



Exit Strategy For SMEs – Macro-economic Relevance and Challenges

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PRESENTATION OUTLINE

1. SMEs: Macro-Economic Relevance

2. SME Exit Strategies: Importance & Challenges

3. Preliminary Observations

SMEs: Macro-Economic Relevance

Evolving Role of SMEs

View on SMEs changed over time

- disadvantaged sector to growth sector
- shift in policy approach and regulatory structure

Two types of SME markets

- *Vibrant*: short-lived, innovative, aiming to attract investment and grow, easy exit → critical for labor absorption & growth
- *Inert*: long-lived, static, inability to grow because bureaucratic-legal obstacles, difficult exit → kills jobs and structural productivity deficit

Economic Importance of SMEs

SMEs	EU	Japan	Latin America	India
Company market share	99.8%	99.7%	99%	95%*
Labor market share	67%	69%	67%	40%
GDP share	60%	55%	30%	17%

(of industrial units)*

SMEs in the Crisis Context

European Financial Crisis

- Household debt crisis- Unlike Latin American & Russian sovereign debt crises, or Asian corporate debt crisis

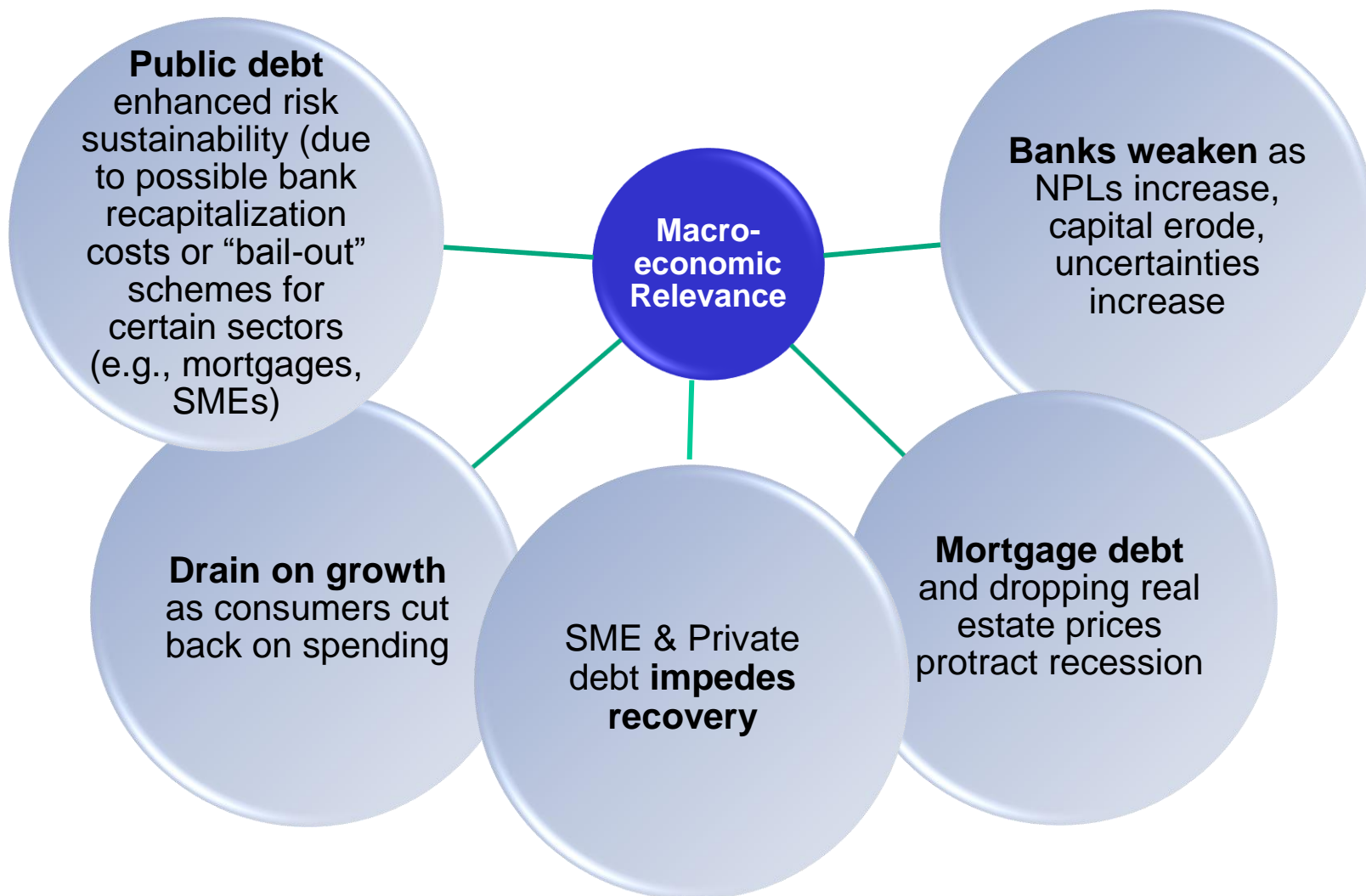
SMEs particularly exposed

- Examples: *(2009 figures)*
- Finland: 17% SMEs declared solvency problems
- Italy & Spain: 25% increase of insolvency filings
- Ireland: SMEs created 172,000 jobs 2000-7

Current crisis highlights SME's vulnerabilities

- Drop in revenue as business declines & late payments
- Income deterioration and personal wealth reduction
- Reduced access to credit as banks tighten lending
- Lack of effective rehabilitation due to weak legal/regulatory framework

Why Does the IMF Care About SMEs?



SME Exit Strategies: Importance & Challenges

SMEs – Building Blocks

Market Entry: Encourage entrepreneurship

- Low bureaucratic thresholds
- Low cost
- Short time

Foster Growth: Access to credit & business continuity

- Ease in licensing
- Access to credit
- Fiscal facilities

Market Exit: Critical to Efficient & Entrepreneurial Market

- Sustains entrepreneurial capital
- Encourages innovation and risk taking
- Aims at business continuity

Key Challenges to SME Exit

Definitional issues

- No special legal framework due to different definitions of SMEs

Access to credit constraints

- common restructuring regimes depend on new credit, which SMEs typically do not have access to

Fiscal constraints

- Lack of adequate tax incentives for distressed SMEs

Constraints on Early Rescue

- Lack of robust insolvency framework to support fresh start for entrepreneurs or early rescue for viable SMEs

