



**SUPPORTING SMALL BUSINESSES
IN DEVELOPING COUNTRIES:
WHICH PROGRAMMES WORK
AND WHY?**





Cover photo: Workers at Soppexcca's coffee processing plant, Matagalpa, Nicaragua.
Christian Aid/Les Stone

Photo: Members of Bairunyi Bee Keepers Association refining raw honey, Embu County, Kenya.
Christian Aid/Matthew Gonzalez-Noda

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FOREWORD

The role of the private sector has never been more central to debates on development and poverty eradication. Governments, donors and civil society are all looking to the private sector to play a crucial part in the realisation of the Sustainable Development Goals (SDGs).

Much of the discussion focuses on the role of larger, often transnational, corporations in stimulating growth and creating employment. Many NGOs tend to centre their programmatic efforts around working with micro enterprises. However, this report focuses on Small to Medium Enterprises (SMEs), often regarded as the 'missing middle', and seeks to understand how best to harness the potential of these enterprises in improving the livelihoods of millions of people - in particular women - in the developing world. SMEs traditionally supply the majority of jobs in developed countries, so the potential for job creation in developing countries is equally large.

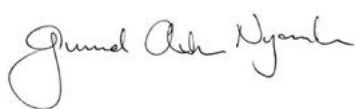
As organisations with a long history of working across the developing world, we understand that there is no one solution to the complex problems facing countries and communities. This research was not undertaken with a view to asserting that the answer to development problems lies solely through working with SMEs and ignoring the importance of other actors. Rather, it is an attempt to understand more clearly this one element of the private sector and how we, as development agencies as well as donors, governments and larger private sector actors, can best work with it.

The agencies that have collaborated on this research are mandated to work on relief, development and advocacy for poverty eradication. Our work is founded on Christian faith, inspired by hope and acts to change the world. We work globally for profound change that eradicates the causes of poverty, striving to achieve equality, dignity and freedom for all, regardless of faith or nationality. With its mix of case studies and reviews of research we hope the report will stimulate debate, collaboration and, above all, action!



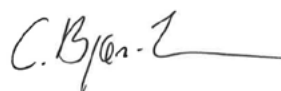
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SUMMARY

This study examines how governments and donors can better promote ‘business enabling environments’ so that small and medium-sized enterprises (SMEs) can contribute to inclusive economic development in developing countries. It focuses on ‘what works’ and contains a review of literature on SME support plus three case studies from our experience as NGOs. It is hoped that the study will inform decision making to ensure policies focus on what SMEs really need.

Despite substantial literature on business development, remarkably little is known about which SME support programmes work and why. There is significant funding of SME support programmes by multilateral development banks, international financial institutions, bilateral donors and governments. However, much of this support is focused on two areas: providing financial loans to SMEs, and advocating general reforms to the investment climate, which mainly benefit larger enterprises, including multinational companies, rather than SMEs. Other support programmes are often neglected.¹ This study challenges these approaches and suggests alternative support policies.

This review focuses on **SMEs**, not micro-enterprises (sole traders with only a few employees). SMEs are regarded here as businesses with 10-100 employees (small) and 101-250 employees (medium). The nature of SMEs varies greatly, ranging from small manufacturers – for example, of furniture, metal parts, clothing or machinery – to service providers, such as restaurants, consulting and computer software firms. They include rural, as well as urban, businesses, notably farmer cooperatives and producer organisations, often involving smallholder farmers.

Three main areas make up the **business enabling environment**:²

- The formal rules, laws and regulations that governments, at all levels, impose on workers, markets and private businesses, such as tax legislation, property rights, employment law, labour rights and trade rules.
- The informal behaviour, customs and norms that determine business conduct and shape how markets work – and where governments can only have an indirect impact.
- Public investment in infrastructure and provision of public goods and services by the government, such as health and education provision, transport and water management.

THE IMPORTANCE OF SMEs

SMEs are critical to promoting inclusive economic development and poverty reduction. They constitute a **vast number of businesses and employ a large number of people** in developing countries. It is estimated that there are approximately 400 million SMEs (defined as those with up to 250 employees) in low- and middle-income countries,³ which account for around 60% of GDP in low-income countries.⁴ The UK's Department for International Development (DFID) notes that SMEs (again, with up to 250 people) employ an average of 66% of the permanent, full-time workforce in developing countries.⁵

There are 8-10 million formal **SMEs owned by women** in developing countries, which represents roughly a third of all formal SMEs (with up to 250 employees).⁶ Thus, supporting women-led SMEs is critical to promoting inclusive economic development. However, as a World Bank evaluation notes, relatively little SME assistance has focused on women.⁷

SMEs are also vital to inclusive economic development since they can provide **basic goods and essential services** to poor and excluded people. They frequently produce light consumer goods – such as food, clothes and wood products – to meet household demand. The UN's Economic Commission for Latin America and the Caribbean notes that promoting SMEs is 'a cornerstone for achieving greater social equality'.⁸ **Job creation** is key to economic development and some studies suggest that enterprises with fewer than 100 employees, and young enterprises (those less than two years old), have the highest job creation rates.

CHALLENGES FACING SMEs

Effective policy making should recognise the challenges to growth identified by SMEs. The biggest constraints to SME growth include a lack of access to finance, lack of access to electricity and technology, political instability, an inadequately educated workforce, and corruption.⁹ SMEs often face difficulty in defending their interests in

bargaining with suppliers and lobbying for policies that are in their interests, especially compared to larger firms. Women-led SMEs face greater, and sometimes different, barriers to those led by men: women nearly always have less access than men to assets, credit, services, markets and information about new technologies.¹⁰ Finally, the business regulatory environment is particularly important for SMEs, because SMEs tend to have fewer resources and staff to handle regulatory matters.¹¹

Support for SMEs

Governments can support SMEs in various ways, by promoting:

- **policy or legislative measures** such as credit, technical assistance and fiscal incentives
- **business development services** such as training, advisory services, information, and technology transfer.¹² For rural enterprises, **extension services and marketing support** can be especially valuable
- **targeted technical assistance**, information and advisory services, and finance to specific enterprises¹³
- **value chain programmes** whereby SMEs are linked to large corporations as suppliers or distributors¹⁴
- **procurement and local content programmes** whereby governments and/or large companies source inputs or services from domestic SMEs.

Governments promote SME support policies in virtually all countries in Asia and Latin America and many countries in Africa. Few spending figures are available, but Latin America is estimated to allocate less than 0.1% of GDP to SME support programmes.¹⁵ While many programmes are successful, some suffer from having a multiplicity of objectives and a lack of coordination, often with no single government department coordinating SME promotion policies, leading to duplication.¹⁶ Some governments lack the capacity or expertise to promote effective SME policies.

Figures on **donor support to SMEs** vary widely. The Organisation for Economic Co-operation and

Development (OECD)'s aid database calculates that donors provided US\$1.7bn in aid for 'business support services' in developing countries in 2013.¹⁷ However, the World Bank states that it, alone, provided around \$3bn a year in support to SMEs during 2006-12.¹⁸ All the multilateral development banks have programmes that address SME access to finance and 16 European development finance institutions make direct investments in enterprises, including SMEs. Donors have moved away from providing direct support to SMEs. The World Bank's Doing Business project advocates reducing government regulation of business to support domestic SMEs. However, considerable research shows that the indicators used in the project are not the major constraints to private sector activity in developing countries.¹⁹

Large corporations can also help SMEs grow by providing training in management, business planning, marketing and quality control and by promoting technology and knowledge transfer and investment in infrastructure.²⁰ Studies suggest that multinational companies are increasingly developing their own local content policies to support local SMEs, motivated by the desire to establish enduring partnerships with local suppliers.²¹

IMPROVING BUSINESS ENVIRONMENTS

Several lessons learned from SME support programmes emerge from the literature and experience:

Proactive government policies are needed, not simply regulatory reform of the business environment.

Considerable evidence, especially from Asia, shows that successful economic development has mainly been due to proactive policies by the state. In contrast to the 'low government regulation-approach' taken by most donors – such as Doing Business and the 'investment climate-reforms approach' focused on facilitating foreign investment – SME development is likely best supported by a 'high government support-approach'. Here,

policies can include providing strategic guidance to companies, targeting specific investors, time-bound subsidies and trade protection, differentiated tax incentives, export promotion, R&D funds, and information services.²²

Local-level policies are critical, and support policies should be based on local needs.

It is not only the business environment in the capital city that is important, but the environment in other areas of the country, including rural areas. Local authorities can play crucial roles in SME project implementation, financing and monitoring. Using local service providers to deliver business development services is more economical and ensures sustainability after the life of the project.²³

Governments should step up public procurement and local content policies and enshrine these in legislation.

Public procurement policies can have major positive impacts on poor people and local economic development. They can provide valuable market opportunities for SMEs if they stipulate sourcing from smallholder farmers or small enterprises for supplies needed in schools, hospitals and other public institutions,²⁴ as demonstrated in the case study from Brazil on page 25. Local content policies can require foreign and domestic investors to source their goods and services from domestic SMEs, boosting local economic development. African governments, especially, could do much more to increase their procurement and local content policies; currently, only a few have explicit local content policies in place, though the number is rising.²⁵

Value chains need to be improved to benefit SMEs.

Promoting SMEs by linking them to large companies in value chains has become a common support mechanism in recent years. This can facilitate the transfer of technology, knowledge and skills, improve SME business and management practices, and increase access to finance and markets.²⁶ Governments can assist SMEs to negotiate better terms with larger contractors and

provide legal assistance and model contracts, tackle the power of supply chains and the anti-competitive behaviour of large companies within them.²⁷ Improving value chains often means promoting inclusive business models. In agriculture, many current value chains are undermining farmers through exploitative relationships, notably through unfair contract farming arrangements and large-scale land acquisitions or land grabs.

Governments must promote a step change in support to women-led SMEs.

Women tend to be marginalised in society and the economy, so supporting women-led SMEs is essential for promoting inclusive development. Yet support programmes for women entrepreneurs rarely address the major constraints to female enterprise growth, such as concentration in low-productivity and low-growth activities, and the role of institutions and behaviour in discriminating against women. Women-led SMEs must pay to hire help whereas men-led SMEs can often exploit the unpaid work of women in family businesses. Support programmes need to engage with government institutions and chambers of commerce to reform legal frameworks that constrain female entrepreneurial activity.²⁸

Tax policies must be progressive in taxing more heavily those actors who have the greater ability to pay and also representative in terms of bringing voices of all sizes and shapes of individuals and companies when policies are set.

In many developing countries, governments effectively favour large companies in their tax policies. At worst, governments lose massive revenues from tax exemptions, the main beneficiaries of which are often large companies while closing down small businesses for the slightest delay in paying local taxes. Many countries have differentiated tax rates for companies, with lower rates or exemptions for enterprises below a certain size. In some countries, for example in East Africa, taxes based on turnover are common, and provide an alternative to profit-based accounting.²⁹

Countries could also adopt a more pro-poor tax policy by reducing taxes on SMEs which, while profit-orientated, also provide goods or services to the poor, such as social enterprises.

Policies that combine different types of SME support tend to work better than single policies.

