successful implementation programs. More research is needed to deepen our understanding of successful tactics and how they may vary across different contexts.

1.0 INTRODUCTION

THE PROMISE OF MOVABLE PROPERTY LENDING

Access to finance is a core underpinning of prosperous and resilient societies. Countries with inclusive financial systems are not only more resistant to economic shocks, their financial sectors directly contribute to reductions in poverty and inequality by allocating funds to the most productive uses, distributing risk and empowering even marginalized groups with the tools they need to achieve sustainable livelihoods[5].

There is growing consensus that expanding access to finance, particularly to small and medium enterprises (SMEs), is key to reducing income inequality, promoting long-term growth and enhancing social stability. The availability of a wide range of financial products, services and processes to overcome price and non-price barriers to accessing financial services plays a critical role in lifting people out of poverty, enabling entrepreneurs to invest in projects and driving broad-based growth.

While it may be only one type of financing, credit is among the most important types of financing for economic development. Credit allows firms to access resources needed to make investments in productivity and growth at a relatively low cost and without major implications for their legal and management structure. At the macroeconomic level, by pooling financial resources to support purchase of productive assets, lending can stimulate productivity and spending, and thereby contribute to economic expansion over time.

Despite its importance, businesses and individuals around the world face significant barriers to accessing credit. According to IFC estimates, formal micro, small and medium enterprises (MSMEs) alone face a global credit gap of over $2.6 trillion,[6] with the total MSME financing gap estimated to be over $5.3 trillion.[7] Of the estimated over 400 million MSMEs in developing countries, only 14% have a formal line of credit and between 50-70% are unserved or underserved by the financial system,[8] meaning they are unable to fulfill their full financing needs given the current structure, requirements and constraints of the financial system.

Borrowers face a range of challenges in accessing credit, and key among them is difficulty in providing collateral. Lenders depend heavily on collateral to secure lines of credit, a common practice globally but particularly in markets where information asymmetries – either real or perceived – are pervasive. Collateral reduces the risk of non-payment and can enable lenders to offer large loans at lower cost. However, legal and cultural preferences for real estate as collateral

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[5] World Bank, "Measuring Banking Sector Development," 2005, http://siteresources.worldbank.org/INTTOPACCFINSER/Resources/Banking.pdf

[6] IFC, "Secured Transactions and Collateral Registries": https://www.ifc.org/wps/wcm/connect/793e79804ac10fff9ea69e4220e715ad/Secured+Transactions+and+Collateral+Registries+Brochure-English.pdf?MOD=AJPERES

[7] IFC, "'Banking on Women," http://www.ifc.org/wps/wcm/connect/industry_ext_content/ifc_external_corporate_site/financial+institutions/priorities/banking-on-women

[8] IFC, "Secured Transactions and Collateral Registries: Global Perspectives and Registry Survey Results," 2016, https://www.iaca.org/wp-content/uploads/World-Bank-Group-Survey-Results.pdf

create barriers to accessing finance, particularly among SMEs that often do not own any or sufficient real estate to secure their credit needs. While 74% of commercial loans use real estate as collateral, on average less than 22% of SME assets are in the form of real estate.

In many developing economies around the world, the only or main form of credit available to most of the population is secured credit. Only the wealthy elite tend to have access to unsecured credit beyond micro-finance. While the extremely poor may have access to small amounts of unsecured credit, in most cases this is only as part of a government- or development fund-sponsored social policy. A lack of suitable collateral is thus blocking SMEs from access to sufficient and affordable credit.

Women, who own less than 20% of privately held real estate worldwide, are particularly vulnerable to being denied access to credit as a result of collateral requirements emphasizing real estate. Only 10% of commercial loans currently go to women; globally, women-owned SMEs face a $1.5 trillion financing gap, 32% of the world total despite accounting for 28% of businesses.[9] Around the world, social norms, institutional barriers and even legislation frequently explicitly and implicitly give men preferential access to real estate over their women counterparts, or bar women property owners from using it as collateral to access finance.

Increasing awareness of this phenomenon has enhanced focus on MPL. According to IFC estimates, approximately 78% of all assets owned by SMEs globally qualify as movable assets that could be used as collateral[10]. Already implicit in the vast majority of developed country financial systems, expanding the range of acceptable collateral in emerging markets to explicitly include movable assets presents a promising pathway to expanding access to finance to many of these would-be borrowers.

While MPL is less commonly a development focus than other tools to enable access to finance, it is not a niche part of developed financial systems. In developed economies, MPL represents around 60% of total lending and is a key contributor to the resilience of banks and the overall financial system.

The promise of MPL has caught the attention of gender and inclusion advocates, who view women and other underrepresented groups as particularly likely beneficiaries in light of known barriers to owning real estate. In addition to boosting SME access to funding, MPL thus also presents an opportunity to narrow gender disparities in access to finance, a key stepping stone in boosting economic participation and broader social empowerment of women and minorities.

THE EXPERIENCE OF MOVABLE PROPERTY LENDING

In recent decades, policy makers and development practitioners have sought to capitalize on the promise of MPL, establishing international standards,[11] investing in partnership with governments

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[9] IFC, "Banking on Women," http://www.ifc.org/wps/wcm/connect/industry_ext_content/ifc_external_corporate_site/financial+institutions/priorities/banking-on-women

[10] IFC, "Collateral Registries for Movable Assets", https://www.ifc.org/wps/wcm/connect/8891c280415edb709ba3bb9e78015671/Collateral+Registries+for+Movable+Assets++Does+Their+Introduction+Spu+Firms+Access+to+Bank+Finance.pdf?MOD=AJPERES

[11] See, for example, the United Nations Centre on International Trade Law (UNCITRAL, *Model Law on Secured Transactions*, http://www.uncitral.org/uncitral/en/uncitral_texts/security/2016Model_secured.html.

in efforts to modernize countries' legal frameworks pertaining to secured lending, and establishing movable property collateral registries.

In a number of countries, these investments have resulted in tangible improvements in access to finance:

- In China, four years after implementing a digital registry and modernizing its legal framework MPL reforms had facilitated over $3.5 trillion of financing of which roughly $1.1 trillion went to new SME financing. 63% of SMEs that obtained new loans using accounts receivable had some female ownership, of which 20% are majority-owned by women.
- Ghana began MPL reforms in 2008 with a new secured transactions law and launched Africa's first modern web-based collateral registry in 2012. At the end of 2014, 60,000 loans were registered, valued at $14 billion. More than 8,000 SMEs received loans.
- Colombia established a secured lending law in 2013 and new centralized collateral registry in 2014. Over 100,000 loans were secured with movable assets in less than one year, and 5,000 of those loans were for SMEs, valued at $3.43 billion.

Despite these notable gains, there is wide and growing recognition that MPL has yet to reach its full potential impact on access to finance, even in countries that have had multiple decades for their systems to mature. In many cases, registries show collateral disproportionally restricted to a few types of assets, such as motor vehicles; banks have been slow to adapt products and services to offer MPL at scale; and SMEs continue to face challenges engaging MPL to overcome traditional barriers to accessing finance. In Jamaica, which has recently modernized its legal framework, banks have failed to make investments in MPL at any meaningful scale. Colombia, recognized as a leader in secured transactions in Latin America, has seen only limited progress. In short, the promise of MPL has yet to fully translate into expected gains in access to finance.

There is an emerging view among secured lending experts and development practitioners that there is a need to review the tactics and strategies commonly deployed to implement MPL and to broaden our understanding about what works. What drives the pace of MPL market development, and what interventions beyond legal reform and registry establishment can foster it? Early hypotheses point towards the need for an "ecosystem" approach that emphasizes the importance of factors beyond legal reform and registry creation alone. Others emphasize the need to view MPL from the perspective of market development and examine the incentives for private investment to grow supply of and demand for MPL-based lending products.

BUILDING GLOBAL UNDERSTANDING

In October 2017, USAID's Office of Gender Equality and Women's Empowerment (GenDev), Deloitte and Banyan Global joined forces to examine this topic. At the outset, our research sought to explore the intersection of MPL and women's access to finance, with a goal of identifying investment opportunities that would enable target countries to achieve tangible milestones in MPL implementation that would translate into new credit opportunities for women-owned SMEs. (The study is detailed in Appendix A.)

Our global survey of industry experts actively implementing MPL policies across over 30 countries surfaced several common barriers to implementation, touching on both supply and demand variables. These barriers represent fundamental challenges to MPL serving SMEs at large, causing us to refocus our research on opportunities for MPL to promote SME access to finance broadly, as a means to serve women.

Key among them was a critical gap in supply of MPL products and services – following the creation of legislation and collateral registries enabling MPL, simply not enough banks are investing in creating products and developing the market. In cooperation with USAID's network of Missions, we selected this topic for investigation, using Colombia as a case study. Guiding our research was the question: *Is there a business case for banks to invest in MPL? And if yes, what is that business case?*

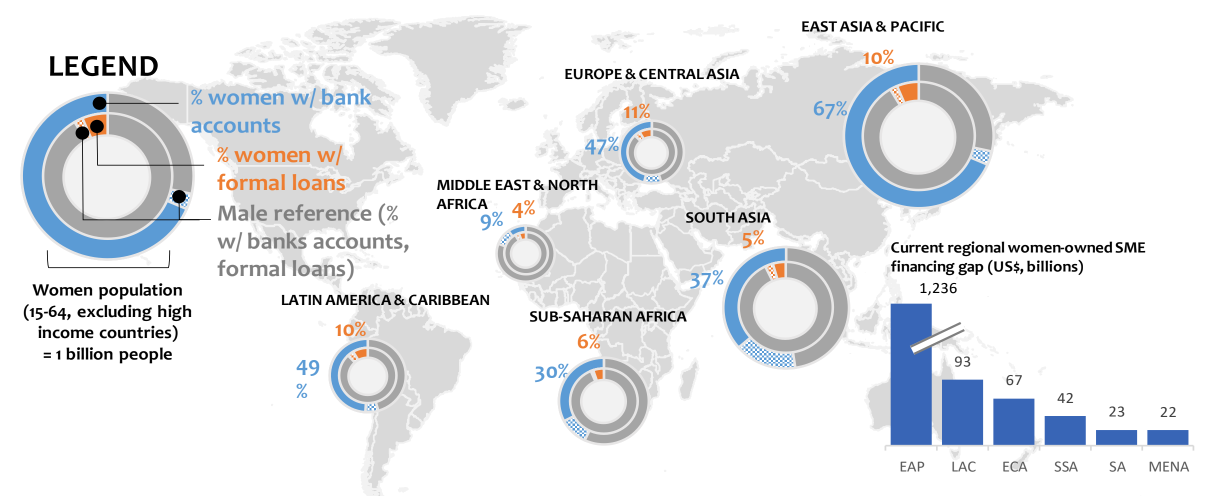
This paper is the second paper in a two-part series that captures our findings. The first in the series is an investor document that describes the market opportunity for MPL in Colombia. Building on our initial research questions, that document does not focus solely on traditional banks but rather evaluates multiple types of lenders that may be poised to enter and catalyze the market.

In this paper, we delve deeper into opportunities and challenges to implementing MPL, drawing on both our global survey and our deeper research in the context of Colombia. In doing so, we focus on the supply side, exploring the market constraints that impact the business case for banks to invest in MPL. Despite the evidence of a market for MPL, our findings indicate that the business case for traditional banks to be first movers into this market today is less clear. Based on these findings, we present a number of insights that shed light on how MPL implementation in Colombia and other countries globally may be approached so as to accelerate and enhance realized benefits.