Special Guarantee Regime

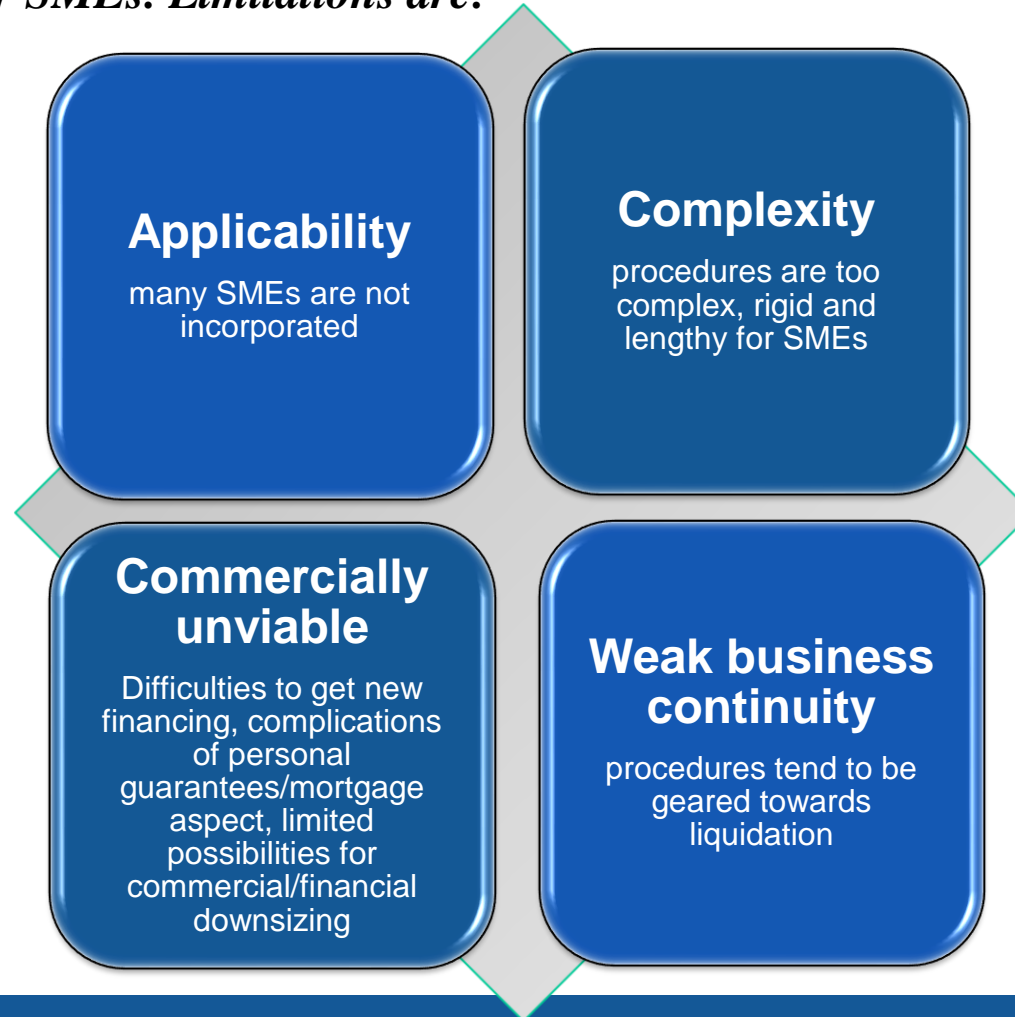
- SMEs typically secure business ventures with personal guarantees and mortgages; business and personal assets are mixed