The need to combine policies, rather than regard any single policy as a magic bullet, is a common finding in the literature on SMEs. For example, the impact of providing non-financial business development services is increased if dovetailed with access to finance initiatives.³⁰ CAFOD's Thinking Small work similarly found that successful NGO projects to support micro-entrepreneurs and small businesses did not focus on one improvement, but tackled all factors affecting the viability of poor businesses – economic, social, political and human. CAFOD's rural livelihood projects not only identified market opportunities and supported viable economic activities, but organised communities to build and maintain local roads, generating shared ownership, social capital and political voice, plus essential local infrastructure.³¹

Access to finance must be more comprehensive.

Some finance programmes for SMEs tend to have a narrow focus, simply providing credit lines to companies; yet access to credit is only one of the financial services that SMEs need. Health insurance or, for farmers, weather insurance, may be just as important but these are often unavailable or unaffordable, with women-led SMEs again most disadvantaged.³² The inclusion of savings instruments in financial packages can often better address the risk mitigation needs of SMEs. Provision of financial services should be complemented with financial literacy education.³³ Governments should prioritise SMEs in providing access to finance. A key is to promote systemic reforms to help build the capacity of countries' financial sectors to supply SME credit demand.³⁴

There is a need to improve worker and management training on human rights and labour conditions.

Labour conditions and skills affect a society's ability to create jobs, especially jobs that are well paid and improve firm productivity. The importance of management training is recognised in the literature on supporting SMEs.³⁵ The UN Economic Commission for Africa, for example, calls for enhancing management and business development in Africa through training and development programmes and the creation of SME Development Centres.³⁶ There is a growing literature evaluating the impacts of business training. Combining entrepreneurship training with access to finance tends to work better than standalone interventions. Programmes for young people are more likely to have positive results.³⁷

Appropriate infrastructure must be provided - including in rural areas.

Lack of electricity is often identified as a constraint to the growth of SMEs. Also important are good roads and transport services, access to water and irrigation, telecommunications, storage facilities and toilet and hygiene services. These infrastructure and public services need to be provided within a 'thinking small' framework that targets the needs of small businesses; too often, these services are size-blind.³⁸ Many governments prioritise urban areas for infrastructure investments, yet improvements in rural infrastructure are critical to farming cooperatives and rural enterprises. More, and better, feeder roads are especially important in rural areas, linking farmers to markets.³⁹

The voice and influence of SMEs in policy making must increase.

It is critical that governments actively consult with SMEs and involve them in policy making, and that there is support for organising SMEs into associations. Business associations, including Chambers of Commerce, are often dominated by large companies, which subsequently have the ear of government. SMEs can often partner with trade

unions and civil society organisations to strengthen their bargaining position.⁴⁰

Curbing corruption has particular benefits for SMEs and should be addressed.

While improvements in the fight against corruption help businesses of all sizes, some policy measures have particular relevance to SMEs. As Denmark's aid agency DANIDA has noted, certain funds could be made available to allow SMEs to take legal action to claim damages caused by corrupt practices involving public officials.⁴¹



Photo: Urban Poor Associates source rejected raw materials from factories and recycle them to make bags which are sold in leading shopping malls. Manila, the Philippines. Christian Aid/Ross Hemingway

INTRODUCTION

This study examines the ways in which governments and donors can better promote 'business enabling environments' so that small and medium-sized enterprises (SMEs) can thrive and contribute to inclusive economic development in developing countries. It focuses on 'what works' and contains a literature review of support for SMEs, plus three case studies from our experience as NGOs. We hope the study will inform decision making to ensure that more, and better, policies target what SMEs really need.

Supporting SMEs is critical to reducing poverty and promoting economic and private sector development in developing countries. These businesses constitute most firms, and in some countries, employ most of the workforce. SMEs may also provide basic goods and essential services to poor and excluded people in urban areas and, via farmers' cooperatives, can be the primary way in which poor people in rural areas are organised and market their production. Thus, they are critical for promoting inclusive economic development, including for women, who not only gain from employment and from the services they provide, but who own and manage a significant proportion of SMEs.

Much NGO work in the private sector - and donor and government policies - has focused either on large companies or micro-entrepreneurs, notably family farmers. The 'missing middle' is now receiving greater attention. Yet despite substantial literature about business development, remarkably little is known about which SME support programmes work and why.⁴² According to a recent evaluation of the World Bank's support to SMEs:

'The literature offers surprisingly little guidance on the actual efficacy of the most common forms of TSME [targeted SME] support, either for direct beneficiaries or, more broadly, for markets and economies, much less the appropriate sequencing and complementarities of interventions.'⁴³

Similarly, a 2014 report by the African Development Bank notes that few SME impact evaluations are publicly available and that, 'to our knowledge, no impact evaluation of SMEs assistance programs has been conducted in Africa so far'.⁴⁴ As regards Asia, an Asian Development Bank report notes that knowledge about the effectiveness of SME support programmes is 'relatively weak'.⁴⁵ This study draws on the information that is available, and adds evidence from our own experience.

There is significant funding of SME support programmes by multilateral development banks, international financial institutions, bilateral donors and governments. However, much of this support is focused on two areas: providing finance to SMEs (improving access to credit); and advocating general reforms to the investment climate, which tend primarily to benefit larger enterprises, including multinational companies, rather than SMEs. Other support programmes are often neglected.⁴⁶ This study challenges these mainstream approaches and suggests alternative support policies.

Definitions: SMEs and the business enabling environment

SMEs

This study focuses on SMEs, not micro-enterprises (sole traders with only a few employees). SMEs are regarded here as businesses with 10-100 employees (small) and 100-250 employees (medium). However, it is often not possible to be precise given that the literature and governments define SMEs differently across the world. In Kenya, for example, a small company is defined as having 11-50 employees and a medium-sized company 51-100, whereas in Mozambique a small company has 10-49 employees and a medium company 50-200.⁴⁷ The different definitions of international organisations are outlined below.

Criteria used to define SMEs⁴⁸

Institutions	Maximum number of employees	Maximum revenue or turnover (US\$)	Maximum assets (US\$)
World Bank	300	15,000,000	15,000,000
Inter-American Development Bank	100	3,000,000	None
African Development Bank	50	None	None
Asian Development Bank	50	None	None
United Nations Development Programme	200	None	None

The nature of SMEs varies greatly. SMEs range from small manufacturers – for example of furniture, metal parts, clothing or machinery – to services providers, such as restaurants, consulting and computer software firms. They include rural, as well as urban, businesses, notably farmer cooperatives and producer organisations, often involving smallholder farmers. Some SMEs do not seek to grow while others are innovation based and growth orientated.⁴⁹

The business enabling environment

Three main areas make up the business enabling environment:⁵⁰

- The formal rules, laws and regulations that governments at all levels impose on workers, markets and private businesses, such as tax legislation, property rights, employment law, human rights, labour rights and trade rules.
- The informal behaviour, customs and norms that determine business conduct and shape how markets work, and where governments can only have an indirect impact. Examples of this include consumer preferences and gendered norms and corruption.
- Public investment in infrastructure and provision of public goods and services by the government, such as health and education provision, transport and water management.

1. THE IMPORTANCE OF SMEs

1.1 Promoting inclusive economic development

SMEs are critical for promoting inclusive economic development and poverty reduction for a number of reasons.

SMEs constitute a **vast number of businesses and employ a large number of people** in developing countries. In many countries, it is often the poorest and most marginalised people who are employed by SMEs, meaning that policies to support them can have a direct impact on the poor.

- There are approximately 400 million SMEs (defined as those with up to 250 employees) in low- and middle-income countries,⁵¹ which account for around 60% of GDP in low-income countries.⁵²
- The UK's Department for International Development (DFID) notes that SMEs (again, with up to 250 people) employ an average of 66% of the permanent, full-time workforce in developing countries.⁵³
- Companies with 5-50 employees account for around 40% of all employment in Africa and South Asia; for companies with up to 100 employees, the figure rises to around 55%.⁵⁴ In Latin America, SMEs with 250 employees or fewer employ 67% of the workforce.⁵⁵
- By contrast, transnational corporations (*large* companies) employ just 4% of the global workforce, amounting to 80 million workers.⁵⁶

The International Finance Corporation (IFC) estimates that there are 8-10 million formal SMEs owned by women in developing countries, which represents roughly a third of all formal SMEs (with up to 250 employees).⁵⁷ Women tend to establish a higher proportion of service-orientated businesses than men, although there is significant variation across regions.⁵⁸ It is not known how many employees of SMEs are women, but the number must be large, highlighting the importance of SMEs in promoting equitable, gender-sensitive development. However, as a World Bank evaluation

notes, relatively little SME assistance has focused on women.⁵⁹

SMEs are also critical to inclusive economic development since they can provide **basic goods and essential services** to poor and excluded people. They frequently produce light consumer goods - such as food, clothes and wood products - to meet household demand. SMEs can be an important part of the supply chain of essential services, such as sanitation and water, and even compete with major service providers in some cases.⁶⁰ Domestic SMEs tend to have stronger links to national and local economies than larger, foreign companies which often work in enclaves. According to the UN's Economic Commission for Latin America and the Caribbean, promoting SMEs is 'a cornerstone for achieving greater social equality'. It states:

'The development of SMEs is critical if countries hope to overcome the deep inequality between the few large companies and the majority of other, smaller ones and advance towards labour markets that are able to create more and more high-quality jobs'.⁶¹

Although many SMEs produce for domestic markets, they can also be major contributors to **exports**. In India, for example, SMEs accounted for around 40% of exports during 1998-2008; in China, they contributed 60% of exports, and in Vietnam, 20%.⁶²

Job creation is clearly critical to economic development and some studies suggest that enterprises with fewer than 100 employees and young enterprises (less than two years old) have the highest job creation rates:

1. THE IMPORTANCE OF SMEs

- A recent OECD study shows that young, small enterprises create a disproportionately high number of jobs, while the International Labour Organisation (ILO) notes that in most countries more than 50% of net employment creation derives from companies with 5-99 employees. The figure is estimated to be 65% for low-income countries as a whole, 60% for Africa and 95% for South Asia.⁶³
- Other studies suggest that small, mature firms have the largest share of job creation in developing countries, with SMEs (with less than 100 employees) generating 77% of the new jobs.⁶⁴
- In Africa, small firms appear to create a disproportionate share of new jobs. A recent report for the UN found that, in the median African country analysed, 47% of new jobs were created in firms with 5-19 workers.⁶⁵

Other studies suggest that once the survival of firms is taken into account, small firms and large firms perform essentially the same in generating new jobs over the medium term.⁶⁶ However, DFID states that recent research provides clear evidence that small firms are good at creating jobs and expansion of the SME sector will boost employment and reduce poverty.⁶⁷ Other evidence suggests that SMEs engaged in exports tend to report higher turnover, growth and employment growth, and to be more productive than, non-trading firms.⁶⁸

This is not to say that SMEs are generally more **productive** than other firms. Data from the World Bank's Enterprise Surveys suggest that larger firms tend to be more productive since they benefit from economies of scale and invest more in machinery and skilled workers, whereas SMEs tend to be engaged in more labour-intensive sectors.⁶⁹ Many studies suggest that the *quality* of jobs is often higher in larger firms and that SMEs trail large firms in wages and benefits in the form of pension plans and health insurance.⁷⁰ However, this is not an argument for failing to target SMEs in support policies, but rather for doing precisely that, to improve the quality of employment. More labour-intensive companies, despite being *less* productive, can still be productive and can be better for the poor because they can employ more people.

It is important to highlight that most SMEs **operate informally**. The ILO notes that only 9% of SMEs globally are formal. India, one of the few countries with reliable data on informal enterprises, reported 17 unregistered SMEs for every registered SME in 2007.⁷¹ This prevalence of informality highlights the potential for developing countries to bring a large number of companies into the tax system, which could increase resource mobilisation and the potential for improving labour standards.