Throughout the paper we circle back to the topic of gender. Despite the clear potential connection between women, property ownership and MPL, in practice the impact on women's access to finance is more complex. In highlighting learnings about contexts in which MPL can impact women's access to finance, we will also point to limitations which remain in our understanding, and to questions for further research.

The global gap in women's access to credit

While overall access to credit in mid and low income countries lags far behind OECD standards, women in emerging markets are disproportionally excluded from the financial system. The financing gap for women-owned SMEs exceeds $1.5 trillion.



Movable property lending: a tool for women's access to finance?

PART I: MPL and Gender – an Introduction

MPL creates new channels to access finance, particularly for enterprises that lack fixed property. Around the world, millions of women are legally or culturally barred from owning real estate, the main form of acceptable collateral. Despite advances in gender norms, today women own no more than an estimated 20% of privately held real estate, increasing the likelihood that collateral requirements pose a barrier for women business owners to secure credit. Thus, while potentially benefiting all kinds of SMEs, MPL can play a critical role in enabling women's access to finance, particularly among women-owned SMEs.

MPL can enable women's access to finance directly and indirectly in four main ways:

- **Enabling entrepreneurial women to scale:** For women that have aspirations to scale their businesses from small, to medium and beyond, MPL creates opportunities to access new and cheaper forms of financing.
- **Activating latent borrowers and entrepreneurs:** In areas where collateral is a key obstacle to accessing finance, making MPL available can provide incentives for creation and formalization of women-owned businesses.
- **Enabling deeper reach through lower transaction costs:** As MPL systems mature, product and process innovations along with economies of scale can help reduce transaction costs, making MPL increasingly accessible even to very small and micro businesses.
- **Creating economic opportunities for women:** By unlocking new flows of capital to enable growth SMEs broadly, both men and women-owned, MPL creates economic opportunities for women.

Which of these **channels** is most important, the initial **scale** of impact and the **timeframe** over which effects materialize will vary based on a combination of factors affecting women's roles in the economy and society-at-large. In countries where women are empowered participants in the economy but real estate ownership is a constraint, MPL has strong potential for short-term gains. In regions where women are accessing finance through alternative products or deep social barriers to women's entrepreneurship exist, impact is likely to emerge after a longer timeframe, or to require other interventions complementary to MPL.

As in many countries, information on the state of women's access to finance in Colombia is sparse. However, evidence suggests the country falls into the latter of these two categories. While women are engaged participants in the business community, the majority of women-owned businesses are concentrated in the micro-sector of the economy where unsecured lending is the established practice. Realizing the full effect of MPL on women' access to finance broadly requires the removal of gendered and gender neutral barriers to entrepreneurship, and time for existing micro- and SME- financial systems to adjust to the option of MPL.

Subsequent sections of this paper explore the case of Colombia in further detail, particularly as it pertains to women's access to finance and MPL. Findings point to a number of key lessons with local and global applications, as well as areas for further research.

Colombia: A Case Study of Challenges and Opportunities in MPL Implementation

2.0 THE CASE FOR COLOMBIA

Countries experience MPL reform differently as a culmination of their respective historical, economic, social and political contexts. Yet commonalities do abound, particularly among countries at similar stages of economic development, making comparison both viable and valuable. Factors such as similar financial system governance structures, market performance (e.g., low credit to GDP ratios) and the sophistication of related and supporting industries lead to common barriers and opportunities for MPL implementation.

Based on our global study, Colombia presented an ideal case study to explore supply-side barriers that have led to banks' slow uptake of MPL among commercial banks. Colombia has enacted one of the more robust packages of secured transactions reforms. However, their collateral registrations so far are primarily comprised of vehicles; commercial banks have not widely adopted MPL products, suggesting an underdeveloped business case for MPL in the private sector. Our team also identified Colombia as an opportunity to model MPL solutions for neighboring countries in Central and Latin America once the business case for commercial banks to provide MPL was developed.

To understand the causes of the relatively slow pace of banks' investment in broadening their portfolio of MPL products and services, and to develop a formalized understanding of the business case for banks to invest in MPL, our team conducted a multi-month study of the MPL situation in Colombia. Over the course of the study, we engaged with over 50 Colombian officials responsible for implementing and regulating MPL, including senior bank executives, financial technology (fintech) leaders, industry executives, SME owners and a variety of other stakeholders in the Colombian financial sector. (Appendix B contains a full list of the interviewees and contributors to the study.)

Colombia is both a regional and global leader in MPL reform, having been one of the first developing countries to successfully reform its legal infrastructure and build a digital registry to align with global standards. In this respect, it offers advantages as a case study, presenting an opportunity to study its experiences over the four years since the legal reforms and registry were up and running. While the country has key distinctive traits, in total its experience with SME finance and approach to MPL implementation present numerous opportunities for comparison with other countries.

Among Colombia's distinguishing features is its micro-finance sector, which is one of the more robust globally, particularly among Latin American and other developing nations[12]. A number of private and government sponsored institutions serve the sector. Guarantee programs delivered by the Fondo Nacional des Garantias (FNG), which covers up to 50% of qualified loans, and the USAID's Development Credit Authority (DCA) program have further encouraged the sector. Colombia represents 13% of cumulative loans issued by the DCA globally[13]. While the strength of the sector presents advantages for financial inclusion, it also affects the potential market for MPL by offering an alternative product to serve SME customers.

A second distinguishing feature is Colombia's unique political and economic situation. While Colombia's financial sector and economy have enjoyed relative stability over time despite pervasive domestic conflict between and among the government and various paramilitary groups, the 2016 peace agreement has cast uncertainty on the future of the economy and key sectors.[14] While the peace agreement presents significant opportunity to improve the predictability of the investment environment and overall macroeconomic conditions, the accords remain tenuous and outcomes far from certain. This uncertainty has been compounded by the dramatic decrease in oil prices that has significantly diminished a critical source of public and private sector revenue. The government has initiated a series of reform efforts to promote diversification of the economy, however this massive undertaking is in its early stages and investment levels remain low.[15]

A third distinguishing factor is Colombia's large informal economy, estimated at over 55% of employment[16], which affects the availability of certain assets that could serve as collateral, particularly invoices. This, together with commonly sub-standard corporate accounting practices in the formal economy, creates challenges for banks to evaluate business creditworthiness by traditional means[17].

Despite its distinctive features, Colombia parallels other developing countries implementing MPL reforms in a variety of relevant parameters. The financial sector has traditionally struggled to serve the SME sector, a key target for MPL, facing many challenges associated with perceived borrower risk, borrower business acumen and financial institutions' ability to reach potential borrowers across underdeveloped infrastructure. Beyond SME services, the financial sector faces common challenges as well, including under-developed capital markets, evolving regulations with some associated issues with regulatory coordination and overlap, among others.

Moreover, the approach to MPL implementation in Colombia has engaged a common set of donor-supported efforts that have taken place or are underway elsewhere. With support from institutions such as the IFC and other World Bank Group members, the Colombian government started its

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[12] IADB, Microfinance Market Trends," 2014

[13] USAID DCA, DCA Data, 2017, https://www.usaid.gov/results-and-data/progress-data/data/dca

[14] OECD, "Colombia: Review of the Financial System," 2016, https://www.oecd.org/finance/Colombia-financial-markets-2016.pdf ; IMF, "Colombia: Financial System Sustainability Assessment Update," 2005, https://www.imf.org/external/pubs/ft/scr/2005/cr05287.pdf

[15] Banco de la Republica, "Current Situation of the Colombian Economy," 2017, http://www.banrep.gov.co/en/publications/report-by-the-governor-april-2017

[16] Council of the Americas, "Weekly Chart: Latin America's Informal Economy," 2015, https://www.as-coa.org/articles/weekly-chart-latin-americas-informal-economy

[17] IMF, "Colombia: Financial System Sustainability Assessment Update," 2005, https://www.imf.org/en/Publications/CR/Issues/2016/12/31/Colombia-Financial-System-Stability-Assessment-Update-18485

MPL implementation efforts with a legal reform effort, followed by the launch of a digital collateral registry, successfully aligning both with international standards. Ongoing efforts have expanded to adjacent training and capacity building, yet have remained mostly focused on senior bank officials and government regulators, a common focus across countries

In this respect, Colombia represents a case where traditional methods have had relative successes yet still present clear opportunities for further growth, allowing research to reveal both effective tactics to reproduce its achievements, while surfacing opportunities to adapt and improve our approach. Ongoing government focus on and support for MPL in Colombia likewise present an attractive market to conduct research, as well as positive prospects that recommendations will lead to tactical reforms in the country.

"Leading the pack yet struggling to hit its stride"

Among countries that have invested in updating their legal frameworks to enable MPL over recent decades, Colombia is recognized as one of the few to have succeeded in aligning its laws with international best practice and establishing a highly effective centralized digital registry. It has the most advanced MPL infrastructure in Latin America and is one of the front-runners among developing economies globally.

Nearly five years since completing its legal reform and four years since setting up the national collateral registry, Colombia provides an opportunity to reflect upon and draw lessons from its trajectory to date. While still in its early stages, understanding how MPL activity has taken shape and the main drivers of the level of activity can inform implementation efforts in Colombia moving forward, as well as other countries either underway with or embarking on similar journeys

A GLOBAL LEADER IN LEGAL REFORM

Colombia implemented Law 1676 in 2013 enabling financial entities to offer movable asset-backed lending products, with the end goal of supporting small business owners in increasing their access to finance.[18] Several decrees and resolutions were subsequently incorporated to bolster the sustainability and feasibility of the legal framework. Major resolutions included the implementation of the movable guarantees registry in 2014, the establishment of movable assets as suitable collateral, and the definition of Chamber of Commerce tariffs for contract execution procedures. These efforts continue with work underway to codify approaches to valuation of collateral, and introduce electronic invoicing to facilitate invoice-based MPL.

The launch of registry and legal reforms triggered an early surge in MPL. Within the first year of establishing the centralized collateral registry, over 100,000 loans were secured with movable assets, indicating the promise of the tool and legal framework.

[18] Ministry of Commerce, Industry and Tourism (MinCIT), "Secured transactions law benefits merchants, business persons, and entrepreneurs, 2013, http://www.mincit.gov.co/englishmin/publicaciones/imprimir/7968/secured_transactions_law_benefits_merchants_business_persons_and_entrepreneurs.

“The public sector efforts to build out the legal framework are complete. Financial entities have the sufficient legal foundation to begin offering movable asset-backed credit products.” – Unidad de Regulación Financiera

MOVABLE PROPERTY LENDING IN COLOMBIA TODAY

Indicators of MPL: Movable Guarantees Registry

Today, evidence of MPL activity is spread across different segments of the Colombian economy, both in terms of borrowers and lenders. Prior to implementation of the formal MPL legal framework, forms of movable property lending were already taking place (e.g. receivables financing via the *cuenta control*/"Lockbox" mechanism and limited forms of receivables financing), and as of November 2017, over 1,600,000 notices of security interests[19] were registered as loan collateral in Colombia, benefitting twenty different industries[20]. While registry statistics such as these reveal high levels of activity, a closer look at the MPL beneficiaries and the most common collateral types in use reveal that the vast majority of MPL in Colombia today is only reaching certain segments of the economy compared to the full MPL market potential.

Users / Beneficiaries of MPL Today

Various types of financial entities leverage the registry today, indicating that usage of MPL is applicable for the greater financial sector. Currently, 95% of registry usage stems from Colombian banks while 5% of the registrations root from other types of creditors such as fintechs, specialized financing companies[21], and individuals.

