Financing for Rural Micro and Small Enterprises in China
New Developments and Opportunities
Acknowledgments

This Executive Summary summarizes the key findings from a joint study by the China Inclusive Finance Research Institute and the United Nations Development Programme (UNDP). For detailed information, please download the full report in Chinese. The study is an important output of the “Leveraging Sustainable Finance, Accelerating Rural Revitalization” Project, a joint collaboration between the UNDP, the China International Center for Economic and Technical Exchanges (CICETE), and Du Xiaoman.


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The core commitment of the United Nations 2030 Agenda for Sustainable Development is to “leave no one behind”, advocating for the support and protection of vulnerable people. As a primary engine of employment and income for the vast rural population in China, micro and small-sized enterprises (MSEs) play a crucial role in improving rural livelihoods. When adequately supported, rural MSEs therefore also play a pivotal part in achieving the Sustainable Development Goals (SDGs) to end poverty and protect the planet by 2030, as well as reinforcing China’s rural revitalization strategy.

As of 2023, China reported a rural population, of around 480 million people\(^1\) - exceeding the entire United States’ population\(^2\). Empirical evidence presented in this study shows that around three quarters of rural participants in an online survey conducted in mid-2023 reported engaging in entrepreneurial activities, highlighting the importance of rural MSEs in socio-economic development. Born from traditional small-scale farming, rural MSEs continue to retain characteristics of family enterprises. They often embark in parallel businesses to maximize resource utilization, as well as boost incomes. Our survey has found that nearly thirty percent of MSEs now engage in such parallel businesses, facilitated by digitalization. The digital economy’s expansion has also had two other positive effects on rural MSEs. Firstly, by integrating technology and machinery into every production stage, smallholder agricultural production has modernized. Secondly, digitalization has increased their value chain integration and market access. Policy innovation facilitating land transfers across individuals and households has also helped to aggregate farmable land, encouraging larger-scale farming.

While digitization is promoting rural MSEs’ innovation and development, it also amplifies existing challenges. For example, structural barriers to MSE financing are blocking adequate investment in rural digital infrastructure. This, along with a shortage of rural technology talent and capabilities, has created a “digital divide,” putting rural MSEs at a disadvantage versus urban competitors and leaving them at risk of being pushed out of the market. The most immediate challenge

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\(^1\) China’s National Bureau of Statistics, 2nd Feb 2024; Statistical Communique of the People’s Republic of China on the 2023 National Economic and Social Development. Available at: https://www.stats.gov.cn/english/PressRelease/202402/20240228_1947918.html

\(^2\) Worldometer, Countries in the World by Population (2024). Available at: https://www.worldometers.info/world-population/population-by-country/

* Based on data by the United Nations, Department of Economic and Social Affairs, Population Division. World Population Prospects: The 2022 Revision.
for rural MSEs is an aging rural labor force, as declining birth rates and the departure of young and middle-aged rural laborers migrating for off-farm work is severely impacting the rural workforce composition. The local workforce is often older and less educated, making it harder to improve productivity. These difficulties are exacerbated by the need to transition to a green development model, in line with the country’s dual carbon goals, of peaking carbon emissions before 2030 and reaching carbon neutrality before 2060, along with a less buoyant macroeconomic backdrop, impacting price competitiveness. Addressing these challenges while improving MSEs’ access to finance is urgently needed, so they can participate fully in the digital and green transformation. This would enable rural MSEs to better contribute to China’s “high-quality development” vision, as well as the SDGs. To facilitate the latter, the government has been working to promote the accessibility, coverage and adequacy of financial services for rural MSEs, through a series of national strategic policies. These include the “Rural Revitalization Strategic Plan (2018-2022)”, the “Plan for Advancing the Development of Financial Inclusion (2016-2020)”, and the “Implementation Opinions on Promoting High-Quality Development of Inclusive Finance”.

Against this backdrop, our study, jointly conducted by UNDP and the Chinese Academy of Financial Inclusion (CAFI), maps the financial demand and supply of rural MSEs, with a focus on digitization. Through evidence-based analysis, it presents the challenges and opportunities rural MSEs face, along with recommendations for their sustainable development in China.

Here, we summarize key highlights from this report, titled Financing for Rural Micro and Small Enterprises (MSEs) in China: New Developments and Opportunities.