Photo: Workers at Nochari's processing plant, Nicaragua, pour 'flor de jamaica' (hibiscus juice) into bottles.
Christian Aid/Paula Plaza

Photo (opposite): Upendo Means Love began as a sewing school, and is now a social enterprise with a workshop and a shop, employing 20 women. Stone Town, Zanzibar.
Norwegian Church Aid/L aurie MacGregor

Gender bias in VAT rates

A study in Vietnam⁷² found a gender bias in value added tax (VAT) that impacted the profitability of female-led SMEs. It showed that the sectors in which women, as SME owners, were more active (trade in food and beverages, textiles and garments) carried a higher VAT rate for inputs than those sectors (products and services) in which men were more active. In particular, inputs needed for trade in food and beverages carried the highest VAT rate, regardless of type of food or trade, thus applying the same rate to a woman behind a stall on the street and in a restaurant. Overall, the data showed that female-led SMEs in urban settings bore 105% of the costs of male-led SMEs and their earnings were just 67% of their male counterparts. Despite this, female-led SMEs were found to contribute 40-60% of household income. This means that boosting profitability of women-led SMEs would greatly contribute to poverty reduction.

Other gendered dynamics were found to contribute to higher costs and lower profits. For example, on average, women had less collateral in their name to use in order to access finance through formal channels; unpaid care duties to fulfil which took away time from their business; and were less likely to register their business, which would have brought financial benefits in the form of VAT refunds. Their SMEs were smaller and less profitable because of higher input costs and no opportunity to claim VAT refunds. Women had fewer resources, both time and money, to shop around for cheaper inputs or to buy in bulk. Conversely, male-led SMEs were able to use unpaid labour provided by women within the household and were more likely to access formal sources of finance.

1.2 Challenges facing SMEs

Effective policy making should recognise the challenges to growth identified by SMEs. Many different surveys are available, though few highlight challenges to women-led SMEs - a major gap in current analysis.

- The ILO notes that the three biggest constraints to SME growth across countries relate to access to finance, access to electricity and competition from informal enterprises.⁷³
- A recent report for the World Bank notes that SMEs report their priority needs to be a reliable electric power supply, an honest and transparent public sector, moderate taxes, political stability, fair rules, so that informal firms cannot compete unfairly, and an adequately educated workforce.⁷⁴ These are outlined in Table 1 (page 16).⁷⁵

SMEs often lack **access to technology** and the scope for innovation, finding it harder than large firms to keep up with technological change. They may employ fewer technical specialists and lack the finance needed to purchase new technology on an ongoing basis. In the least developed countries, even reliable internet access and creating a business website can be challenging.⁷⁶ That said, in some countries and sectors, SMEs can be the most innovative and create new technologies which are then developed (or bought) by larger companies.

SMEs often face **difficulty in defending their interests**, whether in bargaining with suppliers and buyers or lobbying for policies or regulations that are in their interests, especially compared to larger firms. SMEs may be pushed out of markets by the concentration of power in the hands of a few multinationals dominating value chains.⁷⁷



1. THE IMPORTANCE OF SMEs

Table 1: Top constraints facing companies by firm size and income group⁷⁴

	No. of employees				
	5-9	10-19	20-99	100-299	300+
1 obstacle	Power 38.92%	Power 42.52%	Power 41.13%	Power 43.94%	Power 43.91%
2 obstacle	Corruption 35.07%	Corruption 37.95%	Corruption 37.48%	Tax rate 35.74%	Worker skills 35.63%
3 obstacle	Tax rate 34.87%	Tax rate 35.24%	Tax rate 35.48%	Corruption 34.87%	Corruption 33.03%
4 obstacle	Finance 33.75%	Political instability 32.80%	Political instability 32.23%	Political instability 33.32%	Transportation 32.11%
5 obstacle	Political instability 31.16%	Informal competition 32.39%	Informal competition 31.01%	Worker skills 33.28%	Tax rate 32.06%

Key constraints to SME development arising in the business environment include the following:

Lack of adequate **access to finance** has been a perennial concern of SMEs and policies to promote them. Some 55-68% of formal SMEs in developing economies are either not served or under-served by access to finance.⁷⁸ A 2010 study by the International Finance Corporation and McKinsey found that, in Africa, only 5% of bank loans went to small firms (as compared to 13% in all developing countries).⁷⁹

SME financing is limited because of high transaction costs and high perceived risks, meaning that the cost of borrowing is often higher for SMEs than for other companies. Banks do not lend enough to SMEs, partly because they are often unable to assess the risks and so overestimate them, and due to the amount of capital they need to allocate to the lending. This perception of risk is often exacerbated by SMEs lacking collateral to guarantee their repayments.⁸⁰ These concerns and problems are likely to be worse for women-led SMEs, although few studies address the access-to-finance gap for such SMEs (as opposed to micro-finance for women entrepreneurs).

As is also clear from the table above, an unreliable or non-existent **energy supply** is often a major problem, preventing businesses from expanding their operations or investing in a new location. Lack of energy is a particular issue in rural areas which are off-grid, and for smaller enterprises unable to afford alternative or back-up sources of energy such as generators.⁸¹

SMEs may struggle to access the necessary **management and workforce skills**. They may not have the financial resources to train or re-train their managers and workforce, and lack the resources or capacity to assess future skills needs, causing them to lose competitiveness over time.⁸²

Women-led SMEs face greater, sometimes different, barriers to those led by men. Women nearly always have less access than men to assets, credit, services, markets and information about new technologies, consumer preferences and export trade requirements.⁸³ Women also face particular barriers, such as greater time and logistics constraints arising from their (unpaid) care roles in the family. Recognising the challenges faced by women *within* SMEs can also be important, especially in businesses where women form the backbone of actual work but struggle to be heard over their male counterparts. In 2013, the International Conference of Labour Statisticians agreed to redefining what constitutes 'work' to include unpaid work in family businesses and activities mainly for personal use such as subsistence farming. This shift is accompanied by a narrower definition of employment, which counts only those people engaged in activities that are mainly for pay or profit. This should lead to a better understanding of women's workforce participation rate and the time they spend performing unpaid work and unpaid care.⁸⁴

Agricultural SMEs: Constraints to growth

Research by Farm Africa⁸⁵ on agricultural SMEs (with 5-150 employees) found that SMEs are not applying for the finance that might help them to grow. Reasons include the fact that SMEs:

- do not know about the range of products available to them or how they work
- find lending from financial institutions too expensive to use profitably
- do not have the experience, managerial capacity or business-planning skills to apply for loans successfully.

Financial institutions are failing to finance agricultural SMEs because they regard SMEs as being:

- too risky and unprofitable to lend to
- poorly managed, inexperienced and lacking sound business plans
- undercapitalised and without sufficient assets, such as land, against which to lend.

Other constraints to the growth of agricultural SMEs were highlighted:

- **A lack of professional staff.** Many agricultural SMEs are managed by semi-professional people and struggle to employ competent professionals because of unaffordable salaries. They lack the capacity for strategic planning and management systems.
- **Uncertainty.** They may operate in unpredictable and chaotic environments, hence presenting a weaker and unstable supply chain.
- **Cashflow.** Late payment by buyers, and an inability to generate their own finances or access finance from formal sources, make most agricultural SMEs undercapitalised and dependent on informal lenders.
- **Weak business plans.** High financial and business illiteracy among SMEs means they are often unable to prepare and present business plans.
- **Limited market data.** Inadequate quantitative data about the agribusiness market or SMEs makes it difficult for banks to assess market needs, size, and risk. Where data is available, it is often incomplete and inaccurate.
- **Isolation.** Most enterprises operate for years without complying with regulatory certification and licensing requirements and their operations and products remain outside of the formal market systems.
- **Low output.** Small producers lack working capital to finance production, leading to low volumes (low output, poor quality).

Corruption poses major challenges to business in many countries, notably to SMEs, which may find it more difficult to counter or bypass corrupt local practices. Some studies suggest that corruption determines the quality of business regulation in all but the most volatile political environments.⁸⁶

It is likely, although the literature is less clear, that SMEs face greater challenges than larger firms in addressing **climate change**. SMEs have fewer technological or personnel resources to predict extreme weather events and have less cash to prepare for or cope with such events, reducing their resilience.

Finally, the **business regulatory environment** is

particularly important for SMEs, which tend to have fewer resources (notably in terms of staff) to handle regulatory matters.⁸⁷ SMEs suffer more than larger firms from inflexible regulations and standards, high registration costs and high tax rates and often face relatively higher compliance costs.⁸⁸ Regulatory matters tend to have a stronger impact on the performance of SMEs than on large firms. Proportionate compliance costs with regulations can be anywhere from 10 to 30 times greater for SMEs than for larger firms.

SMEs may also have limited resources to implement **international standards on responsible business**, such as the UN Guiding Principles on Business and Human Rights, and international labour laws.⁸⁹

Country-specific examples: SMEs in Zambia, Cambodia and Nigeria

Promoting SMEs in Zambia

The Zambia Business Survey highlights the key determinants of productivity growth among Micro, Small and Medium Enterprises (MSMEs) in the country. It notes that firms with large capital stock have greater worker productivity and that, in agriculture, increased land size, as well as capital stock, increases productivity. It finds that educational attainment of the firm's owner affects productivity in non-agricultural firms (but only slightly in agricultural firms): completing secondary school raises productivity in non-agricultural firms by 26% compared to owners with less education. It also highlights the importance of access to productive inputs, such as water, electricity, banking and mobile phone services, as tending to increase productivity⁹⁰ and concludes that the key issues are to increase physical access to infrastructure, to promote basic education to help future firm owners, and to extend business facilitation such as training in financial record keeping, the availability of the internet and business networks.⁹¹

SMEs in Cambodia

One study of SMEs in Cambodia, part of a project implemented by the Economic Research Institute for ASEAN and East Asia (ERIA), studied the main barriers SMEs face, and put these in the context of the government's SME development policies. The study focused on manufacturing SMEs, 80% of which were in the agro-processing industry, and most of which had fewer than 10 employees. The three main barriers to SME development identified were the weak regulatory and legal framework, limited access to finance and a lack of SME support activities. The same three issues were acknowledged as important by the World Bank and the Asian Development Bank. The main problems with the regulatory system mostly related to the correct application of the rules rather than to the rules themselves. Beyond being exposed to burdensome, often unnecessary, regulations, Cambodian enterprises have to deal with the costs and uncertainties caused by poor governance and infrastructure and weak courts. The four main areas identified by the Government Sub-Committee on SMEs as being in need of targeted support were: business development services, access to (national and regional) markets, competitive technology and quality human resources, and links to value chains, government and other businesses.⁹²

Constraints for manufacturing SMEs in Nigeria

A World Bank survey in Nigeria of more than 2,000 firms across the country, most registered manufacturing SMEs, found that electricity, finance and transportation were the three most important investment climate impediments. The study emphasised the importance of fostering management capacity, underlining that 'good managers can be almost as productive in a poor business environment as poor managers are in a good environment'. It noted that a favourable investment climate is not useful if firm owners' entrepreneurship is weak, and called for central and local governments to provide initial enterprise support, especially in the form of management and business skills training.⁹³

2. SUPPORTING SMEs

2.1 Governments

Successful business linkages in India

One successful case study of enhancing linkages to SMEs identified by United Nations Conference on Trade and Development (UNCTAD) is that of the automotive and information technology sectors in India. The Indian government, both at the federal and state/regional level, helped shape industrial development in the country by formulating and implementing a coherent policy framework, establishing infrastructure and inducing a shared commitment among the parties. The factors explaining India's experience in attracting foreign investment and promoting business linkages with local enterprises include:

- sustained investment in education and research infrastructure
- the design of targeted policies and support measures to develop strategic industrial sectors
- the proactive role of the government in creating a critical mass of vibrant and entrepreneurial SME suppliers, which played a key role in motivating transnational corporations (TNCs) to forge business linkages with indigenous firms for mutual growth
- the emphasis given to cluster development strategies and the relevance attached to the creation of public-private sector partnerships.