Registry statistics additionally reveal that MPL is far more often used for individual borrowers than registered businesses, but of the business registrations, SMEs are the most common borrowers.[22] In terms of industries represented, while MPL is applicable to all industries with suitable assets, the services, transport and warehousing, construction and manufacturing industries have been first in the market to leverage MPL in Colombia.

Movable Collateral in Use

While motor vehicles comprise the significant majority (85%) of registry submissions, the presence of lending secured by accounts receivable and specialized machinery and/or equipment indicate the potential for broader use of MPL in the market. Accounts receivable, machinery and equipment

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[19] According to UNCITRAL, a notice of security interest is a communication in writing that articulates a legal claim on collateral that has been pledged, usually to obtain a loan

[20] Movable Guarantee Registry, Confecámaras, 2017

[21] Financial entities specialized in financing a specific asset class

[22] The debtors are mostly natural persons (98%), or individuals, while the remaining two percent are registered businesses. Approximately, three-fourths of registered businesses are small and medium enterprises (74%), a key target population to benefit from MPL.

today make up only a very small share of registrations today at 0.5%, 0.4% and 0.4% respectively.[23]

The MPL activities that leverage accounts receivable products include usage of a lockbox account, or a *cuenta control* mechanism; factoring; and term loan practices by both banks and non-financial entities alike. Financial entities (mainly non-bank institutions), and fintechs are leveraging accounts receivable as collateral by establishing relationships with their borrower's client, often big buyers or anchor companies with credible payment histories to validate their providers cash flow. Factoring (the sale of invoices in exchange for a discounted sum of cash) by banks and fintechs also leverage the possibilities behind invoice financing.

In terms of machinery and specialized equipment, a few financial entities are pursuing partnerships with specialized industry players to acquire an expertise on particular machinery needs in the marketplace. This development facilitates access to clients, resale markets and valuation procedures. In a similar vein, bank and non-banking institutions are engaging in financial leasing practices to leverage machinery and specialized equipment as well.

"Lending against cars [in Colombia] is not a new practice. As an economy, we are at an inflexion point where we should be thinking about sustainable mechanisms for financing such as lending against the movable guarantees or assets that we know enterprises have." – Juliana Alvarez, Banca de las Oportunidades

UNFULFILLED POTENTIAL

While MPL is occurring in Colombia today, it is limited in reach and diversity of transactions. 85% of movable collateral registrations arelimited to motor vehicles,[24] a practice which occurred before the new MPL legal framework but which is benefitting from the new framework's efficiency. Over-representation of vehicles may be due to the merging of the automobile registry and the movable property registry, transferring over collateral already in use (primarily vehicles) rather than representing new lending catalyzed by new MPL opportunities. This may indicate that much more of the registry activity may represent existing lending than initially suggested by the statistics.

The concentration of motor vehicle collateral registrations is indicative of the reality that few banks have invested in expanding their MPL offerings. While most express interest in MPL products, this has not translated into meaningful changes in their portfolio of products and services. Previously existing financial leasing and factoring remain the predominant forms of MPL beyond vehicles.

Consequently, there is reason to believe that the types of MPL occurring in Colombia today may not represent significant new lending activity, particularly to the scale anticipated given the volume of SMEs. While efforts to move existing lending based on movable collateral onto the registry is a positive sign, there is reason for skepticism around whether activity to date is indicative of product innovation that can broaden financial inclusion over the longer term.

[23] Accounts receivable make up 3.6% of non-vehicle registry submissions while machinery makes up 2.6%; this amounts to 0.5% and 0.4% of total registry submissions; Source: Confecamaras, registry data, 2017

[24] Of the submissions to the movable guarantee registry, 85% are vehicles. Movable Guarantee Registry, Confecámaras, 2017

To help enable and accelerate update, regulators are investing in additional support infrastructures such as the centralized registry for electronic invoices or *facturas*, and the development of a virtual secondary market, *el martillo electronico*, to support implementation of the legal framework. However, this investment has yet to incentivize fully the greater financial ecosystem to consider investing in MPL based products and its impact remains to be seen

3.0 MAKING THE CASE FOR AN MPL MARKET

Are Colombia's banks missing a critical business opportunity by failing to invest fully in MPL? The answer to this question begins with understanding the market. Growth in factoring, leasing and other emerging MPL products, coupled with a large SME financing gap in Colombia indicate a significant market for MPL, with key entry opportunities around three main types of collateral.

SMES ARE THE TARGET MARKET

Small and medium enterprises represent the core of the market for MPL in Colombia and are a large potential customer base. Across the country, there are estimated to be over 4 million MSMEs, including nearly 250,000 formalized small and medium enterprises[25]. They are responsible for around 80% of employment and over 40% of GDP[26].

Today, SMEs are dramatically underserved by the country's financial system. According to the ANIF, less than 35% of SMEs are accessing formal credit[27]; an IFC study found that over 70% of SMEs report being underserved[28]. While statistics may vary, all tell the same story – financial institutions are leaving a huge customer segment untouched, representing a financing gap – and thus potential market – estimated at over $36 billion[29]. Taking into consideration large companies omitted from this figure, the market is likely significantly larger.

According to IFC global estimates, movable assets – any asset that is not fixed to the ground – comprise on average 78% of total business assets[30]. For SMEs, particularly growth stage or women-owned businesses that are less likely to own their own real property, the share is often even higher. While not all movable assets can effectively serve as collateral, conservative estimates posit over 85% of Colombia's SMEs have suitable assets[31] in the form of either accounts

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[25] IFC, 2010

[26] Ministry of Commerce, Industry, and Tourism, "Productividad, formalización, innovación y internalización, desafíos para Mipymes," 2016, http://www.mincit.gov.co/publicaciones/36871/productividad_formalizacion_innovacion_e_internacionalizacion_desafios_para_mipymes

[27] ANIF "La Gran Encuesta PYME," 2017, http://www.anif.co/sites/default/files/encuestas_pyme/2017/12/gep_regional_i-2017.pdf

[28] IFC & McKinsey, "Two trillion and counting- Accessing the credit gap for micro, small, and medium-sized enterprises in the developing world," 2010, http://documents.worldbank.org/curated/en/386141468331458415/pdf/713150WP0Box370rillion0and0counting.pdf

[29] ibid

[30] IFC, "Collateral Registries for Moveable Assets: Does Their Introduction Spur Firms' Access to Bank Finance?" http://www.ifc.org/wps/wcm/connect/8891c280415edb709ba3bb9e78015671/Collateral+Registries+for+Movable+Assets++Does+Their+Introduction+Spu+Firms+Access+to+Bank+Finance.pdf?MOD=AJPERES

[31] Estimation of businesses having 'suitable assets" is based on an assessment of whether MSMEs have some amount of either accounts receivable, equipment, inventory or a combination of these, based on the nature of their business. It does not take into consideration the volume and associated value of these assets and whether the value would meet a minimum viable threshold for MPL based on current industry standards

receivable, equipment or inventory[32.] Based on estimated average financing gaps, this represents a potential credit market of almost $6.2 billion among formal SMEs alone (almost $16 billion if micro and informal SMEs are included), excluding potential applications for large enterprises.[33]

Beyond market size estimates, businesses providing finance to SMEs are demonstrating the potential of the MPL financing market. Companies such as Mesfix, a financing company focused on factoring (the sale of invoices in exchange for a discounted sum of cash), have seen rapid growth (see box below). A survey of SMEs by independent investment banking firm Heritage Capital found broad agreement among participants over the need for tools to finance technology equipment upgrades. Compared to global benchmarks, MPL is far below the expected share of the economy. Factoring amounts to just under 4% as a share of GDP in Colombia, compared to nearly 12% in Chile and over 15% in the United Kingdom.[34] The market remains wide open and far from saturated.

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and transaction costs. It also does not take into consideration whether MPL would be the best financing tool for these businesses, which would need to be based on a more comprehensive understanding of each business's financial needs and standing.

[32] Deloitte analysis, based on SIREM Income Statement Database (2017) – Superintendence of Societies

[33] "Credit market" refers to the total estimated face value of the loans required to fill the outstanding demand for credit represented by SMEs in Colombia that have accounts receivable, equipment or inventory that could be used to secure a loan (estimated 86%), and either report being unserved or underserved by the Colombian financial system (estimated 53%). The total is based on an estimated average credit gap per business, according to the business's size category. It is assumed that MPL could address part of this market. Insufficient data is available to assess what share. It does not represent the potential revenue or profit to the lenders, which would be a fraction of this value.

[34] Factoring turnover statistics (includes domestic and foreign factoring): FCI, Annual Report 2017, 2017, https://fci.nl/downloads/Annual%20Review%20%202017.pdf

4.0 CRITICAL MARKET CONSTRAINTS

While market potential points towards a substantial opportunity for MPL in Colombia, the ability and desire of Colombian banks to capture that market are influenced by constraints that shape their expectations around potential returns. These constraints take several forms: some are real, while others may be only perceived because of information asymmetries; some affect the addressable market, while others impact financial institutions' abilities to capitalize on that market; some have direct effects on the market, while other may be indirect. Each points to a discrete challenge for MPL implementation. While some are the result of the relatively short time span since the legal system was modernized and will ultimately require time to shift traditional habits and mindsets, others suggest the potential to accelerate MPL implementation through strategic interventions.

The Colombian banking executives we interviewed consistently recognized three categories of constraints that limit their ability to access the MPL market profitably. Other constraints discussed below represent ecosystem factors that, while less universally cited, restrict the addressable market and raise the expected initial cost of market entry.

CONSTRAINTS ON THE BANKS

The three most common barriers to MPL market entry cited by banks were valuation; seizure; and resale. For most banks, these challenges clearly placed MPL below the threshold for priority investment.

Valuation

Banks perceive the valuation of the specific business assets used as collateral for credit to be challenging given the complexity of valuing different asset types, the lack of valuation standards and the current undeveloped valuation industry. As a result of these considerations, the perceived cost, feasibility and risk of valuation undermines banks' appetite for investment in broad MPL market entry.

Lack of understanding and perceived complexity of valuing collateral in large or high-value segments, such as crops, inventory, and specialized machinery is a key concern. Executives focused heavily on the challenge of assigning value to assets that may evolve in form over time, such as manufactured goods or crops. Limited existing standards heightened perceived risk and ambiguity associated with this task. Others recounted the cost required for frequent visits to borrowers to assess the status of the collateral.

In addition to challenges assigning a value to an asset, banks were also concerned with the cost of outsourcing that service to third-party providers, which is common practice in developed-country MPL markets. Given the relatively small number of valuation companies and limited standards on fees for service, banks reported general concerns about the potential for high or unpredictable fees. This increased concerns about the costs of building a capability in-house that would be able to capture a sufficiently large market to be profitable.

While some banking executives interviewed acknowledged the potential for specialization and partnerships to overcome some of the costs and other challenges of building a valuation capability in-house, for most the associated risk of doing so in an environment without valuation standards was a strong disincentive.

There is some question as to whether these represent real or perceived barriers. Discussions with banking executives in developed markets did reveal a ready availability of asset valuation consultants as key to success. These executives also emphasized two other factors that reduce the criticality of collateral asset valuation: first, the norm of lending primarily against cash flow and client relationships, with collateral viewed as an expression of that trust and commitment rather than as a prime justification for lending; and second, the fact that developed country provisioning requirements tend to be based on loan performance rather than collateral coverage. This suggests ways in which banking and regulatory practices can evolve in relation to collateral valuation, to better support development of the MPL market.

Default and seizure

Concerns related to seizure were twofold: the risk of asset flight, and also potential impact on community relations.