**Evolving financial requirements of rural MSEs.** Influenced by factors such as crop production cycles, traditional rural MSE financing is typically characterized by short-term and frequent loans of relatively modest funding amounts, with relatively short lead-times for capital deployment. However, as rural MSEs engage in parallel businesses, with larger operations, along with greater integration into value chains and digital technology application, their financial demands evolve, with the following characteristics emerging.
Firstly, parallel business operations call for loans targeting different purposes. Usually related to the extent of the MSEs' diversified activities. In July 2023, a joint survey conducted by CAFI and Zhejiang E-Commerce Bank Co., Ltd. (MYBank) found that 41.4 percent of loan customers from rural MSEs required loans for more than two purposes. These included financing demands for both production and livelihoods purposes, including consumption. As a result, many loans taken by rural MSEs are “mixed” loans, that cannot be distinctly identified for a specific usage.

Secondly, expanding production scales are increasing MSEs’ demand for loans. The aforementioned survey also found that 48.8 percent of rural MSEs required financing through loans, with 38.3 percent demanding medium-term loans and 61.7 percent requiring short-term transfer loans. Such growth signifies a transition towards capital-intensive operations. The increasing scale of financing demands primarily stems from factors such as leasing land, acquiring production equipment and hiring employees, etc., all of which require more capital investment.

Thirdly, rural MSEs are demanding insurance to mitigate risks. Throughout their operations, rural MSEs encounter risks inherent to their production and business activities, as well as external risks arising from market dynamics and climate change. As a result, insurance is necessary to reduce potential losses resulting from these risks.

Fourthly, digital and green transformations have given rise to new financial demands among rural MSEs. In the context of digital transformation, rural MSEs require additional funds for equipment upgrades. Meanwhile, agricultural MSEs also need capital and green financial tools to fulfill the requirements of environmentally sustainable practices in their production and operations.
The rural financial system is adapting. Thanks to the development of fintech, financial institutions are increasingly overcoming limitations, continuously innovating financial products and improving their service quality. Credit systems have been particularly effective in fulfilling demand for small-scale loans. Digitization has also created new opportunities for small and decentralized rural insurance services.

1. **Financial services have become more accessible for rural MSEs.**

   A continuously improved credit information system has enhanced the availability of commercial and public data. As a result, financial institutions have innovated financial products to better meet the demands of rural MSEs. Specifically for women's business and entrepreneurship, there are also policy-based, commercial, and philanthropic credit products available. In addition, financial institutions aim at providing capacity building to enhance women technical skills. Currently, financial demands of rural MSEs for smaller amounts, short-term or urgent needs are basically being met. However, rural MSEs still face challenges in finding financial products that meet their long-term and large-scale funding needs, especially when collateral or guarantees are required, with financial institutions often failing to provide suitable options.

2. **Supply chain development has increased financing opportunities for MSEs.**

   As rural MSEs become more integrated into industrial chains, financial institutions have explored diversified financial products relating to their supply chains. These enterprises can leverage their cooperation with leading enterprises to obtain guarantees, thereby enhancing opportunities to obtain loans from financial institutions. Furthermore, rural MSEs, which have transactions with leading enterprises and become part of the supply chain can access internal financing established by such leading enterprises. Supply chain financing is increasingly becoming an effective approach in diversifying the financing sources for rural MSEs.

3. **Insurance products for rural MSEs have developed rapidly**

   accompanied by increased agricultural insurance types. This enhances insurers' capacities to share risks, while increasing collaboration between insurance institutions and other entities. With government support, particularly direct subsidies, the scale of agricultural insurance has rapidly expanded. However, a gap remains between existing insurance types and demands of MSEs. For example, the government-subsidized agricultural insurance can only cover partial risk losses of these enterprises.

4. **Financial institutions have engaged in capacity-building initiatives for rural MSEs**

   encompassing training in production and operational skills, as well as financial capabilities. These have greatly improved the comprehensive capabilities of rural MSEs, enabling them to develop better and to cultivate more potential high-quality corporate clients.
The government has also made significant efforts to improve financial services in rural areas.