Source: UNCTAD, Creating Business Linkages: A Policy Perspective, 2010

There are various ways in which governments can support SMEs, either directly or indirectly:

- Interventions can promote an enabling environment by focusing on **policy or legislative measures**. The instruments most commonly used in SME policies are credit, grants, technical assistance and fiscal incentives.
- Provide **business development services**, such as training, consultancy and advisory services, marketing assistance, information, and technology development and transfer.⁹⁴

For rural enterprises, **extension services and marketing support** can be especially valuable. **Cluster strategies** can also be promoted whereby services are provided to companies in specified geographical and/or sectoral areas.

- Interventions can **target specific enterprises directly**, with technical assistance, information and advisory services, and provision of equity capital and other forms of finance.⁹⁵
- **Value chain programmes** can be promoted, whereby SMEs are linked to large corporations as suppliers or distributors.⁹⁶
- **Procurement programmes** (such as buying goods and services) can involve governments and/or large companies sourcing these inputs from domestic SMEs.
- **Local content policies** are those promoted by governments or companies to encourage the use of local materials, labour or services rather than importing these or relying on foreign supplies. For example, they encourage businesses to source their inputs from local producers, employ local labour, contract services from local providers and use local manufacturing plants in their operations.
- In all these areas, governments should (but rarely do) promote **gender-sensitive policies** that support women-led SMEs or women workers within them.

In Asia, virtually all countries assist SMEs in some way, such as by promoting access to finance (notably, lowering the cost of finance) and providing various types of training for workers and entrepreneurs, technology extension services, marketing assistance, and business development services.⁹⁷ Similarly, almost all countries in Latin America, and many in Africa, have a simplified tax regime or differential labour regulations for SMEs, as well as programmes to facilitate access to credit and a set of subsidies and services aimed at supporting SMEs in different activities.⁹⁸

Many SME support policies involve the **direct delivery of services** to SMEs by public sector

2. SUPPORTING SMEs

agencies, for example, governments providing business development services or, in rural areas, providing agricultural extension services to farmers' cooperatives. Over the past decade, however, there has been a trend towards reforming public SME support programmes to incorporate market principles.⁹⁹ Thus, public agricultural extension services have been significantly cut back in many African countries in recent decades, in favour of part-privatised, cost-recovery programmes.

While SME support policies are generally considered important around the world, they tend to suffer from **particular problems**. An Asian Development Bank report notes three common problems with government SME programmes:

- They tend to suffer from a **multiplicity of objectives**, some contradictory. For example, support to SMEs may pursue social goals (such as providing certain input products) at the expense of promoting entrepreneurship and competitiveness.
- Often, no single department controls or coordinates SME promotion policies, leading to **duplication or lack of coordination**.
- They tend not to be subject to rigorous **evaluation**.¹⁰⁰

Another study of SME government support policies in developing countries notes that governments

may lack the capacity or expertise to promote effective SME policies. Support mechanisms may be centralised in capital cities with insufficient buy-in or capacity at local or regional level. Many countries also lack adequate data, such as on the competitiveness of certain sectors, to promote effective SME policies. Finally, there is the perennial danger of SME policies existing on paper but failing to be fully or effectively implemented.¹⁰¹

According to the UN Economic Commission for Latin America and the Caribbean, governments in the region began to take a greater interest in SMEs in the mid-1990s, owing to a marked rise in unemployment. But 'despite the good intentions, SME-support policies have so far yielded few concrete results', the analysis notes. The institutions that design these policies wield little influence and suffer from a shortage of effective policy instruments. Agencies include the Micro and Small Business Support Service (SEBRAE) in Brazil, the Production Development Corporation (CORFO) in Chile, the National Commission for Micro and Small Businesses (CONAMYPE) in El Salvador, and the Fund to Support Micro, Small and Medium-sized Enterprises in Mexico. Despite these efforts, actual spending on SMEs in Latin America is low – averaging less than 0.1% of GDP.¹⁰² Figures for spending on SMEs in other regions are not known.

SME support in Indonesia

In Indonesia, support to small firms has been an important facet of policy, ranging from giving privileged access to such companies in certain sectors, to more traditional credit programmes or subsidies, and training and counselling. Since 2008, support to small firms has been a duty of government, and most ministries, and many local government agencies, are involved in the delivery of support to MSMEs. One particular feature of Indonesia's support policy is that, since 2003, a law has mandated state-owned enterprises to allocate up to 5% of their net profit to support the development of MSMEs and co-operatives. This includes providing soft loans to non-bankable firms and grants to assist capacity-building activities in areas such as production and processing, marketing and technical skills improvement through mentoring programmes.

However, some analyses suggest that a lack of effective coordination has resulted in overlapping measures and inefficient delivery of support. Studies show that the form of assistance most often delivered is not necessarily that which is perceived by firms to be most effective. Counselling, training and financial assistance are the services most frequently provided but rank lower in terms of effectiveness than business linkage and networking and technology development, which are offered less frequently.¹⁰³

SME support in Kenya

A study of SME support policies in Kenya highlights institutional and regulatory challenges, including inadequate private and public dialogue at county level, poor enforcement of legislation and the lack of a policy document to guide the SMEs sub-sector. A further problem is poor coordination of SME activities due to several institutions providing support to, and regulating, SMEs - sometimes with conflicting interests. This contrasts with countries such as India and South Africa, where SME issues are coordinated by a central institution.¹⁰⁴

Kenyan SMEs are, however, likely to benefit from the government's commitment to enact new local content legislation. Kenya's Ministry of Energy and Petroleum issued a draft *National Energy Policy* in 2014 which highlights 'inadequate manpower, technical capacity and local content in gas exploration and production activities' as key challenges, and sets out a plan to develop local content policies for 2014-2030.¹⁰⁵ The draft policy aims to overhaul existing legislation and for oil companies to procure 60-90% of their goods and services locally, within 10 years. Companies would be required to produce annual local content plans and a Local Content Development and Monitoring Unit would monitor and implement local content provisions. Companies would need to give 'first consideration' to Kenyan services, goods and labour in their operations and all operations would have to include at least a 5% equity participation by an indigenous Kenyan company.¹⁰⁶

2.2 Donors

DFID's approach to access to finance¹⁰⁷

The UK's Department for International Development (DFID) support to an IFC financing programme notes the importance of going beyond traditional approaches:

'Traditional approaches have tended to concentrate only on providing credit lines to banks and have not always leveraged the banks' own capital as effectively as they might have done. Some banks are not liquidity constrained but are choosing to invest their capital in low-risk/low-return assets. Lines of credit although relevant in liquidity-constrained contexts have not always proven effective in getting banks to increase their lending to SMEs on a sustained basis. Very often, the financing to SMEs slows down or disappears when the donor support falls away. We propose to take a more comprehensive approach to address the SME financing gap. We believe that (a) providing banks with risk capital, funding for technical advice and technological innovations as well as providing liquidity; and (b) improving information about SMEs' credit worthiness, provides a more rounded package and has a better chance of causing banks to sustainably increase lending to SMEs. Reforming wider financial structure issues (for example, to drive more competition between banks, facilitate market entry) is also part of the solution to drive down lending costs and promote more risk appetite.'

Figures on donor support to SMEs vary widely. According to the OECD's aid database, multilateral and bilateral donors provided \$1.7bn in aid for 'business support services' in developing countries in 2013; Africa received \$463m and South/Central Asia \$365m. The largest donors were the US, World Bank, EU, Germany and Denmark.¹⁰⁸ However, the World Bank states that it, alone, provided around \$3bn a year in support to SMEs during 2006-12.¹⁰⁹

All the multilateral development banks have programmes that address SME access to finance and most provide technical assistance to governments on policy reforms affecting the business environment. The International Finance Corporation is the largest development finance institution supporting SMEs, although only 2% of its portfolio is in Africa.¹¹⁰ Some 16 European development finance institutions (DFIs) specialise in making direct investments in enterprises. A recent evaluation of DFI support to SMEs in Africa notes that 'providing support to the SME sector is viewed by development finance institutions as a powerful means for achieving economic and social development objectives'.¹¹¹ In the aftermath of the financial crisis, the G20 has also sought to scale up support to SMEs, notably through an SME Finance Challenge and an SME Finance Innovation Trust Fund.¹¹²

As briefly noted earlier, donor support is mainly focused on providing access to finance and reforming investment climates, notably through the Doing Business project of the World Bank, including the Enabling the Business of Agriculture project, which focus on reforms to business regulations.¹¹³ Donors have moved away from providing direct forms of support to SMEs:

- European DFIs, for example, favour providing financial support to financial intermediaries, who then on-lend to SMEs.¹¹⁴
- A recent evaluation of the World Bank's support to SMEs notes that it promoted 103 projects providing access to finance but only 25 provided business development services during 2006-12.¹¹⁵

Photo: Food production cooperative, Young Women's Christian Association, the occupied Palestinian territory. Christian Aid/Charlotte Marshall

The Doing Business project promotes reducing government regulation of business to support domestic SMEs. However, considerable research shows that the indicators used in the project are not the major constraints to private sector activity in developing countries. As a World Bank Independent Evaluation Group (IEG) report states, the Doing Business indicators stress ‘too partial a picture’ of the policy reforms relating to the business climate and do not cover crucial factors on which investment decisions depend, such as infrastructure, labour skills, corruption or macro-economic stability.¹¹⁶ The IEG concluded that:

‘The Doing Business indicators... do not and cannot be expected to identify priority actions across the business climate as a whole... Nor can the Doing Business indicators be expected to help determine policy actions because they cannot situate the regulatory constraints within a country’s policy context and macro-economic framework.’¹¹⁷

Several other studies draw the same conclusion.¹¹⁸

The bilateral donor community is highly fragmented in its support for SMEs, and donor strategies to finance SMEs vary greatly, with some focusing on institutional, legal and regulatory reforms to improve the investment climate, others on interventions to remove the constraints to growth faced by SMEs. One recent report concludes that individual development agencies are not generally aware of the projects and policies of their peers, and there is little coordination, either globally or at the country level.¹¹⁹

South-South partnerships are playing an increasingly important role in supporting SMEs. For example, the China Development Bank has signed development-financing agreements for SMEs with the Development Bank of Southern Africa and the West African Development Bank, while the Export-Import Bank of China and the Agricultural Bank of China have both signed cooperation framework agreements with the African Development Bank to finance the development of SMEs.¹²⁰



The European Commission has published criteria for supporting private sector actors in development:¹²¹