The most common concern among surveyed banks related to enforcement was that, by nature, movable assets could easily disappear in the case of pending default and seizure. While the MPL legal framework enables an expedited execution process (via a Chamber of Commerce or notary instead of being limited to traditional judicial processes) that would reduce the risk of an asset disappearing or deteriorating in the time to seizure, the question remains whether banks could effectively capture the asset in a timely manner.

Surveyed banks also perceived the consequences of default and therefore seizure of the movable collateral to be potentially damaging to their brand, and thus difficult to do. Banks risk their current and potential client relationships, and community standing when physically removing a key asset that may be tied to a client's livelihood, production activities, and employment in the community.

The challenge and associated brand risk of seizing movable collateral was the most commonly cited concern related to accounts receivable or invoice-backed financing, which would otherwise circumvent challenges associated with valuation and liquidation by nature of the fact it is already in "near-cash" form with a denoted value. Surveyed banks generally held the view that accounts receivable could simply "disappear overnight" and thus presented significant risk. As we discuss later in this paper, mechanisms and practices exist to significantly reduce this risk in relation to accounts receivable.

Liquidation and resale

Key barriers to investment in MPL related to liquidation and resale focused on the cost and logistics of holding a physical asset until liquidation, and the feasibility to convert the assets into cash efficiently. Although a critical part of the execution process, pursuing resale markets for a variety of assets is not part of banks' core business, and executives commonly believe that the potential illiquidity of markets for used, specialized business assets would lead to high storage costs and reduced effective valuation/sale costs.

While some banks engaged in the leasing business manage a resale capability internally, this is generally limited to vehicles, which have a mature second-hand resale market in Colombia. Nonetheless, leveraging an existing platform, perhaps focused on a narrow set of specific asset classes, and formation of alliances with equipment manufacturers and distributors to accommodate assets for resale may prove viable and profitable.

“The banking sector’s delayed reaction may be perceived as disinterest in MPL products. In reality, banks are interested, but also find it challenging to accept movable collateral due to additional considerations in valuation, seizure and resale.” –Ida Mestre, Asobancaria

ECOSYSTEM BARRIERS

Beyond the main direct challenges highlighted by banks, a broad range of other “ecosystem” barriers affect the viability and market for MPL in Colombia today. Some of these barriers represent institutional gaps that can be filled through investment-driven solutions in the short to medium term. Others, however, are the result of deeply embedded norms which impact the nature of risk assessment and, in turn, the potential for MPL.

Level of business formalization

Colombia’s economy, like many other countries at comparable stages of development, is driven in part by a large number of informal enterprises. The combination of taxes on formal businesses, often weak enforcement of laws restricting the informal economy, and arguably less familiarity with formal business management systems, has caused many businesses in Colombia to refrain from formally incorporating and registering. Although the simplified corporations law (Law 1258, 2008) did have a notable impact on bringing a significant number of businesses into the formal sector, the policy mainly targeted a limited category of “corner stores”, and thus has not had as large an impact on other sectors.

The prevalence of informal business has an impact on the availability of suitable assets that can be used as collateral. Ownership of or rights over business assets may not be sufficiently documented to support their legal assignment as collateral. Further, informal enterprises prefer to conduct businesses in cash, which results in avoiding invoices that could be used as collateral. While this is particularly common in the agriculture sector, it affects other sectors as well, including retail and services. Informal accounting processes affect the ability of businesses to demonstrate the basic cash flow required to analyze a loan application. Many of these businesses may have steady cash flow due to long standing relationships with buyers, but may not have the documented history of invoices to prove it.

Informality curbs demand for MPL by disincentivizing growth past a scale where businesses can remain informal, thus capping the scale of their financing needs and their potential contribution to the economy. Moreover, informal business are more likely to tolerate imperfect financing products and tactics, such as using multiple personal credit cards, which represent profitable alternative means for banks to serve SME customers over investing in MPL.

Alternative products

SMEs’ approaches to accessing their financing needs in Colombia today, particularly to the extent that it generates profits for banks, significantly impacts the business case that banks perceive for MPL. In the case of Colombia, both government-supported guarantees (mainly for “unsecured” lending), as well as common use of high interest rate personal loan products detract from the business case for investment in MPL products which may be seen by individual banks (and individual departments within banks) as detracting from the market for these existing practices.

Government sponsored loan guarantees, such as those offered by both the Fondo Nacional des Garantias (Colombian Guarantee Fund, or FNG) have a complex impact on the market for MPL and the business case for banks. While they create an important pathway into the financial system for many borrowers by lowering the risk-to-serve taken on by financial institutions, guarantees can also create incentives that increase the relative attractiveness of credits secured only by the guarantees compared to other collateral such as MPL.[35] Size limits on some qualifying guaranteed loans also creates an incentive to provide loans at smaller amounts than may otherwise be demanded by the market. This has a distorting effect on the market for MPL, encouraging banks and microfinance institutions to provide larger microfinance products without collateral than the market would otherwise allow, rather than develop more suitable MPL products. As a result, microloans cut into the potential MPL market, suppressing both supply and demand.

Beyond enhancing the attractiveness of unsecured lending, some banks have reported that they attribute an increase in default rates among borrowers to guarantee programs, which reduce the consequences of such defaults. This perpetuates a perception among banks that they are already serving the riskiest, marginal clients, thus creating skepticism that adding MPL as a product offering would allow them to grow their customer base.

Reliance on external guarantees also dulls the incentive for banks to develop their risk assessment, lending and collateral competencies that would otherwise assure greater inherent financial resilience, and greater capacity to develop and manage an MPL portfolio.

Other common practices among SMEs to access finance when loans are not feasible are bank account overdraws and personal credit cards, which often carry high interest rates. In addition to masking the potential market for MPL, these products are highly profitable for banks, creating little incentive for banks to invest in other products that might move customers away from them.

Nature of competition within and among banks

One of the main arguments for investing in MPL is customer retention and the opportunity to increase market share by capturing customers with more competitive products. However, a number of banks in Colombia view customers banking with multiple banks as validation of customer credit standing and have this embedded into their risk mitigation strategies. Broadly, while they may pursue incremental growth products, Colombia’s largest banks are largely comfortable with their current market positioning and are not necessarily growth-oriented. The lack of a corporate culture that values aggressive pursuit of market share in turn detracts from the attractiveness of any objective business case for MPL.

Banks’ internal structures also affect the pipeline of potential MPL customers and the case for investment. Some banks are structured so that different business units serve different customers at different stages in their development. For example, Bancamia (majority owned by BBVA) provides micro-finance, while BBVA bank serves larger customers. As a result, while hypothetically banks might be incentivized to offer MPL to retain customers as they grow, and also move them into more stable, profitable categories (assuming larger businesses are more profitable), this does not necessarily play out in reality. “Graduating” borrowers from micro-finance actually manifests as customer loss to the micro-finance business, and therefore the business may not be incentivized to actively help customers matriculate to different products. This adds to

[35] This does not imply that MPL is an appropriate substitute for unsecured lending in all cases. In particular, frequently small loans / “micro-finance” are more efficiently delivered as an unsecured lending product, to both the benefit of the lender and borrower. The exact threshold over which secured lending is beneficial compared to unsecured lending will vary by market and borrower.

other pressures for micro business to stay micro or limit their financing demands to what can be served through micro-finance.

These structures detract from the business case for banks to invest in MPL, and also suppress demand. Banks with profitable micro-finance businesses (which, as noted above, are often supported through guarantee programs) are unlikely to encourage small or micro businesses to pursue alternative types of financing, which would generally be a key channel for businesses to learn of and move into MPL. They are also unlikely to work with borrowers to build their capacity to access larger loans or more mature forms of financing.

Related and supporting industries

MPL depends on a number of related and supporting industries, among them valuation, resale markets, and insurance. In Colombia, weaknesses in these industries increase the investment banks must make in order to deliver them in-house or promote their growth externally, reducing potential ROI and detracting from the business case.

While valuation and resale are discussed elsewhere in this paper, insurance is likewise a challenge. Compared to more mature MPL markets such as the US where there is a strong culture of insurance and supporting industry, Colombia lacks an established standard and practice to insure assets beyond vehicles, land and buildings. MPL commonly relies on multiple layers of insurance in order to protect pledged movable assets and assure payback in the case of damage to or theft of the assets – this is particularly true for crops and other perishable assets.

In Colombia, insurance could help enable MPL to meet banks' standards, yet for many insurance appears as a fee, and thus acts as a disincentive to MPL demand. Multiple other barriers make it difficult for SMEs to access insurance, particularly related to the relative maturity of the insurance sector: the agricultural sector in particular reports lack of specialized insurers who understand their business (e.g., crop insurance). Others face challenges getting crop insurance because their crop size is too small.

An assessment of the role of insurance in the Colombia context indicates that the importance of insurance is a function of broader insurance practices. While gaps in insurance may deter some banks from MPL, it is likely not as critical to a functional MPL ecosystem as it is in developed countries such as the United States where diverse types of insurance are more commonplace and are a cultural and business norm.

Data collection

While Colombian banks have a general sense that there is a market for MPL, there is inadequate understanding of the specific nature and scale and distribution of the market potential. Few studies have focused on the demand for financing among SMEs, distinct from micro enterprises. Moreover, many banks do not track how many customers they are losing because they "graduate" from micro-lending and do not have the appropriate credentials to access financing through other bank products.

Because of the absence of data, banks are not clear on the market potential of MPL, allowing them to dismiss investment to serve the market and reinforcing a perception that MPL is costly relative to potential gains. Lack of understanding of target customer segments also contributes to banks' sense that they do not have the capacity to successfully introduce MPL, causing further hesitation to invest.

Reputational and relationship concerns

The nature of confidence and trust between banks and their customers inherently influences how banks and borrowers assess risk and in turn the perceived feasibility of MPL. In Colombia, the country's recent history of conflict, with groups living outside the law, drives skepticism among banks around the likelihood of being able to take control of assets that could by their nature be moved. Trust in the rule of law and the value of contracts thus plays a key role in making the case for MPL.

Banks, SMEs,borrowers and other stakeholders in the financing ecosystem also describe a broad culture of skepticism of banks among the public. This raises concerns about the optics and feasibility of seizing assets. Banks are concerned that seizing assets, whether a piece of equipment, crops or accounts receivables could have a sufficiently negative impact on the public's view of them that it could damage their reputation and cost them business. They are also concerned that the public skepticism about banks could limit their ability to seize assets (e.g., concerns about safety, etc.) This supply-side concern is generally corroborated by demand-side stakeholders, who commonly report a public view that banks often are not aligned to their values and may not be trusted.

Risk assessment practices

For borrowers that do aspire to grow and move into customer categories that could utilize MPL, broader gaps in Colombia's entrepreneurship ecosystem and specifically capabilities within banks to serve high-growth companies present barriers to scaling and deter them from seeking credit from banks. Entrepreneurs commonly report a lack of understanding among bank customer service representatives of how to evaluate the risk levels of companies investing heavily in growth that may appear net-negative on cash. As a result, these companies commonly turn away from the traditional banking sector for financing, instead accessing credit through personal products, international funds, private investors, friends and family, among other sources, thereby also eliminating a potential customer base for MPL.

Beyond the banking system, broader challenges for entrepreneurs such as the lack of early stage seed funding also limit the number of businesses that graduate from micro and move into SME categories. While indirectly related, the weakness of the entrepreneurial ecosystem stymies the pipeline of businesses that would potentially seek out and benefit from MPL.

Movable property lending: a tool for women's access to finance?