In 2017, China put forward the “Rural Revitalization” strategy, outlining a comprehensive plan to develop rural areas and sectors, including the agricultural industry centered around rural MSEs. To enhance the accessibility of financing for rural MSEs, the government has implemented numerous measures to improve the service environment of financial institutions, including:

- Introducing supportive policies, including fiscal policies related to interest rates, subsidies and risk compensation, as well as monetary policies concerning special loans and refinancing for MSEs. This improves the MSE financing environment, in terms of both capital supply and demand;

- Establishing a government digital credit information platform, to alleviate information asymmetry during financing for rural MSEs;

- Creating a financing guarantee system with government support, providing measures to share risks and enhance credit for MSEs during financing; as well as;

- Establishing a rural property transaction platform to revitalize rural assets, enhance asset liquidity and provide more qualified collateral options for MSEs seeking financing.

However, difficulties in securing financing for rural MSEs persist. Although China’s rural financial system has already made significant progress in supporting MSE financing, and the path for promoting financial development through digitalization has become clearer, challenges remain.
Firstly, it is difficult for rural MSEs seeking expansion to obtain financing beyond their credit limits

On the back of limited collateral and access to guarantees, as well as limited ability to conform with banks’ mortgage requirements. Consequently, they struggle to meet the financing demands of credit loans, and they also face challenges in obtaining other loans from banks.

Secondly, the quality of rural credit information systems varies

due to inconsistent data availability. Rural credit information systems are constrained due to inadequate MSE coverage, uneven data quality across different regions and relatively inefficient data-sharing.

Thirdly, the value creation capability of data assets should be improved.

Rural MSEs have limited capacity for digital transformation, digital management and value creation, reducing the willingness of financial institutions to provide loans.

Fourthly, the mismatch between supply and demand of agricultural insurance services remains prominent.

At present, agricultural insurance can only cover some rural MSE risks: existing agricultural insurance products cannot meet the many different demands of rural MSEs.

Finally, policy implementation hurdles persist.

For example, policies and measures supporting rural MSEs lack coordination, limiting their effectiveness. Most of them focus on small financing demands, leaving demand for larger scale financing untapped. Finally, a larger role of market-oriented measures may reduce distortions and improve returns.
Against this backdrop, our report provides the following recommendations to the government and financial institutions to support rural MSEs financing and thus their sustainable development:

**For the government:**

▲ **Increase the government’s role in guarantees and risk compensation**, expanding fiscal support for guaranteed funds and increasing policy-based guarantees for larger loan demands from rural MSEs.

▲ **Form and implement different policies and regulations** to guide development of a sustainable finance ecosystem for rural MSEs, while encouraging financial institutions of different scales to provide specialized and differentiated services for rural MSEs.

▲ **Accelerate improvement of rural credit information systems**, strengthening functions of the digital credit platform by the government and enhancing national data governance capacity.

▲ **Improve rural property rights transfer infrastructure**, by continuing to establish and improve a rural property rights transfer trading platform, strengthening its transaction management mechanism and exploring rural property rights mortgage innovation.

**For financial institutions:**

▲ **Give play to the specialization of different financial institutions:** Banks, insurance institutions and other financial organizations should provide differentiated services for rural MSEs, based on their respective advantages.

▲ **Improve the overall financial and market resilience of rural MSEs**, by helping rural MSEs to build up their capabilities through specialized courses, as well as improve their financial literacy, operating capabilities and digital transformation.

▲ **Explore the role of insurance in the development of rural MSEs**, by enhancing risk guarantee levels of various insurance products, as well as promoting the combination of insurance products and other financial products to jointly serve enterprises.

▲ **Promote financial institutions’ digitization**, by increasing fintech investments, while consolidating and expanding applications of digital technologies in financial services.

In conclusion, rural MSEs play a critical role in efforts to achieve sustainable development for all in China. They are evolving for the 21st century through digitization, boosting parallel businesses, production and business models, along market access. However, their challenges are also expanding, particularly in obtaining adequate financing and insurance, deepening the digital divide. For MSEs to fulfill their great potential for sustainable development, further support is urgently needed from policymakers and financial institutions to overcome these difficulties. This should focus on increasing sustainable finance, rural credit and property transfer tools, risk management and insurance, along with enhancing rural MSE business capacities, including in digitization. Such steps are vital to ensuring a thriving rural economy of tomorrow, leaving no one behind.