- **Measurable development impact.** Support given to a private enterprise or financial intermediary has to contribute in a cost-effective way to the achievement of development goals such as job creation, green and inclusive growth or broader poverty reduction.
- **Additionality.** Without public support, the private enterprise would not undertake the action or investment, or would not do so on the same scale, at the same time, in the same location or to the same standard. The supported action should not crowd out the private sector or replace other private financing.
- **Neutrality.** The support given should not distort the market and should be awarded through an open, transparent and fair system.
- **Shared interest and co-financing.** Partnerships with the private sector have to be based on cost-effectiveness, shared interest and mutual accountability for results.
- **Demonstration effect.** A supported action should aim to have a clear demonstration effect that catalyses market development by crowding in other private sector actors for the replication and scaling-up of development results.
- **Adherence to social, environmental and fiscal standards.**

2.3 Companies

Large corporations can help SMEs grow and become more viable business partners by providing training in basic skills such as management, business planning, marketing, distribution and quality control. They can assist through technology transfer, direct investment in infrastructure and sharing knowledge. These can help make SMEs more competitive and access credit. They can also benefit large corporations by creating more effective and inclusive supply chains.¹²²

Some multinational companies are choosing to support local SMEs by developing their own

local content policies. A recent study of local procurement among 23 companies found that companies have become increasingly motivated by the desire to establish enduring partnerships with local suppliers, as part of their business model.¹²³ For example, gas multinational BG Group develops a procurement approach benefitting local companies for each location.¹²⁴ Italian oil company ENI requires each subsidiary in the upstream sector to develop its own local content plan and offers local companies support and training.¹²⁵ Multinational drinks business Diageo recently met its target of sourcing 70% of the agricultural materials used in its African operations locally from within Africa by 2015, and has now increased its target to 80% by 2020.¹²⁶

3. CASE STUDIES

This section provides three case studies from the experience of the NGOs producing this report, which show how SMEs – in urban and rural areas – are being successfully supported through public procurement programmes, advocacy networks and access to finance schemes, and the impact this is having on poor people who benefit from them.

3.1 Brazil: How public procurement is supporting small farming businesses

Brazil's public food procurement programmes are good examples of how farming cooperatives and associations can be helped to develop. These are directly improving the enabling environment for small businesses, as shown in the example of the COOTAP organic rice cooperative.

The Brazilian government is promoting a Food Acquisition Programme (*Programa de Aquisição de Alimentos*, PAA) and a National School Feeding Programme (*Programa Nacional de Alimentação Escolar*, PNAE), which comprise one of the world's largest 'institutional procurement' initiatives involving purchasing food produced by farming cooperatives and smallholder farmers. These programmes benefit more than 200,000 families growing and selling food.¹²⁷ The government budget in 2013 for the PAA's food purchases was R\$1.4bn (US\$397m) and R\$1bn (US\$284m) for the PNAE.¹²⁸

- In the PAA, government bodies purchase food from smallholder producers with no bidding process and at set prices. The UN estimates that more than three million tonnes of food have been purchased through the PAA over 10 years.¹²⁹ In 2012, more than 22 million Brazilians were consumers of food in the PAA programme.¹³⁰
- Since 2009, Brazilian law has also required at least 30% of food for school meals to be purchased from family farms; the PNAE programme provides school meals for at least

43 million students.¹³¹ These purchases directly increase the incomes of farmer associations and smallholder farmers.

The PAA has resulted in various economic and food security benefits for Brazilian smallholders and wider society. A study for the Food and Agriculture Organization of the United Nations (FAO), for example, notes that commonly assessed impacts include: greater diversification and increase in family farm production; increased income for farmers; and strengthening and development of collective organisations. Increased production and incomes derives not only from the PAA providing a guaranteed market for sales, but because the programme pushes up local prices for family farm products. The FAO report, the guarantee of the PAA market and its set price 'enables family farmers to negotiate prices in the private market, or even with traditional intermediaries, and therefore also obtain, outside the programme, a price closer to the market one'.¹³²

Other studies suggest that farmers participating in the PAA receive anywhere between 30-100% higher prices than from private intermediaries or selling directly to the market.¹³³ New cooperatives have arisen as a result of the PAA. 'Studies demonstrate that these were created to enable family farm producers to access PAA, and also help participants to access other markets and/or mobilize political and economic resources'.¹³⁴

Brazil's procurement policies have been brought about partly due to lobbying by social movements and faith-based organisations, including *Movimento Sem Terra* ('The Landless Movement' or MST), a partner of Christian Aid, and other NGOs in the ACT Alliance. MST is Brazil's pioneering organisation for enabling landless people to access land for farming; it has helped settle 13 million families and maintains 19 cooperatives for producing and marketing agricultural produce.¹³⁵ More than 90% of the production from MST cooperatives goes to social programmes through the PAA and PNAE.¹³⁶

3. CASE STUDIES

MST has a long history of advocating market access for smallholders and now supports other organisations to do this at a regional level. Most family farmers are organised into cooperatives or associations and can collectively lobby authorities on these public policies. MST was a key player in pressing the government to make it national law that a percentage of purchases for institutional programmes should come from smallholders. As a result of these legal changes, smallholder farmers can earn between \$2,122 and \$3,087 per family, per year from selling food products to the PAA, and can earn an additional \$7,718 annually, selling products to the PNAE. Lobbying has helped improve the programmes' effectiveness, and reduced bureaucracy, enabling them to work more efficiently for farmers' cooperatives.

Cooperative of Settled Workers in Porto Alegre

One beneficiary of Brazil's public procurement is a farming cooperative in Rio Grande do Sul state called COOTAP (the Cooperative of Settled Workers in Porto Alegre)¹³⁷ which mainly produces organic rice, selling it to the procurement programmes. COOTAP works in 17 cities and towns in the Greater Porto Alegre area and involves 471 families. Founded in 1994, COOTAP began planting rice on 100 hectares in 1997. Since then, the crop area has grown exponentially and COOTAP's rice farmers now work an area of 4,799 hectares and produce 475,000 bags of organic rice per year. In the 2014/15 season, they produced more than R\$19m (US\$5.39m) worth of rice.¹³⁸ On average, each family producing rice currently makes around R\$40,000 (US\$11,340). COOTAP's organic rice farmers are achieving higher incomes than many conventional farmers because their input costs are lower and they invest the saved capital in developing their business, for example, by increasing processing. These gains are also likely to be achieved over the medium and long term because organic production is preserving biodiversity and soil fertility.

COOTAP sells most of its rice to Brazil's procurement programmes, leaving some to be sold on private markets, such as to grocery stores, supermarkets and restaurants. Some 80% of COOTAP's revenues derive from sales to the National Supply Company (CONAB), a state body that operates a national food-stocking policy to guarantee minimum prices for farmers and maintain sufficient stocks to keep prices stable.

Most of COOTAP's remaining 20% of revenues derive from sales to the national school feeding programme (PNAE). In 2014, COOTAP signed an agreement with the São Paulo city government to sell 1,000 tonnes of organic rice a year to the PNAE, a key achievement for the cooperative that will directly benefit 140 family rice producers and indirectly benefit many more. Women farmers, who produce much of the rice, will especially benefit, as will the schoolchildren, eating chemical-free food. COOTAP's Coordinator Nelson Luís Krupinski says that the market access achieved through the PAA and PNAE has not only reinforced the role of smallholder producers in Brazil but has enabled farmers to achieve larger-scale production. Finding markets has also reduced wastage, which sometimes reached 70% of production due to lack of proper transportation. Krupinski says that the 'institutional market' of the PAA and PNAE has a further important by-product: improving organisation and cooperation among farming families. He says:

'To a certain extent, these programmes have been changing the situation in settlements in terms of production, work methods, economic and productive development, as well as quality of life. In fact, families strengthen their culture, gain independence, provide healthy sustenance, boost their self-esteem and make land fulfil its social role when they themselves produce and don't have to work for others for a living... These achievements help families make plans and become organised because they gave us a steady market share. This allows us to compete and organise our production.'¹³⁹

COOTAP's farmers are also focused on selling more to private markets. In 2012, the largest supermarket chain in Brazil, *Pão de Açúcar* ('Sugar Loaf') agreed to purchase 15 tonnes of organic rice from COOTAP. The success was reinforced by the fact that sales were of COOTAP's own brand of rice - *Terra Livre* ('free land') - whose growth on the market has been made possible by the increasing storage, processing and packing facilities among the cooperatives with which COOTAP works. COOTAP has recently begun selling its rice in vacuum packaging, which lengthens the expiration date - and consequently the selling price. Although the costs of vacuum packaging are higher, so are the profits.

COOTAP supports its farmers by buying their production and providing finance in pre-harvest periods. It supports other cooperatives of small farmers by outsourcing to them the processing of the rice sold by COOTAP. In addition, there is a technical assistance cooperative, COOPTEC, which helps farmers promote organic farming and assists others in making a transition to organic approaches. COOTAP's organisation is based on a system inspired by MST. Groups of families manage production systems for different crops, such as rice, fruit, medicinal plants, milk, fish and vegetables, and families organise groups to set up street market stalls in the cities around Porto Alegre.¹⁴⁰

COOTAP's partners, MST and Christian Aid, have been working with the organisation to develop business plans to continue its growth. Expanding their markets is especially important, as the state's procurement policies are still not large enough to guarantee markets for the production of all smallholders and are not implemented in many remote areas. Increasing access to markets means acquiring new skills in marketing and branding. The farmers face significant challenges. COOTAP lacks adequate storage facilities as its production increases, and currently has to outsource some 30% of its production to other storage facilities. Farmers also lack sufficient working capital to invest further in their businesses and suffer cash flow problems, due mainly to the amount spent on the purchase of feedstock, which equates to 69% of COOTAP's costs.¹⁴¹

Brazil's public procurement programmes have room for growth; the PAA currently benefits only 5% of Brazil's family farmers.¹⁴² However, the

programme is under threat due to the current political and economic crisis in Brazil. The model is being replicated in Africa. PAA Africa, based on the Brazilian model, was launched in 2012 jointly by the Brazilian government, the FAO, the World Food Programme (WFP) and the UK's DFID. The programme is currently carried out in five small-scale projects in Ethiopia, Malawi, Mozambique, Niger and Senegal.¹⁴³

3.2 Philippines: The PRESENT Coalition

A broad coalition in the Philippines, involving partners of ICCO, has spearheaded groundbreaking change to improve the business environment for social enterprises. The coalition, known as PRESENT (Poverty Reduction Through Social Entrepreneurship) is an alliance of around 20 networks of social enterprise practitioners, advocates, NGOs and academics which have come together to advance social entrepreneurship as an approach to poverty alleviation and economic development. Co-chaired by the Ateneo School of Government and the Foundation for a Sustainable Society (FSSI), the coalition comprises microfinance, cooperative, fairtrade, small producers and enterprises united in saying that social enterprise is a viable approach to addressing poverty sustainably.