Social & Political Considerations

- Social and political considerations impact exit strategy for SMEs

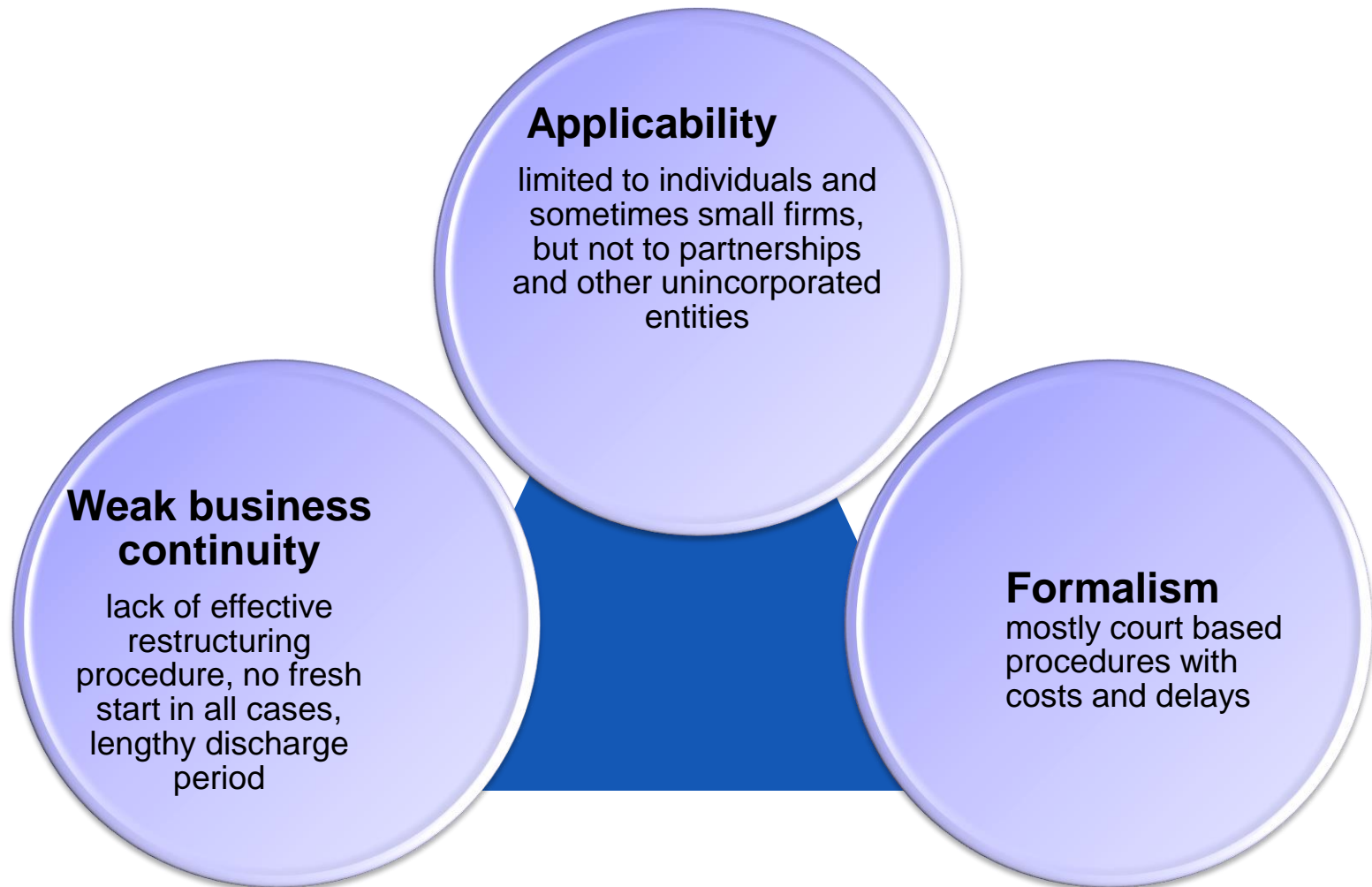
SMEs Corporate Insolvency Procedure

UNCITRAL Guide has provided useful guidance that can be further developed and tailored for SMEs. Limitations are:



SME: Personal Insolvency Procedure

No International Best Practices exist, but cross-country experience provides guidance.



SMEs: Out-of-Court Regime

INSOL Principles

- May be selectively applied to SMEs

Availability

- Special out-of-court regimes for SMEs are not widely available, however, some countries do have them (e.g., India).
- Where they do exist, they tend to be ineffective (e.g., lack of incentives).

Recent Developments

- Some countries recently adopted special out-of-court regimes for SMEs (e.g., Spain and Portugal)
- Their effectiveness remains untested.

Special Regimes for SMEs

Spain (9/2013) – Out-of-Court Procedures

Access limited to individual entrepreneurs and legal entities with fewer than 50 creditors and liabilities below €5m

Enforcement actions stayed up to 3 months (excluding secured or public creditors)

Mediator appointed by the Commercial Registrar

Payment plan with a mandatory cap of not more than 25% on haircut and deferral of 3 years

Approval by creditors of 60% in value

Not affect secured or public creditors

Special Regimes for SMEs

Portugal (2012) – Out of Court Procedures

SIREVE targeted at SMEs

Facilitated by IAPMEI, a mediation entity associated with MoE

Tax and social security authorities required to participate in the negotiations

Standstill applicable to creditors participating in the SIREVE

No cram down

Preliminary Observations

Preliminary Observations

Increasing Importance

- Account for a large share of the economy
- Macro-economically critical
- Ineffective current legal regime for market exit
- Need a targeted insolvency regime to help preserve SMEs

Tailored Legal Regime

- Simplified procedures
- Speedy process
- Lower costs
- Fresh start for individual entrepreneurs
- Early rescue of viable SMEs
- Out-of-Court procedures

Supporting Factors

- Efficient exit needs support of other laws (e.g., tax incentives)
- Provide for additional financing (e.g., from government)
- Raise awareness and make available information
- Need efficient institutional framework (mediation, arbitration, insolvency administrators, court system)

Thank You!