PART II: The Case of Colombia

Women are active participants in the Colombian economy. Both the public and private sectors have taken significant steps in recent decades to make financing products available to women, leading to the establishment of lending institutions such as Banco W, and Fundación de la Mujer, among others. Yet, while stakeholders concede there is still a gap in women's access to finance, early evidence suggests the potential short-term effect of MPL is constrained by two main factors: the pipeline of women SME owners, and support for alternative unsecured lending products.

In conservative, less affluent areas where social norms are more likely to bar women from owning real estate and using it as collateral, these same norms also tend to prevent women from growing their businesses beyond micro and very small scale. As a result of these norms against women's economic participation, women are under-represented among SME owners;

whereas they own micro and very small enterprises at roughly equal rates to men, estimates of ownership of small and medium enterprises range from 20-35% of the total, which are generally perceived to be generous estimates.[36]

This creates a scenario where women-owned/operated businesses are concentrated at a scale where micro- and unsecured- lending predominates. Women most likely to suffer from a lack of collateral as a barrier to accessing finance are less likely to run businesses at the scale required for MPL to be financially viable in early stages. Particularly in Colombia where unsecured micro-lending is well-developed and commonly subsidized through public sector sponsored guarantee programs, unsecured forms of credit are perceived to be a preferable product for both borrowers and lenders in this market, up to a much larger loan value than might be accepted in markets without the existence of a subsidized guarantee system.

While data is limited, anecdotal evidence suggests that women in Colombia that do operate true medium and large enterprises may more commonly benefit from an ecosystem of norms and support mechanisms that compensate for and diminish gender disparities in property ownership. While there are exceptions, preliminary findings indicate these women more often have education, income, professional networks, inheritances and/or other forms of empowerment that narrow disparities in property ownership with men, and may enable them to look outside the formal banking system. Women in this category do face barriers to accessing finance. However, many attribute them to general factors shared with male-owned SMEs, rather than to gender-based barriers tied to collateral (e.g., banks cannot reconcile their cash flow with a healthy business). While qualified women-owned businesses in this category likely would make use of MPL, it is thus unclear that this would have an impact different from the impact on non-women-owned businesses.

More research needed

Building the case for MPL as a tool to impact women's access to finance in Colombia requires looking beyond known existing financing gaps and taking a longer-term view. While current market gaps may appear to offer limited opportunity for MPL to significantly affect women's access to finance, MPL has potential to activate latent borrowers, move active borrowers onto more appropriate lending products, and broadly support business growth than can enable women's economic participation, empowerment and access to finance. Moreover, as MPL capabilities progress, there is potential for innovations to reduce transaction costs, enabling MPL to reach smaller enterprise categories with higher concentrations of women business owners.

In certain markets, women are already active MPL consumers. In Jamaica, registry notices are nearly split evenly between sexes. Further research on the range of gender-related factors influencing access to finance and economic participation is critical to fully understand the short- and long- term role that MPL can play in expanding women's and women-owned businesses' access to finance in Colombia. There is a common perception among banks and regulators, including those with a specific mandate to support women, that women have equal access to finance; data broken down by sex on SME-owners' current borrowing habits and property ownership is lacking and would be a significant asset to test these hypotheses. Further analysis

[36] IFC, 2010

around innovative MPL products that could reach the micro-lending sector, such as cash advances at strategic points-of-payment, may also surface potential opportunities.

While recognizing the clear potential of MPL for increasing women's access to finance, catalyzing MPL in Colombia is likely best accomplished by focusing on businesses broadly, both in environments where the immediate demand among women is limited and in cases where there is a clear women-owned business market. Not only can women benefit from gains made by SMEs regardless of ownership, this broadens the size and attractiveness of the MPL market opportunity. Depending on specific institutions' predisposition towards gender, focusing on women as a target entry segment may have value given women's tendencies to have lower default rates and greater customer allegiance.

5.0 NEXT STEPS FOR COLOMBIA

What do these constraints mean? In the aggregate, these constraints diminish the business case for banks to invest in expanding MPL, particularly those banks with the largest market share of existing, traditional lending products and practices.

Catalyzing supply of MPL, particularly among banks, depends on alleviating these constraints. While some represent long-term challenges, such as cultural attitudes towards contracts and lending, others can be addressed in the short to medium term through new or adapted interventions. Still others represent misperceptions that can be effectively addressed through education and awareness.

BUILD AWARENESS

Address outstanding gaps in understanding: While leadership of the banks and financial institutions seemed to be nearly all conscious of the MPL legislation and the potential opportunity it presents at a general level, lack of a more practical understanding of the registry and MPL legislation costs and benefits, as well as how they differ from existing lending practices remains a key barrier. Bank executives interviewed were generally able to articulate the objectives and opening created through the law. However, they demonstrated varied, and often incomplete understanding of the technical elements of the law that could truly change their evaluation of cost, risk and returns.

Many of their concerns over valuation, seizure and liquidation stem from misconceptions of what is necessary for MPL to work under the law and how it differs from traditional banking. For example, they had limited knowledge of the potential for blanket liens (e.g., over inventory or a business's assets – a common tool in mature MPL markets); as well as the process and time to enforcement in case of default. Other notable gaps are around the ways in which the law can help guide risk assessment. While time is inherent to overcoming these knowledge gaps and changing mindsets, they also suggest additional communications and training may be required for the management and executive levels of banks, specifically on common MPL products and benefits.

Training across staff levels: While bank executives may be conscious of MPL, there is significantly less understanding of MPL among customer-facing representatives at financial institutions who are likely best positioned to identify opportunities for MPL. Focusing on educating this category of banking employees could help stimulate bottom-up demand for the product and help drive better understanding of the scale and nature of the market.

PROVE THE MARKET

Expand view of target first movers: Current policies and implementation efforts primarily focus on Colombia's largest banks. In working with banks, MPL implementers should seek to identify target banks equipped and incentivized to be most agile in building capabilities to capture the MPL market. Competitive dynamics and incentive structures in Colombia suggest that second-tier banks or alternative lenders may produce greater returns and should be part of an expanded view of potential first movers that receive support. These are likely to have greater interest in making investments to aggressively grow their customer base, or to have deeper knowledge of specific borrower sectors (which helps overcome asset valuation, maintenance and resale barriers.)

A further approach could be to broker strategic partnerships between traditional banks (which have branch networks, lending expertise and access to financial capital) and business equipment manufacturers and distributors (which know equipment values, maintenance requirements, and resale markets) to develop and promote MPL financing products which can simultaneously grow bank lending business and support increased equipment sales.

Banks commonly cite the desire to "see how MPL is done." Encouraging foreign banks as first movers could be one route, however alternative institutions may be more agile and rapid market leaders. In fact, a range of financial institutions are already beginning to seize on the opportunity of MPL and are testing products that demonstrate the market potential. While continuing to support banks as key allies, MPL advocates and reformers should seek to identify these actors and support this organic market exploration. Categories of institutions may include fintechs, SEDPEs,[37] equipment manufacturers, trusts, etc. This may include setting up programs that act more like venture funds, helping early stage financial service providers expand or scale their offerings.

Capture market data: Little is understood about the borrowing needs and habits of the SME sector. Official statistics paint significantly different pictures of the nature of demand, ranging from assessments that less than 5% (ANIF) to nearly 70% (IFC)[38] are underserved. Few banks capture data about the customers they may lose in the transition from micro, to small, to medium-sized enterprises. There is also little understanding of what products SMEs are using to finance their businesses today, thus eliminating the potential to evaluate the comparative competitiveness of an MPL product.

A comprehensive study, incorporating sex-disaggregated data, would help shed light on the scale and nature of the market opportunity. Key areas research should focus on including: current SME borrowing habits; satisfaction with current credit and drivers; banking relationships; assets and collateral; and gender effects of these.

REDUCE BARRIERS TO ENTRY

Government or donor guarantees: Guarantees are important tools to offset risk and potentially lower costs of entry into new markets. Wisely designed guarantee programs could have a beneficial impact on inducing investment into MPL. However, they can also have distorting effects and can impose costs on government that in the long run may be unsustainable. Thus they should be considered with strategic objectives and these limitations in mind. A structure such as availability of second-loss guarantees for MPL within a specific time window may encourage a potential first mover to enter the MPL space, for example.

Banks interviewed affirmed that a second-loss guarantee could make investing in MPL more attractive, for example by reducing the risks associated with barriers such as valuation and seizure of pledged assets. Under this approach, the government or donors could guarantee to pay a portion of loans in the case of default, if lenders find formal MPL enforcement routes ineffective (or if the market needs time for lenders to hone their enforcement processes). A parallel or alternative effort may seek to review existing unsecured loan guarantee programs to examine how they could be optimized to encourage banks to transition borrowers to MPL and other secured lending products where they can offer a more advantageous option for the borrower and lender. MPL implementers and advocates should undertake an effort to review the effects of current guarantee programs on MPL supply and consider whether a properly structured second-loss guarantee could be applied to jump-start the market.

[37] Specialized Society in Deposits and Electronic Payments, a type of alternative financing institution defined in Colombian law

[38] National Association of Financial Institutions (ANIF), "La Gran Encuesta PYME (2017-II)", 2017, http://www.anif.co/sites/default/files/publicaciones/gepnacional_ii-17.pdf; IFC, 2010

Specialization at the system level: While banks are generally conscious of the need to specialize for MPL to work, a concerted effort led by public and private sector officials to prioritize MPL in certain strategic sectors could help reduce barriers to entry in these target markets. Making a system-level prioritization could help accelerate the development of related and supporting industries (e.g., insurance, valuation) needed to lower barriers to investment. As discussed in detail in the related report on the market for MPL in Colombia, specializing in accounts receivable, equipment financing, or inventory financing[39] – each focused in an industry familiar to the bank concerned – appear to offer the most attractive forms of MPL for initial market entry.

ADAPT REGULATION

Adjust provisioning requirements: Current Colombian regulations require provisioning against collateral at a discount regardless of the loan rating, necessitating focus on valuation. Given the relative weakness of Colombia's valuation industry and banks' concerns over valuation, adjusting the regulations to allow for more flexible provisioning for good standing loans could potentially reduce concerns around collateral valuation as a barrier to entry. While bank regulation should not stray from the rules set out in the Basel Accords, this points to the need for better coordination of secured transactions regulations and regulatory law.

Adjust focus of coordination on growth: While coordination across government can present unique challenges, increased alignment of agencies, programs and policies around the objective of facilitating enterprise growth could highlight opportunities for MPL to improve growth opportunities for SMEs and help remove competing, less efficient products. Effective coordination would require shifts in incentive structures to promote the flow of users between and across different financing products, while supporting institutional agility in decision-making and implementation.

There could also be further alignment between agencies responsible for designing and implementing MPL, and agencies running guarantee programs to support SME access to finance, such as the FNG. Both types of agencies have important roles to play in enabling access to finance, and additional joint efforts to uncover how their programs can work together to ensure financial institutions are incentivized to offer SMEs financial products best aligned with their needs would encourage overall growth.

[39] Note that in certain cases, inventory financing also involves accounts receivable financing as, when inventory is sold, the security interest extends to both new inventory and the receivables generated from the sale of the first-generation inventory. This means that security is increased with the increase of the value of the collateral. This is also true when encumbered equipment is leased, in which case the security interest extends to the equipment but also to the rents,

Global Implications: From Colombia and Beyond

6.0 APPLYING LESSONS LEARNED

The findings and recommendations described in the previous pages of this report reflect Colombia's unique social, economic and historical context. The country's robust micro-finance industry, recent economic challenges and trajectory and experience with governance and conflict, among others, each influence how the country's experience with MPL has played out.