Photo: Organic rice, produced and packaged by MST in Rio Grande do Sul state in the south of Brazil. Christian Aid/Tabitha Ross

Social enterprises

Social enterprises are organisations providing goods and services for the purpose of improving the wellbeing of poor and marginalised people. They invest in the poor to become effective workers, suppliers, clients or owners and reinvest their profits into the enterprise. The social enterprise movement has been building in the Philippines for several years, and there are more than 30,000 social enterprises in the country, the vast majority being cooperatives and associations.^{144,145} Women probably occupy as many leadership and management positions in Filipino social enterprises as men.¹⁴⁶ Social enterprises are crucial to SME development and pro-poor economic development, helping to supply affordable public goods and providing jobs.¹⁴⁷

Typical challenges facing social enterprises include a lack of government programmes supporting social enterprise development and corruption in regulatory bodies. Internally, social enterprises tend to lack adequate financing, find it difficult to develop capacity among managers and people and struggle to manage operations efficiently to meet volume and quality requirements of markets.¹⁴⁸

Advocacy for new legislation

The Coalition has drafted the Poverty Reduction Through Social Enterprise (PRESENT) Bill, promoting social entrepreneurship, and was able to convince legislators to sponsor the bill in both the House of Representatives and the Senate. A general election is taking place in the Philippines in 2016, and it is hoped the bill will remain a priority for the new government and will be enacted without further delays. The bill could have a dramatic impact on the welfare of the poor in the country. A study by the Philippine Institute for Development Studies, for example, notes that the record of the past 25 years of market-led development in the Philippines has failed to improve public services significantly, and that the development of social enterprises can be a solution to the failed provision of public goods.¹⁴⁹

Until now, policy makers have not recognised social enterprises as playing a vital role in development, although the government is promoting some policies that support SMEs.¹⁵⁰ Current government programmes tend to deliver services to the poor by treating them simply as clients or recipients of services rather than as actors in their own development. Thus the PRESENT coalition is undertaking a range of advocacy and awareness-raising activities.¹⁵¹ Activities have focused on policy analysis, public education and direct promotion of social entrepreneurship. Coalition members undertake lobbying of various government departments and both chambers of Congress. The post-2015 policy agenda has been important in making the case for the government to legislate for

social enterprises, and roundtable discussions at the Senate have been promoted by the coalition for this purpose. FSSI, alongside the Philippines Social Enterprise Network (PhilSEN) and the Institute for Social Entrepreneurship in Asia (ISEA), which are other major actors in the coalition, are also promoting social enterprises in various conferences and seminars in the Asian region. ISEA has led the coalition's academic research work and produced learning materials for social enterprises and their advocates.¹⁵²

The PRESENT Bill¹⁵³ promises to give an unprecedented boost to social enterprises in the Philippines, and calls on the state to 'empower the poor as primary stakeholders in social enterprises... and extend the assistance necessary for their advancement... provide technical and financial assistance, incentives and other services to enable Social Enterprises to develop into viable and vital anti-poverty agents'.¹⁵⁴

The bill adds that the PRESENT programme 'shall be established as a flagship program of government' and that it should identify 'strategic economic subsectors with the potentials for growth and where the poor are concentrated or could be major players'.¹⁵⁵ This is one of the major highlights of the bill that provides a mechanism for making the poor partners in development through social enterprises and for mainstreaming such enterprises in economic development.

The bill also contains some crucial commitments on the part of government:

- It establishes a Centre for Social Enterprise Development (CSED) in the existing Micro, Small and Medium Enterprise Development Council, itself an agency of the Department of Trade and Industry, to promote social enterprises. The CSED will develop and implement the PRESENT programme by designing and delivering training, education and capacity building in social entrepreneurship development.
- The government will create a Social Enterprise Development Fund, with resources of 500m pesos (US\$10.7m), to support the capacity-building component of the PRESENT programme.
- The Land Bank and the Development Bank of the Philippines and other government financial institutions will establish special credit windows to provide social enterprises with risk-based, non-collateralised loans.
- 'Key' government departments will allocate 'at least 10%' of their annual budgets specifically for projects to be procured from social enterprises.¹⁵⁶

However, the biggest disappointment is the removal of tax exemptions proposed for social enterprises in earlier versions of the bill. Social enterprise networks argue that tax incentives are important to enable social enterprises to upscale because they provide services that the government should be providing. Tax incentives could also ensure revenues generated by social enterprises are ploughed back to the community. There is also an inconsistency, in that tax incentives are given to some other domestic and foreign companies even though they may provide no social or environmental benefits.

The most important aspect of the proposed legislation is that, for the first time, social enterprises are recognised as key actors in economic development in the Philippines. But the financial resources allocated to social enterprises, and in particular the government procurement commitments, also promise to provide a big boost to the sector.

The bill is not without its critics, including senators, who oppose it, arguing that some corporations which are not strictly social enterprises, will seek to take advantage of its benefits. The bill has only a limited explicit focus on gender, calling for 'gender-sensitivity by ensuring women's equal

rights and access to social enterprises' resources'.¹⁵⁷ But due to the significant role of women in the country's economy, including in rural areas and in the informal economy, women are likely to benefit significantly from the bill.

Challenges for social enterprises in the Philippines

Regardless of the outcome of the bill, social enterprises face a number of challenges in the Philippines, which the government, donors and others could help to address.¹⁵⁸

1. The need to secure more funding for activities to support social enterprise development. The PRESENT coalition has worked on a shoestring budget, with little funding for advocacy on social enterprise compared to that available for CSO campaigns on other issues. While other organisations often receive funding from international donors and UN agencies, the coalition receives support only for activities such as maintaining a network coordinator and conducting two-to-three roundtable discussions and coalition meetings. Other activities are largely funded by FSSI with counterparts from coalition members; this funding amounts to less than 1m pesos (US\$21,346).
2. The need to generate more research and evidence on the benefits of social enterprise for the poor, the community, the environment and the economy, and on ways in which such organisations could be better supported. In particular, more research should be conducted into how to link pro-poor social enterprises with larger businesses, to ensure the latter play a more positive role in the country's economic development.
3. The need to boost workforce skills. Social enterprises in rural areas often lack appropriately skilled staff with sufficient business skills, especially in remote, rural areas. Some of the most successful social enterprises, in terms of size and scale, are those hiring people with corporate experience. Formal and informal mentoring could be especially important in building business and marketing skills.
4. Learning about social enterprises can be enhanced through education. Several tertiary

3. CASE STUDIES

academic organisations in the Philippines provide social enterprise programmes and courses and there is growing focus on social enterprise at secondary, and even primary, level. The government could encourage a greater focus on social enterprises in the education system and promote more vocational training.

5. Access to finance is likely to remain a critical area despite the new bill's provisions on this. Access to finance is described as a major constraint by many social enterprises in the Philippines; stakeholders identify problems accessing particular types of finance and often lack collateral for securing loans, while investors may face difficulties finding suitable investees.
6. Partnerships between social enterprises, government and business organisations are needed to scale up the impact on the poor, for example, by promoting inclusive business and impact investments and developing a more comprehensive support programme for social enterprises. Overall, government and business institutions need to be willing to change policies and practices that have not worked in favour of the poor and be willing to undertake innovations to support the scaling up of social enterprises.
7. Social enterprises need more support in navigating the Philippines' fiscal and regulatory requirements. The government's *Go Negosyo* programme provides some support for this and there are some tax exemptions for some micro- and small enterprises, but only for organisations with assets of less than 3,000 pesos and a maximum of 10 staff. It is often difficult, in practice, to access and process this tax exemption, and few social enterprises are likely to be taking advantage of it.

3.3 The ACRE programme: Building SME capacity and finance to help rural producers and consumers

Access to Capital for Rural Enterprises (ACRE) is a not-for-profit consortium of international NGOs, led by Christian Aid and including Challenges Worldwide, Practical Action, Traidcraft and Twin. It supports SMEs in countries where access to finance is a challenge, by building their capacity to manage successful businesses, helping them to evaluate their social impact and increasing their ability to access finance. It supports enterprises that have growth potential and a clear social and economic impact on their communities and the markets in which they operate. The ACRE consortium has, so far, identified 100 enterprises in Africa, Asia and Latin America that need patient investment, alongside technical assistance, to expand sustainably, potentially lifting hundreds of thousands of people out of poverty and improving the market systems in which they operate.

ACRE has a two-phased approach. First, it provides business skills and helps strengthen the capacity of SMEs to promote their impact investments, focusing its support on enterprises that will create wider social and market change. Second, it engages investors and strives to catalyse increased patient capital by building investor confidence and raising awareness of the challenges rural enterprises face, as well as demonstrating their social impact.

The NGO members of ACRE identify, and then visit, the enterprises and gather information to produce a comprehensive review, and propose technical assistance to complete pre-investment preparation. Funds are raised to cover the cost of this technical assistance and support the enterprise in producing its business plan. Technical assistance is sourced from long-term technical volunteers, pro-bono consultants, in-house experts or external consultants. In ACRE's experience to date, the following have been identified as being among the key constraints to SME growth:

- lack of access to affordable finance
- management skills gap
- lack of accurate market information and profile of competitors
- cumbersome regulations and red tape
- lack of awareness of options for growing internal governance structures in the company sometimes constrain the ability to scale up.



Lèt Ayogo

Examples of SMEs supported by ACRE in Africa

In Zimbabwe, where long-term finance is difficult to source due to the current economic and political environment, ACRE has been supporting an enterprise engaged in sustainable social entrepreneurship through the authentication, processing and marketing of high-quality organic products, including essential oils, herbs and spices for the international market. The enterprise trains and facilitates the cultivation and production by small-scale producer groups, especially women, and supports the certification of high value crops – Organic EU, National Organic Program (NOP), Union for Ethical BioTrade (UEBT) and Fairtrade. It also promotes the production of organic staple foods, in addition to securing fairtrade prices. The relationship between the enterprise and the farmers is based on cooperation and empowerment. Communities that previously depended on subsistence farming in typically dry lands now have a crop that provides them with cash and the flexibility that it brings.

Using the ACRE business support tools, the due diligence team identified 15 development points, which fell into two main areas: governance (financial information, reporting and analysis to be integrated into decision-making processes) and operational practices (the development of a growth strategy and a business plan). This analysis was used to design a technical assistance package that was delivered over a period of four months by an accounting specialist and a business advisory firm. Aside from improvement in the day-to-day running of the business, the enterprise now has a strategic plan for growth and a business plan. The latter has been used by the enterprise to lead negotiations with an investor to fund their expansion plans.

In Uganda, an SME cooperative supported by ACRE produces and trades award-winning speciality coffee in the west of the country. The company, which has 36 staff, sources its natural processed coffee from 5,237 members who are typically poor and disadvantaged, and channels the products to roasters in North America and Japan. This SME is unique, operating on three different fronts: its coffee business; providing micro-finance to rural communities; and promoting holistic capacity building projects, especially on climate change adaptation and gender equality.

The company approaches its business using the gender action learning system (GALS), which ensures that voices of both women and men are reflected in strategic decision making, for example, in household finance planning and community development. With access to finance, the company plans to install drying facilities at its headquarters and at its micro-stations; this will increase the volume of coffee collected from members that can be processed and exported to international markets. Business expansion will not only create more jobs in the local area but enable the company to extend more loans to people in communities. The expansion of funds will enable the company to establish an education loan programme for the children of coffee farmer members, whereby farmers can pay back loans in coffee.

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Impact and lessons learned

To date, ACRE has diagnosed the needs of 27 enterprises: 14 enterprises have received an early-stage pre-investment appraisal; 13 enterprises have been supported with pre-investment technical assistance and two have pitched to the syndicate of investors. Through supporting these enterprises, a total of 12,746 poor and marginalised individuals either supplied goods or benefitted from services. All these enterprises demonstrate clear intentionality to pro-poor market development and most of them source inputs and outputs from/to more than 84% of poor and marginalised individuals.