While these factors, among others, warrant caution in drawing direct correlations between the experience of MPL in Colombia and what can be achieved in other countries, we believe that some lessons are broadly applicable. Reflecting on these learnings can help ongoing and future efforts to implement MPL. One of these is that successful implementation of MPL in any given country will be situation-specific, and the introduction of MPL-enabling legislation and a collateral registry should be complemented by a suite of other enabling interventions informed by a holistic assessment of country-specific enablers and barriers. Our research in Colombia provides a guide to the factors which should be emphasized when evaluating which complementary enabling interventions hold most promise for allowing investments in MPL to achieve their potential.

The following recommendations aim to contribute to the understanding of what inputs and approaches can lead to more effective implementation of MPL, in a way that allows countries and economies to most benefit from its use. The list does not aim to be comprehensive, but rather focus in on those factors most relevant and universally applicable based on our findings in Colombia and from our global review of MPL implementation. Each serves to highlight new stakeholders and factors that impact the nature, scale and rate of MPL uptake, to inform interventions moving forward.

APPLY AN ECOSYSTEM APPROACH

MPL reform has traditionally been equated with legal and regulatory reform, along with the establishment of a digital collateral registry. While these pieces are vital, only recently has the concept that MPL depends on a much broader ecosystem begun to gain momentum. The case of Colombia clearly affirms the importance of bringing an ecosystem approach to MPL implementation.

What is an "ecosystem"?
The term ecosystem, when applied outside of the natural sciences, refers to "the complex of entities, their environment, and all their inter-relationships." In the context of MPL, this concept conveys that projects seeking to implement and enable MPL should consider the full financial sector, social and economic

What is an "ecosystem"?
context to which MPL is being introduced, and should be designed to account for the relationships between different aspects of that environment to which MPL is being introduced.

MPL ultimately depends on the development of markets for MPL products and services, which by nature is complex. Those markets include capable borrowers, product suppliers, and underlying enabling factors that range from laws to supporting industries to social norms to physical infrastructure. Adopting an ecosystem approach allows policymakers to understand how these different factors, including human agents, interact with one another and ultimately influence borrower and lender behavior, driving supply and demand.

As described in earlier sections of this paper, a variety of factors influence banks' willingness and ability to offer MPL and the market broadly. Some have a direct influence, such as provisioning requirements; others have an indirect, yet equally as important influence, such as levels of business formalization or social norms related to entrepreneurship that impact the pipeline of demand for MPL. It is important to note the extent to which factors beyond the banking system can influence the market for MPL.

The role of the MPL ecosystem is apparent when one looks at more mature MPL markets. For example, Deloitte's experience in the U.S. shows that banks' ability to provide accounts receivable financing depends on factors ranging from a strong insurance industry; norms around consolidating banking services with one bank; community alert mechanisms; valuation and collections agencies; to an effective legal enforcement system, and so on.

Understanding what factors are important, how they relate to each other, and the collective impact on MPL can inform strategic interventions to encourage MPL uptake, and also help set realistic expectations around scale and rate of impact. Appendix C provides a summary of factors that commonly influence MPL and can provide a starting point for analysis.

The main implications of an "ecosystem" approach for MPL development and implementation are threefold:

- **Baseline understanding:** Understanding the inner workings and relative maturity of the factors that make up an enabling MPL ecosystem provides a useful starting point to design a suite of interventions that can optimize the scale and speed to impact of MPL. Conducting an MPL ecosystem assessment early in a reform project can be a valuable exercise to direct interventions and resources.
- **Resource allocation:** Understanding the role of diverse ecosystem factors ultimately points to the need to allocate resources to support a diverse array of MPL interventions, beyond the traditional focus on legal reform and collateral registries. Institutions financing MPL implementation may need to take a broader view of the types of projects to support, and the scale of resources required for MPL implementation.
- **Collaboration:** Given the diversity of influencing factors and implications for financing, implementing MPL ultimately requires more and continuous collaboration across a broader range of stakeholders than has been practiced in some cases. Beyond coordination across secured lending entities, MPL advocates may find value in partnerships with institutions tackling social challenges such as entrepreneurship, as well as with industry players such as equipment manufacturers, who can help align ecosystem forces and potentially plug resource gaps.

CONTINUOUS EDUCATION AND TRAINING

Outstanding gaps in understanding of MPL nearly half a decade after implementation of legislation enabling MPL affirm the importance of continuous education and professional training. In doing so, trainings should seek not only build the financial sector's technical understanding of the legal system, but also directly confront and challenge traditional mindsets that prevent financial sector leaders from grasping the value of MPL.

Professional training should target employees at different levels within banks and other financial institutions, including not only executives, but also customer service agents and risk officers who are responsible for identifying and approving potential MPL customers. Bank lawyers and judges often have significant influence on banking executives and should be a further priority. This will better equip lending institutions to bring MPL to market.

In developing programs, trainers should recognize the link between banks' abilities to serve entrepreneurs and the potential pipeline of MPL customers. Growth stage SMEs are often prime candidates for MPL given the nature of their asset and investment structures. However, customer service agents and risk officers often lack the understanding to recognize viable borrowers among this group, as such borrowers frequently have erratic or net-negative cash flows even though the underlying businesses are healthy. This can drive growth-stage companies from the formal financing system, cutting away at the demand market for MPL.

ANTICIPATE POLICY CONSEQUENCES AND ADAPT

Laws, policies and regulation are tools to influence behavior and drive outcomes. Depending on the context, similar laws and policies can produce unique behavior, and in some cases, unintended consequences.

Accepted modern legal frameworks for MPL provide an excellent baseline standard for policy reform. However, awareness that different ecosystems will respond to policies in different ways should inform MPL implementation. For example, laws intending to shift risk through requirements on insurance can serve to enforce the health of the MPL system in one country, but ultimately deter activity in another where the insurance sector is relatively weak, or not common practice.

In the case of Colombia, there is some evidence to suggest that standards for loan capital provisioning place added emphasis on valuation of collateral due to discounting requirements for even highly rated credits. This curbs interest in MPL among banks that are already concerned about the cost and feasibility of valuation. While a full assessment is necessary to understand the full implications of adapting this regulation, altering the legislation to lower the threshold for discounting collateral value in provisioning could potentially ease some of the focus on valuation while the sector develops.

Recognizing the potential challenges associated with changing and adapting policy, legislators should aspire to as much agility as possible in adapting regulations and guidelines based on impact, to best catalyze and steer the market for MPL. Implementation should include careful monitoring of policy impact and openness to the need to adapt policies and regulations when justified.

FOCUS ON STRATEGIC FIRST MOVERS

Large, mainstream banks have traditionally been the focus of MPL implementation. Indeed, large banks represent important players given their scale and impact on the financial system, and must be engaged in MPL reform and implementation. At the same time, actors seeking to catalyze an

MPL market may partner with smaller banks or alternative financial institutions to jumpstart the market.

A common barrier to banks' investment in MPL is general comfort with current business margins, the dampening effect of regulation on competition causing a relative apathy towards capturing new customers and market share. This is most common among large banks that hold a significant share of the market, and may also benefit from other informal or formal market protections. These factors thus dilute their propensity to invest in new, particularly perceived complex and risky ventures.

In this climate, smaller banks and a range of other types of financial institutions could present strategic partners to jumpstart, and ultimately prove the market for MPL. In Colombia, fintechs are moving into the MPL market and using the law and registry to develop innovative products. Equipment and vehicle manufacturers and retailers are also active. Other alternative partners could include micro-financing institutions, leasing and factoring companies, as well as trusts and funds.

While focusing on smaller institutions may not directly translate to significant market penetration in the short term, these institutions can play a critical role of testing the system and proving the market, and in serving the needs of specific sectors. These results can help signal the market potential to larger, later-stage movers.

When taking the first steps into MPL implementation and identifying strategic partners, understanding both the structure of competition between banks, as well as within them, is an important first step. Large banks that serve both micro and very small enterprises and large corporations might appear to be an ideal fit for MPL to support customer retention. However, internal business unit structures with separate bottom line metrics can detract from their incentive to build out these products as MPL, in bridging these segments, may be seen cutting into their markets at the margin.

CULTIVATE MPL AS A PRODUCT

While MPL is most commonly differentiated from other forms of secured lending by the type of collateral used, the capabilities and innovation needed to implement MPL are also more complex. Given the nature of the collateral as well as the use cases it serves, MPL requires not only a specific set of capabilities to conduct processes such as valuation and seizure, but also a tailored approach to risk assessment, pricing, customer selection, marketing, client management, and sales, among others.

In Colombia and other markets where MPL is new, many bank managers and executives describe the adopting of MPL as developing the capability to use movable collateral to secure existing loan products, rather than viewing it as its own distinct product category requiring a unique market strategy and operating model. This particularly applies to forms of MPL other than factoring or leasing that are less common in Colombia, focused mainly on using movable collateral to secure lending for working capital. Failure to grasp this distinction limits banks from understanding the full scale of the new market opportunity (essentially to compete with leasing companies with asset-specific loan products) that MPL represents. Moreover, it can result in investments that are either insufficient or misaligned with the types of resources and capabilities that are required for MPL to be successful.

Legislators, regulators and the broader development community focused on MPL can play an important role in cultivating this mindset among financial institutions by incorporating it into advocacy and capability building initiatives, and calling attention to those non-traditional players that are leveraging the potential of MPL in this way. This entails focusing messaging that captures the unique uses and holistic operating models required to deliver MPL that make it distinct from traditional forms of secured lending. Encouraging this mentality not only among executives, but also across all staff levels engaged in offering MPL is moreover imperative.

CAREFUL USE OF INCENTIVE STRUCTURES

As described in the Colombia case, the success of the FNG, as well as USAID's Development Credit Authority (DCA) guarantee programs, in encouraging lenders to broaden access to unsecured/micro-finance lending among MSMEs is evidence of the potentially powerful role that government or donor guarantees can play in encouraging financial institutions to take up new lending products or expand to new customers. Many of the key barriers to catalyzing investment into MPL trace back to the cost and risk profile of the investment. Wisely designed government- or development-funded guarantees for MPL could be an effective tool to shift the risk profile of MPL over a threshold acceptable to banks and other financial institutions.

Although they have utility, government or donor guarantees for MPL also carry several risks. Key among them is the potential to distort financial markets by incentivizing use of MPL over more efficient or appropriate products. Depending on how they are constructed, guarantees can also contribute to dependency on public funding and inhibit banks from developing the strong internal processes required to manage risk independently. In the worst cases, the net outcome of these effects can be to undermine the natural competitive forces that drive efficient distribution of capital and resilience in the financial system.

In the case of Colombia, guarantees for micro-lending enable banks to service a larger share of the market with unsecured lending. While having many social and development benefits, one side effect of this is to weaken the immediate business case for investment in more sophisticated secured lending offerings such as MPL that could position banks to serve other customer segments more efficiently and enable them to operate independently of external government or development support. While existing guarantee programs have had immense benefits in bringing more borrowers into the formal financial system and enabled them to access credit, emerging evidence suggests that these benefits may come at a cost to the broader financial system, and access to finance for other customer segments.

The potential risks and benefits of MPL guarantee programs emphasize the need to develop tailored programs that ultimately work towards financial sector innovation and independence. MPL guarantees should be scoped to work in unison with other programs and policies to encourage lending practices that help move both lenders and individual borrowers off guarantees over time, enabling the redirection of remaining resources to new customers and needs. As previously noted, a second loss guarantee for MPL paid out only after all standard routes for enforcement have been deployed could be an effective model to achieve this outcome.

MPL AND GENDER

As previously discussed in this paper, MPL presents a critical opportunity to broaden women's access to finance, particularly in areas where sex disparities in real estate ownership have limited women's engagement in the credit market. In many cases, simply making the product available will open doors for women along with men.