Currently, ACRE has 100 enterprises at the 'identification stage' in its pipeline in Africa, Asia and Latin America. More than 68% of enterprises are located in Africa (Ghana, Uganda, Malawi, Kenya, Mali, Rwanda, Zimbabwe, Burundi, Tanzania, Mozambique, Sudan and Swaziland). In Asia, ACRE enterprises are in Africa (Burundi, Ghana, Kenya, Malawi, Mali, Mozambique, Rwanda, Sudan, Swaziland, Tanzania, Uganda, Zimbabwe). In Asia, ACRE enterprises are in Bangladesh, India, Nepal and the occupied Palestinian territory, and in Latin America, in Bolivia, Chile, El Salvador, Honduras and Nicaragua.

In terms of industry profile, 48% of the ACRE pipeline enterprises are in the agricultural sector, working directly with smallholder farmers or harvesters. The agricultural sector does not only cover large commodity crops such as maize, sesame, peanuts and coffee, but includes indigenous leafy vegetables, baobab fruit and karaya gum. Service provider enterprises include clean energy and information and communication technology, such as mobile platforms for agriculture and services related to hospitality, including tourism.

A number of key lessons regarding 'what works' are emerging from ACRE's experience:

Importance of partnership

Partnership is the cornerstone of ACRE, which connects SMEs to international NGOs and investors, legal advisers and technical assistance providers, many of whom provide pro-bono

services or offer hugely discounted rates for their services. Expanding this partnership network and mobilising support from like-minded organisations and individuals is crucial to achieving impact and scaling up, and is generating interest from other NGOs which hope to join the ACRE platform. providers, many of whom provide pro-bono services or offer hugely discounted rates for their services. Expanding this partnership network and mobilising support from like-minded organisations and individuals is crucial to achieving impact and scaling up, and is generating interest from other NGOs which hope to join the ACRE platform.

Pre-investment support is fundamental

Many SMEs, even larger ones, often lack appropriate growth strategies, operations plans and capacity to produce investable business plans. ACRE draws up the needs of enterprises and provides tailored support by match-making with appropriate service providers.

Strengthening value chains

Supporting an SME is important, but strengthening a value chain helps many more poor and marginalised people who are not necessarily within the remit of the particular enterprise. Some SMEs supported by ACRE play a pivotal role in opening up new opportunities in markets by engaging in advocacy to change policies and practices. For example, an enterprise in Zimbabwe was instrumental in lobbying the EU to allow the import of baobab into Europe, opening up a huge market. Similarly, an enterprise in Bangladesh played a vital role in influencing the government to allow e-commerce in the country. By working with such enterprises, ACRE hopes to facilitate market opportunities.

Enhancing SMEs' human resources

Critical to SME success is employing capable staff, but SMEs often find it difficult to access the right people, which can hold back business growth. Several enterprises identify the need to recruit marketing or sales staff, for example. There is often a lack of competent staff members for these roles, since they may operate in remote locations and/or offer relatively low pay. ACRE is working with partners to increase technical capacities available.

4. WHAT WORKS AND WHAT IS NEEDED IN SME SUPPORT?

SME support programmes can promote development and reduce poverty, as illustrated in the earlier case studies. This is also highlighted in recent studies by, or for, the Inter-American Development Bank, the World Bank, the

Independent Evaluation Group of the World Bank and the International Labour Organisation, as shown in the box detailing the 'recent reviews of SME support programmes', below.

Recent reviews of SME support programmes

A impact evaluation, by the **Inter-American Development Bank (IADB)** of support to SMEs in Latin America and the Caribbean, notes that a 'substantial share of the economic development literature suggests well-targeted policies aimed at promoting SMEs can lead to positive development outcomes'.¹⁵⁹ The IADB evaluated support to Brazilian manufacturing SMEs and assessed credit support, business consulting, export promotion and clustering. The study found that credit support had the most positive impact on employment and wages; companies receiving such support experienced a 15% increase in the number of employees, a 2.4% increase in wages and gains in the value of exports and trademark registrations. SMEs receiving business-consulting support increased their number of employees by an average of 16%.¹⁶⁰

One review of 20 impact evaluations of SME support programmes in developing countries for the **World Bank** evaluated three types of support: business development services, research and development (R&D) programmes (to promote investments in R&D, stimulate development and the introduction of new products and production processes), and financing programmes (typically concessionary loans for working capital, debt restructuring, and financial incentives to promote investments). It found generally 'positive impacts of program participation on intermediate outcomes, but mixed results for impacts on firm performance'. Half of the developing country studies found positive impacts on performance measured by sales and exports, although none found evidence of employment gains. The study noted that many developing country studies find gains in intermediate outcomes such as R&D expenditure, worker training, new production processes and quality control programmes, networking with other firms and with different sources of information and funding. Business development services that focused on export promotion and network development services (in Chile) and worker training and technology upgrading (in Mexico) were found to have achieved net gains in technology adoption, worker training, management and quality-control practices.¹⁶¹

The same study considered impact evaluations of SME support programmes in four Latin American countries (Chile, Colombia, Mexico and Peru). It found 'generally positive and significant impacts for several (but not all) SME programmes in the countries reviewed'. All four country studies found statistically significant impacts of participation in any SME programme on sales, and on other measures of firm performance, varying by country. The study suggested that 'these findings imply that the pessimism of earlier SME program evaluations may have been largely due to the methodologies used'.¹⁶²

The recent **Independent Evaluation Group** review of World Bank support to SMEs notes that there has been a generally successful record for targeted SME projects. Of 47 IEG-reviewed projects during 2006-12, 85% achieved successful development outcomes, while business development services and other technical assistance projects had successful development outcomes in 84% of IEG evaluations over the same period.¹⁶³

A recent **ILO** review of SME support programmes notes that a large number of studies show that interventions lead to improved business practices (in the case of training initiatives) or income stabilisation (for measures promoting access to finance). Fewer studies show improvements in sales or profits and the majority of the studies do not show positive effects on employment.¹⁶⁴

Despite such reviews outlining successful outcomes from SME support programmes, support targeted at SMEs is not always the optimal policy. One reason is that not all programmes have been successful. Another is that there is often insufficient knowledge of what does, and does not work, due to a lack of rigorous documentation of such programmes. The Independent Evaluation Group of the World Bank states:

‘Although there is substantial evidence that systemic improvements in the business environment and the financial sector can promote growth by improving market dynamics and levelling the playing field, especially for SMEs, there is little rigorous evidence to support the positive (or negative) impact of targeted programs. There is no rigorous evidence on the economic impact of lines of credit, a little evidence to support partial risk guarantees, mixed evidence on private equity schemes in developing country contexts, and limited evidence of the benefits of matching grants and advisory services’.¹⁶⁵

The two main economic justifications for supporting SMEs are: to address market failures specific to this size segment; and to promote the special economic contributions they make, especially in creating employment. Yet while there is broad agreement about the existence of market failures, there are conflicting views on the special economic contributions made by SMEs.¹⁶⁶ Some analysts stress the importance of promoting a better investment climate rather than targeting support to companies, whether SMEs or not. Another view prevalent in the literature is that policy should focus on support to companies that create the most jobs, regardless of size, not necessarily SMEs. The ILO, for example, notes that because young, small enterprises have the highest employment growth rates, policy makers should target them. It states that, although most entrepreneurship development interventions in developing countries

focus on small enterprises and self-employed people, reflecting the desire to support the most marginalised, these interventions can have lower employment impacts than focusing on young, high-growth enterprises.¹⁶⁷

The importance of promoting an enabling business environment is clear. A review by the International Fund for Agricultural Development (IFAD) of its support to rural enterprises in four African countries notes a number of lessons learned in promoting an enabling environment for MSEs, some of which are likely to be relevant for SMEs:

‘To promote medium-sized enterprise (MSE) development, a conducive business environment must be created. This includes the formulation of appropriate MSE policies, the institution of appropriate structures to promote MSE development, the availability of the institutional capacity of government agencies to effectively deliver services to the private sector, an increased capacity of MSEs to leverage investment funds, an improved market information system and a national system of standardisation, certification and accreditation.’¹⁶⁸

Yet changing the enabling environment is complex and comprises various functional areas that affect business activity, including: simplifying business registration and licensing procedures; streamlining tax policies and administration; facilitating access to finance; adapting labour laws and administration; improving the overall quality of regulatory governance; improving land titles, registers and administration; simplifying and accelerating access to commercial courts and to alternative dispute-resolution mechanisms; broadening public-private dialogue processes, including the promotion of social dialogue; and improving access to market information.¹⁶⁹ To draw lessons from all these areas is too extensive a project for this report. However, the final section outlines specific lessons learned from some of the areas that emerge from the literature and experience, and makes some recommendations.

5. LESSONS LEARNED AND RECOMMENDATIONS

1. PROACTIVE GOVERNMENT POLICIES ARE NEEDED, NOT SIMPLY REGULATORY REFORM OF THE BUSINESS ENVIRONMENT

Governments can improve business enabling environments in various ways.¹⁷⁰ They can:

- set out a framework for economic transformation and growth
- regulate markets
- invest in infrastructure, social capital and labour skills, in gender-sensitive ways that promote women
- establish and enforce policies, regulations and legal frameworks
- develop and implement safeguards, including social safety nets, to protect the interests of the poor
- promote a transparent and inclusive business environment and practices.

Governments can also build the capacity of SMEs, for example, by providing vocational training, creating municipal-level agencies for SME start-up development and management and by encouraging SMEs to engage with large corporations.¹⁷¹

There is, by now, considerable evidence, especially from Asia, showing that successful economic and private-sector development has mainly been due to proactive policies by the state. In contrast to the 'low government regulation- approach' taken by most donors, such as the World Bank in their Doing Business project, and the 'investment climate'-reforms approach focused on facilitating foreign investment, SME development is likely best supported by a '**high government support-approach**'. Here, policies can include providing strategic guidance to companies, targeting specific investors, time-bound subsidies and trade protection, differentiated tax incentives, export promotion, R&D funds and information services. Policies can also support new and small firms, funded by taxpayers in the form of information, advice, training or finance, government assistance to enterprises to negotiate terms with large contractors, the provision of legal assistance and

model contracts, and increasing the voice of SMEs in policy making and consultations; most of these policies go far beyond the minimalist recommendations of Doing Business.¹⁷² A report by the German Development Institute concludes that these kinds of policies are likely to be more successful than those simply focused on deregulating the business environment since these 'are not appropriate to achieve high levels of innovation-oriented entrepreneurship.'