Beyond an inclusiveness agenda, women can be advantageous target customers for MPL. Global studies, reaffirmed by evidence from Colombia, show that women as a segment tend to have lower default rates, and show greater allegiance to their banks. While some of these effects dissipate in larger enterprises, banks that can capture women customers through MPL have an opportunity to improve the performance and value-per-client of their customer base.

Focusing on women customers requires understanding women as a unique customer segment or set of sub-segments, and intentionally designing products and services to serve their particular needs. In the case of MPL, awareness of the types of financing requirements, the scale, the nature of collateral they have access to and the benefits of competing products is particularly critical to designing competitive products.

In economies where ecosystem factors limit women's business ownership to micro-enterprise predominantly, using MPL to broaden women's access to finance in the short term can present a challenge. In the early stages of MPL implementation, cost per transaction can be a deterrent to using MPL for transactions at the small scale required by most micro-enterprises. In this context, product innovation to reduce transaction costs is critical to making MPL viable for women business owners. In the case of Colombia where most women business owners run micro-enterprises, engaging technology in product innovation to better serve the needs for micro and very small enterprises in a way that complements existing infrastructure for unsecured lending is critical for broadening direct effects on women's access to finance.

Even if product innovations are successful, the full impact of MPL on women's access to finance is likely to materialize over the longer term, through several channels:

- **Enabling entrepreneurial women to scale:** For women that have aspirations to scale their businesses from small, to medium and beyond, MPL creates opportunities to access new and cheaper forms of financing.
- **Activating latent borrowers and entrepreneurs:** In areas where collateral is a key obstacle to accessing finance, MPL can provide incentives for creation and formalization of women-owned businesses.
- **Deeper reach through lower transaction costs:** As MPL systems mature, product and process innovations along with economies of scale can help reduce transaction costs, making MPL increasingly accessible even to very small and micro business owners.
- **Creating economic opportunities for women:** By unlocking new flows of capital to enable growth SMEs broadly, both men and women-owned, MPL creates economic opportunities for women, indirectly improving their positioning to access finance as individuals, or as business owners.

These effects can work together to improve women's overall economic empowerment, by directly enabling them as entrepreneurs, and more broadly increasing their visibility as valuable contributors to the economy.

The extent of this effect depends on systemic factors that determine the ability of women not only to access finance, but also to grow their enterprises. These factors can range from social norms around family roles, to access to education, and so on. Understanding these factors and how MPL interacts with the socioeconomic system is imperative to implementing MPL to encourage women's access to finance.

Sex-disaggregated data is an important input to developing this awareness and product focus. As exhibited in Colombia and in other markets, existing gaps in data limit understanding both market potential and product needs specific to women, inhibiting investment as well as product and policy design. Capturing data on women's specific financing habits, needs and the influence of collateral on both is critical to optimizing MPL as a tool to address gaps in women's access to credit.

In pursuing MPL as a tool to enable women's access to finance, three main factors should guide the approach:

Adopt an ecosystem approach: Effectively reaching women with MPL requires understanding the full "ecosystem" that influences their demand for and ability to access credit, and the attractiveness of MPL products and services relative to alternatives. As described through the Colombia case, this can include factors beyond legislative and governance reforms, ranging from how they are solving their financing needs today (representing products competing with MPL), to social norms that shape the pipeline of SMEs with appropriate financing needs. Realizing the full potential of MPL may require complementary interventions or tailored products that reflect these factors.

Data-informed, context specific complementary interventions are likely needed to achieve the full gender benefits. In countries like Vietnam, where women are highly engaged in the economy and the banking sector is highly competitive, MPL's benefits may emerge with limited need for other gender-related interventions. For many other countries which have invested in MPL-enabling legislation and collateral registries but where female employment and financial inclusion lags, further interventions informed by an assessment of gender financing norms could reap significant benefits. In still other countries which have implemented MPL such as El Salvador and Honduras, society-wide low use of formal financial services and broader security issues suggest that the a longer time horizon for realizing MPL's potential gender benefits is justified.

Build a system that works for SMEs, keeping women in focus: While women may face unique challenges as entrepreneurs and in accessing credit, in many respects the MPL products they require and enabling systems are the same as what will benefit all SMEs generally. Particularly in cases where the immediate pipeline of women-owned SME demand for MPL may be limited, focusing on building an MPL system that works for all SMEs, including women, can not only benefit current borrowers, but provide an "on-ramp" for women to gain in the long run.

This approach does not imply gender-neutrality; rather, as opposed to building a parallel system for women, reformers should apply a gender lens to decisions that guide the focus and delivery of an integrated system. Design choices with particular potential to determine the system's relevance for women include industry and product focus, banks selected as partners for early pilots/implementation, outreach and communications channels, among others. For example, prioritizing industrial equipment-backed financing may have less relevance for women entrepreneurs who are more commonly focused in service industries in many economies.

Understand women as customers: Whether women choose to access MPL will depend on the extent to which MPL products and services meet their needs, and are attractive relative to current product solutions. This requires a shift from thinking of women as beneficiaries, to viewing them as empowered customers that can be activated through strategic marketing, products design, and positioning. With this framing, reaching women requires understanding what motivates them as borrowers and seeking to influence or adapt MPL products and systems to that mindset.

7.0 CONCLUSIONS

MPL offers great promise for expanding access to credit and improving financial sector resilience, leveraging private sector resources and market-driven solutions to drive development. Yet, as global experience has shown, growing a robust MPL system cannot be achieved overnight; it requires both long-term vision and tailored interventions that incorporate global best practices while also responding to the unique dynamics of the individual country's financial system.

Legislators, regulators and local and international development organizations each have an important role to play in supporting the uptake of MPL in a way that enables financial inclusion. Efforts to date focused on legal reform, creating digital registries and creating global standards for MPL have provided a critical foundation for implementation efforts. However, as many practitioners active in the field have increasingly vocalized, this is only a part of the full effort required to catalyze MPL take-up and achieve its full potential benefits.

Comparing the case of Colombia and evidence from other countries at different stages in their development of MPL points to opportunities to revise and build on the approaches commonly deployed today. Understanding the ecosystem required to support MPL, fostering a product mindset, thinking broadly about strategic first movers and responsibly deploying regulatory and market incentives to shift the risk/return profile that lenders associate with MPL are among the key themes highlighted in this paper.

In some cases, these tactics are already being deployed and should be affirmed and reinforced; in others, they represent an addition to the status quo that stakeholders should be agile in reflecting on and embracing. Still in others, resources may be the main barrier to execution, putting it upon project sponsors to recognize and adapt to shifting awareness of what it takes to catalyze an MPL ecosystem. In each case however, whether MPL implementation has been underway for a decade or is just starting, reflecting on how these learnings can help improve and accelerate outcomes is a key step towards enhancing the long-term benefits for MPL.

At its core, MPL should be viewed not just as a tool for credit or access to finance, but as one element of a deeper financial system that supports broad-based, resilient economic development. While SMEs and particularly women business-owners have strong potential to benefit from MPL, the effects of MPL can touch all members of society. Like all parts of a dynamic financial ecosystem, it is at once a product of and an input to resilient and inclusive societies and thus must become a standard element of the development community's toolkit.

QUESTIONS FOR FURTHER RESEARCH

The findings in this paper do not represent a comprehensive prescription for how to make MPL work. Indeed, the case of Colombia and others points to both the need to further contextualize and adapt MPL interventions to individual countries' financial ecosystems, and to a number of areas of where further research could enhance our understanding of how to realize the development benefits of MPL. Key areas for further research include:

On the finance seekers (demand) side:

- **Financing habits and gaps of SMEs:** Globally, we face a critical deficit in country-level data and information on SME financing trends and needs. Efforts to explore these topics outside the formal financial system in a way that captures trends in the unbanked and informal sectors, and among banked businesses which also access finance through channels other than formal lending institutions are critical. An understanding of how needs and sources of finance evolve through the lifecycle of SMEs, to better inform potential roles and opportunities for MPL, would also add to the MPL development community's understanding.

- **Financial inclusion gaps of women and financially disadvantaged minority groups:** Information on how women-owned businesses access finance, their product needs, specific relationships with collateral, and the explicit and implicit barriers to accessing finance that they face, is similarly sparse and would enable better targeting of products to serve women business owners. Similar knowledge gaps and considerations apply to other financially disadvantaged groups, such as indigenous peoples and remote rural communities.

- **Applications for MPL in micro-finance:** When people reflect on the potential for MPL, particularly to address gaps in women's access to finance, they commonly picture a woman who owns a micro-business who may have no more than a few sewing machines as collateral, but who aspires for growth and a need for financing to realize that ambition. Yet today, transaction costs generally limit applications for MPL to SMEs and large enterprises with more substantial financing needs. Moreover, there remains a debate on whether any form of secured lending should be prioritized over unsecured lending for these customer segments. Further research into to whether and how MPL can be an effective tool to address financing needs of micro-enterprises at the base of the pyramid can help inform future investments.

On the finance providers (supply) side:

- **Impact of government or donor guarantees:** While this paper ultimately supports the potential of wisely crafted guarantees to open new channels for underserved populations to access finance, more research is required on the net impact of guarantee programs on overall financial sector performance. Research to explore best practices in ensuring guarantees can minimize market distortions and encourage long-term financial sector sustainability and enterprise growth will be particularly important to informing how guarantees can be best deployed in support of inclusive finance in general, and MPL in particular.

- **Impact of banking industry structure and regulation:** Our research in Colombia points to the strong influence that institutional structure, industry competition and regulation has on the banking sector's ability and appetite to invest in new products such as those enabled by MPL. Deeper research into this topic, within individual countries and across countries with differing conditions and experiences would add significantly to our understanding of under what circumstances a banking sector will and will not enthusiastically adopt MPL.

- **Non-bank financial institutions:** Our research has shown the willingness of non-bank financial institutions to experiment in the use of MPL to serve finance-seeking businesses. Further study of the potential for these actors to adopt MPL and help achieve its social and developmental benefits is warranted.

Additional holistic country studies:

- Our research in Colombia has highlighted how the outcome of the same essential elements of MPL – enabling legislation, a movable collateral registry, and a consortium of sponsoring institutions – depends on the specific enabling conditions and financial ecosystem to which those elements are introduced. Understanding the interplay between other parallel legislation and legal reforms (e.g., insolvency law) can also be better understood. Additional country-level studies of the experience, barriers and enablers of MPL can greatly amplify the knowledge generated. Ultimately, we should seek an understanding of what patterns of enabling conditions and combinations of interventions are likely to support a range of positive MPL outcomes. A generalized approach to assessing baseline conditions and shaping successful MPL implementation programs seems achievable with sufficient underlying research.

IN CONCLUSION

This study has surveyed the lessons and impacts of efforts to implement MPL in countries around the global and has deeply examined the experience with MPL of one country – Colombia – as a rigorous case example. We have affirmed that implementation of MPL is an essential and beneficial element to deepening a country's financial sector, with consequent benefits for financial resilience, inclusion and economic growth.

We have also found that the pace and extent with which those MPL benefits can be realized depends on the complex interplay of several contextual dependencies, including existing cultural norms related to lending, asset ownership and access to finance; and other aspects of banking regulation and financial industry structure. While more research is needed in several of these areas, many of these variables can be influenced by already proven development and regulatory interventions. Thus, the promise of accelerated MPL uptake is achievable.

APPENDIX A: PHASE 1 OVERVIEW

In October 2017, USAID's Department of Gender and Development (GenDev), Deloitte, and Banyan Global began conducting research on the intersection of MPL and women's access to finance, with a goal to identify investment opportunities that would enable target countries to achieve tangible short- and medium-term milestones in MPL implementation that would translate into new credit opportunities for women-owned SMEs.

As part of this first phase, our team identified a number of countries on the cusp of change with respect to MPL. Countries were initially filtered on the basis of possessing the core MPL legislation necessary to supply lending. Core MPL legislation is comprised of:

- **Modern legal secured transactions law** regulating all security interests
- **Single digital collateral registry** for all interests that allows easy tracing and confirmation of asset ownership, including movable property

This filter provided a wide selection of countries across geographies, including Latin America and the Caribbean, Central and Southeast Asia, Western Europe, Middle East and Northern Africa, and southern Africa. From this subset, our team prioritized countries based on a high-level assessment of their performance across the following enabling factors and their corresponding indicators:

Enabling Factors	Sample Research Indicators	Sources
MPL readiness	• Evidence of government effectiveness and stability • Engagement on women's financial inclusion and/or MPL issues by international organizations, corporations, foundations, etc. • Relevant regulations around microfinance and alternative finance	• Desk research • GenDev insights • Expert interviews (USAID, IFC, World Bank, Women's World Banking)
USAID priorities	• Mission activities and resources	
Macroeconomic factors	• Contribution of MSMEs to GDP • Size of commercial sector and growth trends • Women's workforce participation	

As an output of the above framework exercise, the countries were sorted into three groupings based on their enabling factors:

- **Ecosystem Support –** Reformed legal framework and registry in place, but system requires refining and development of MPL ecosystem
- **System Organization and Implementation –** Modern system and registry in process or recently completed, but support required to implement
- **Fundamentals Development** – Large gaps in modern legal framework and supporting institutions need to be filled

The majority of countries pursued in our research were represented by the Ecosystem Support group, wherein a legal framework and registry lacked supporting infrastructure within government and/or civil society to catalyze MPL as a viable product for potential borrowers. Moreover, in many Ecosystem Support countries, potential borrowers did not have the financial literacy required to access MPL from lenders.

Within the commercial sector, private banks demonstrated limited engagement with MPL due to the lack of a perceived business case for providing MPL products. Micro, small and medium-sized enterprises (MSMEs) continue to face difficulties accessing commercial lending as borrowers because they frequently possess limited fixed collateral and have limited capacity to access MPL through banks. Our findings also revealed that some countries with active collateral registries primarily have vehicles in their records rather than present and future goods, equipment, and livestock, which limits potential commercial activity based on MPL.

Financial inclusion and women's entrepreneurship also remain a challenge in most Ecosystem Support countries, and MPL-driven interventions will likely require enabling MSMEs to access lending on a wider scale in order to open a path for women to engage in the sector as business owners.

From these initial findings, Colombia presented an ideal case study to explore supply-side barriers that have led to banks' slow uptake of MPL among commercial banks. Within the Ecosystem Support group, Colombia has enacted one of the more robust packages of secured transactions reforms. However, their collateral registry is primarily comprised of vehicles and commercial banks have not widely adopted MPL products, suggesting an underdeveloped business case for MPL in the private sector.

Despite the limited uptake of MPL, microfinance is already in the advanced stages in Colombia, implying a healthy appetite for alternative finance. Bridging the gap between microfinance and MPL in Colombia requires additional research, as there is limited understanding of the broader SME market and the perspective of banks that could provide MPL as products to the population.

Our team identified Colombia as an opportunity to model MPL solutions for neighboring countries in Central and Latin America once the business case for commercial banks to provide MPL was developed. The Colombia project's key objectives were scoped to first determine if there is a business case for banks to invest in MPL through domestic industry research and then articulate it to key relevant stakeholders if identified.

The project was also scoped to focus on the broader MSME sector as potential borrowers rather than solely women. Desk research and conversations with country experts revealed that women's prevailing limited commercial access would likely not be directly impacted by private sector adoption of MPL without wider enabling of the MSME sector. Additionally, although there was initial evidence that enabling the MSME market could facilitate women's participation in the commercial sector more broadly, female entrepreneurship, women's commercial access, and the wider MSME sector in Colombia have been historically under-researched, Our project thus presented the opportunity to establish a more refined understanding of Colombia's MSME sector as potential borrowers of MPL in order to identify a broad-based business case for MPL that could significantly expand access to finance for MSMEs in the short to medium-term and ultimately improve women's access to finance in the medium to long-term.

APPENDIX B: INTERVIEWS & CONTRIBUTORS

This paper draws on interviews and other contributions from the following individuals and institutions in Colombia:

Traditional Financial Institutions

Bancamia

Banco Agrario

Banco Mundo Mujer

Banco W

Bancolombia

BBVA

Davivienda

Fundacion de la Mujer

Procredit

Alternative Financial Institutions

Aflore

Aktiva

COMFAMA

Heritage Capital

Interactuar

Mesfix

Sempli

Government Agencies

ACOPI Bogotá

Asobancaria

Asomicrofinanzas

Banca de las Opportunidades

Confecámaras

Fondo Nacional de Garantias

iNNPULSA

Ministry of Commerce

National Registry of Valuation Experts (RNA)

PTP – Programa de Transformación Productiva

Superintendencia Financiera de Colombia

URF – Unidad de Regulación Financiera

Industry and Businesses

Alpina

Bolsa Mercantil de Colombia

Café de la Huerta – Guasca

Carmen Ceraje

Dosakin

Fede Cacao

La Migueria

Obleas Michelle

Pelanas

Termiexpress

Development Stakeholders

Endeavor

Fundación Capital

IFC

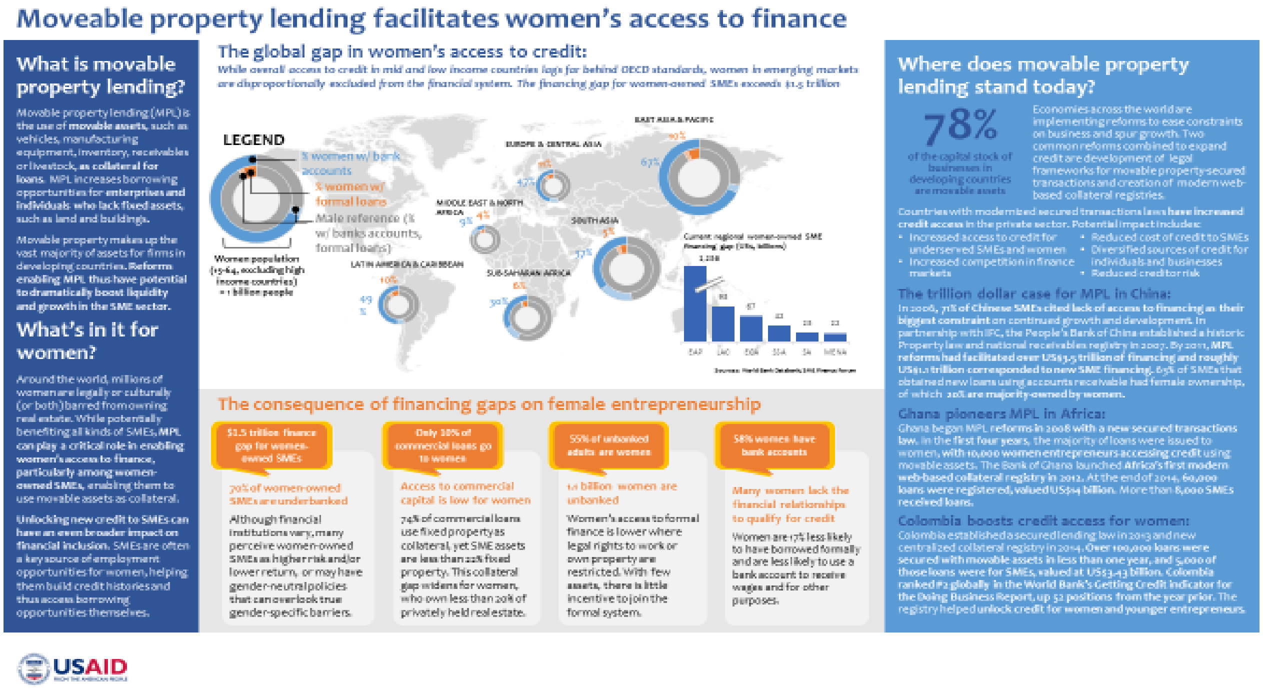
Impact Hub

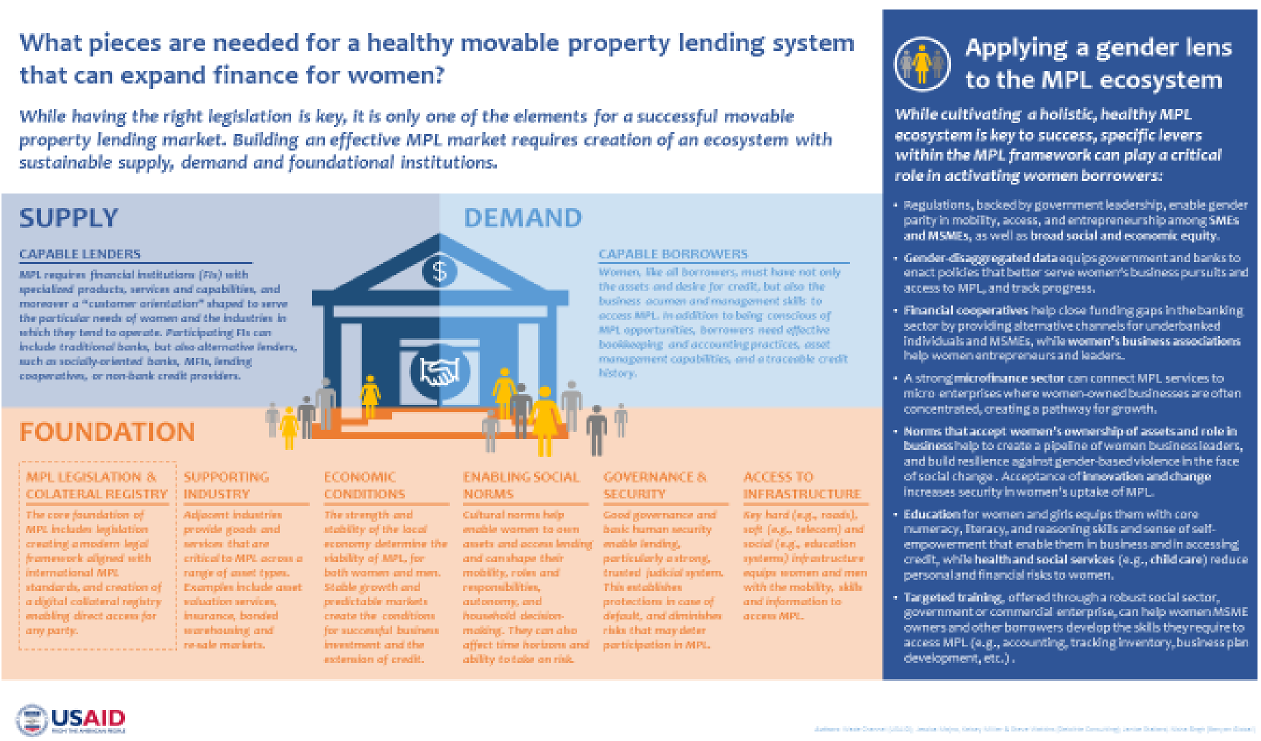
Marulanda & Consultores

Mastercard CIG

USAID

APPENDIX C: MPL & WOMEN'S ACCESS TO FINANCE - INFOGRAPHIC





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