The Independent Evaluation Group of the World Bank notes that SME interventions must focus on leaving a sustainable supply of the service (whether financing, business development services or training) by establishing well-functioning markets and institutions, and that support should not simply focus on a temporary supply of benefits to a small group of firms during a project's lifespan.^{173, 174}

One aspect of the debate on this issue is who should pay for services to SMEs. The financial sustainability of SME support policies is a concern in much of the literature. In the past, many states (and donor agencies) provided services for free, and in many countries, SME support policies continue to be paid for out of general taxation. In Brazil, for example, the Micro and Small Business Support Service (SEBRAE) has a budget of \$1.8 billion and is the world's largest small business agency. It receives funding from the government via a special tax of between 0.3% and 0.6% levied on employers' payrolls; this tax not only funds the agency's programmes, but various government training initiatives.¹⁷⁵ State-funded services and support programmes can be argued to be critical since the market may not provide some services, SMEs themselves may not be able to afford to pay for such services and the benefits to broader society can be large. Yet many donor agencies argue that the provision of 'private' services by public officials can distort local markets, discourage the growth of indigenous management consulting services and encourage dependency on donor funding.¹⁷⁶

5. LESSONS LEARNED AND RECOMMENDATIONS

An IFAD report documents lessons learned from support to rural enterprises in Ghana, Rwanda and Senegal, focusing on projects providing business development services, financial services, project management and technology promotion. The study concludes that, for existing businesses, a demand-driven approach to enterprise development, where businesses pay for services, is effective in helping SMEs. For newer or more vulnerable businesses, however, direct targeting and assistance in establishing new SMEs is more appropriate.¹⁷⁷

2. LOCAL-LEVEL POLICIES ARE CRITICAL AND SUPPORT POLICIES SHOULD BE BASED ON LOCAL NEEDS

It is not only the business environment in the capital city that is important, but in other areas of the country, including rural areas. District assemblies and local authorities can play crucial roles in SME project implementation, coordination, financing and monitoring. According to IFAD:

‘Mainstreaming project activities into the local governance system commits governments through the local authority to provide the right environment, resources and support to medium-sized enterprise (MSE) development on a sustainable basis... Two crucial elements are strengthening local authorities by building their capacity to play their roles for MSE promotion and development and creating a conducive environment for sustainable rural MSE development’.¹⁷⁸

In Ghana, one policy contributing to the development of MSEs at local level, mandates all metropolitan, municipal and district assemblies to set up MSE subcommittees within the local governance structure.¹⁷⁹

IFAD’s review of support to rural enterprises also notes that using local service providers to deliver business development services is more economical and ensures sustainability after the life of the project.¹⁸⁰ Similarly, the Independent Evaluation Group of the World Bank states that, regarding the IFC’s advisory services, where local staff or their capable local partners had adapted products to local needs, the results were generally superior, whereas where staff simply pursued volume or replication through standard approaches, results sometimes suffered.¹⁸¹

3. GOVERNMENTS MUST STEP UP PUBLIC PROCUREMENT AND LOCAL CONTENT POLICIES AND ENSHRINE THESE IN LEGISLATION

As shown in our case study from Brazil, public procurement policies can have significant positive impacts on poor people and local economic development. Government procurement policies can provide valuable market opportunities for SMEs if they stipulate sourcing from smallholder farmers or small enterprises for supplies needed in schools, hospitals and other public institutions.¹⁸² A related policy is to enhance local content policies by requiring foreign and domestic investors to source their goods and services from domestic SMEs.

There is much greater scope for developing countries, especially in Africa, to increase their procurement and local content policies and to enshrine these into legislation. Currently, few African countries have explicit local content policies in place, though the number is rising. In the oil and gas sector, only one of the 48 least developed countries – Angola – has so far introduced explicit local content requirements.¹⁸³

When companies spend more on local inputs and employ more nationals, this tends to inject more money into local and national economies. For example, BG Group says it paid \$578m to suppliers from its Tanzanian operations in 2013, of which \$354m went to Tanzanian companies or international suppliers in Tanzania.¹⁸⁴ In Ghana, some analysts suggest the country will gain four times the amount of revenue from mining companies buying more local goods and services, than from their royalty payments.¹⁸⁵ However, in some countries, especially the poorest, local and

national markets for supplying key goods and services are very undeveloped. In these cases, even if companies want to procure locally, they are often unable to. This reinforces the need for governments to be proactive about developing SMEs to be able to service larger companies.

There are clear economic rationales for the use of local content requirements.¹⁸⁶ They can develop or strengthen the domestic industrial base, often promoting 'infant industries' that may become internationally competitive. They can encourage more value-added activities, especially in countries or sectors where investment activities have traditionally focused on enclaves, and only marginally benefitted the wider economy. Local content policies can also enable developing countries to learn, adopt and adapt technologies and production processes innovated elsewhere.¹⁸⁷

There is plenty of experience to draw on in promoting good local content policies. Brazil, for example, is an often-cited success story, whereby, until the 1990s, the state-owned Petrobras was the sole developer of all Brazilian oil and gas – but with licensing agreements with international firms allowing Brazilian suppliers to develop state-of-the-art technologies in an environment protected from overseas competition.¹⁸⁸

The capacity for governments to legislate and implement local and public procurement policies to support the development of SMEs must not be undermined by international trade agreements. Government procurement policies were not covered as part of the original World Trade Organization agreements, but since then, bilateral trade agreements have begun to stipulate that governments must open public procurement up to competition from transnational corporations. Much of the current debate around the controversial Transatlantic Trade and Investment Partnership (TTIP) centres on this issue and concerns that TTIP could become the model on which trade deals around the world are based, potentially limiting the policy space of developing world government.¹⁸⁹

4. VALUE CHAINS NEED TO BE IMPROVED TO BENEFIT SMEs

Promoting SMEs by linking them to large, often multinational, companies in value chains has become a common support mechanism in recent years. As UNCTAD has noted, TNC-SME business linkages are potentially one of the fastest and most effective ways of upgrading domestic enterprises, facilitating the transfer of technology, knowledge and skills, improving business and management practices, and facilitating access to finance and markets. Strong linkages can also promote production efficiency, productivity growth, technological and managerial capabilities and market diversification in local firms.¹⁹⁰

Such support can be provided in various ways. Governments can, for example, assist SMEs to negotiate better terms with larger contractors, provide legal assistance and model contracts, tackle the power of supply chains and the anti-competitive behaviour of large companies within them (such as supermarkets). More generally, they can help increase the voice and influence of SMEs in policy consultations.¹⁹¹ There are few evaluations of such TNC-SME linkages, however, and such schemes also pose challenges.¹⁹² Integrating small farmers' cooperatives into value chains dominated by large firms poses major risks and often leads to over-reliance on one customer, or islands of success, rather than raising the overall welfare of a sector.

At the same time, the terms of engagement involving an SME, often involving small farmers and a large corporation, are frequently unequal or exploitative.¹⁹⁴ Improving value chains may mean promoting inclusive business models. In agriculture, this is vital given the current prevalence of large-scale land acquisitions, sometimes land grabs, and public-private partnerships which undermine farmers.

5. LESSONS LEARNED AND RECOMMENDATIONS

Two recent reports consider the conditions under which small farmers and their organisations can benefit from supply chains. A key finding is the indispensable role of the state. A report for the Ford Foundation notes that the full benefits of value chains – whether provided via a third-party certified chain or based on private company standards and relationships – require private sector initiatives to be complemented by targeted investments in producers and communities. Investments are typically needed to upgrade producer skills, bolster producer organisations and intermediaries to meet market requirements (such as on quality, consistency, production standards and processing capacity), and enhance the rewards and/or reduce exposure to risks of participating in the chain (such as by increasing productivity and improving business skills).¹⁹⁴

The UN's High Level Panel of Experts on Food Security and Nutrition also highlights conditions needed for small farmers and their organisations to benefit from value chains:

- The value chain must be an inclusive process with the authorities, establishing a 'clear regulatory framework for contracts' between farmers and firms to reduce the power gap.
- Secured land tenure is essential.
- The presence of farmers' cooperatives and production groups must support small farmers in contractual schemes by increasing their bargaining power and provide a structure to receive services such as finance and technology extension.¹⁹⁵

5. GOVERNMENTS MUST PROMOTE A STEP CHANGE IN SUPPORT TO WOMEN-LED SMEs

The importance of women-led SMEs, and the particular barriers they face, has been noted already. Since women tend to be marginalised in society and the economy, supporting women-led SMEs is essential for promoting more inclusive development.

Yet few government SME support programmes appear to be targeted at women-led SMEs. A further problem is that those that have, have often been less successful. The ILO, for example, notes that access to finance and entrepreneurship training programmes targeting women appear to be less successful in terms of income generation

and employment creation. However, it adds that 'this should not be used as an argument to stop these interventions, since the results probably reflect the different goals of women entrepreneurs and the structural inequities they face'. The latter include women's lack of decision-making autonomy within the family, the additional requirements on their time and limited educational opportunities. 'Nevertheless', the ILO states:

'The findings do call for a rethinking of current approaches, especially on the need to overcome structural inequalities. The most recent evaluation results show that adding new design features to women's entrepreneurship programmes, such as mobile money services or in-kind capital, increases the decision-making autonomy of female entrepreneurs and improves business performance.'¹⁹⁶

One potential explanation for why support programmes for women entrepreneurs have weaker outcomes than those for men is that they rarely address the major constraints to female enterprise growth, such as concentration in low-productivity and low-growth activities, intra-household choices, the role of institutions, gendered norms and behaviour, and legal frameworks in shaping the business environment for women entrepreneurs. 'Addressing these constraints requires designing programs more holistically and combining instruments and services oriented to addressing these barriers'. Public perceptions also need to be addressed. 'It is critical for programs to try to change these narratives with public campaigns, events, and discussions with community leaders'. Support programmes need to engage with government institutions and chambers of commerce to reform legal frameworks that constrain female entrepreneurial activity.¹⁹⁷

Improving the business environment for women, specifically, is critical. A World Bank review of support programmes to women entrepreneurs suggests the need for more experimentation in the design and delivery of services, and engendering support programmes to address gender-specific constraints specifically; this includes paying greater attention to factors that induce women entrepreneurs to diversify into higher value-added activities. The review states ‘there is significant anecdotal evidence pointing towards the positive impact of mentoring and networking on women’s entrepreneurship activities’ and suggests that these services, in addition to education on business practices and technology extension services, can increase the effectiveness of programmes.¹⁹⁸

6. TAX POLICIES MUST HELP, AND NOT DISADVANTAGE, DOMESTIC, SMALL COMPANIES

In many developing countries, governments effectively favour large companies in their tax policies. At worst, governments lose massive revenues from tax exemptions, of which the main beneficiaries are often large companies. NGO studies suggest that tax incentives to large companies should normally be abolished or radically reduced; where they are provided, they could be made conditional upon companies sourcing inputs from local SMEs.¹⁹⁹ A UNCTAD report on Rwanda recommends that tax incentives be made available to all investors irrespective of their size, since Rwanda is more likely to attract SMEs.²⁰⁰ In El Salvador, credit and savings cooperatives that invest in MSEs are exempted from income tax due to the greater assumed social impact of these investments.²⁰¹

Many countries have differentiated tax rates for companies, with lower rates or exemptions for enterprises below a certain size. For instance, in Rwanda the SME tax regime includes a 3% tax on turnover for small taxpayers and four categories of fixed payments for micro-enterprise taxpayers. More generally, size-neutral tax systems may fail to take the context of SMEs into account. In some countries, for example in East Africa, taxes based on turnover are common, and provide an alternative to profit-based accounting.²⁰²

Agriculture and fishing are frequently given special treatment in national tax legislation. In India, agricultural cultivation is exempted from

income tax at the federal government level, while agricultural livestock producers are included in the tax system.²⁰³ Rwanda applies larger tax exemptions to agricultural companies than to non-farm-based enterprises, to make up for their disadvantaged position.²⁰⁴

While tax rebates for SMEs can compensate them for size-specific disadvantages, they can also create ‘size traps’ that disincentivise them from growing beyond a certain threshold. Transitioning from a turnover-based tax system to a profit-based tax system will involve a higher compliance cost - and usually the hiring of an accountancy firm. However, SMEs account for only a small share of tax revenues in many countries, and the administrative cost of collecting taxes from them can be higher than the potential additional tax revenue in both turnover and profit-based accounting systems - thus a high exemption threshold should be considered on these grounds as well. Countries could also adopt a more pro-poor tax policy by reducing taxes on SMEs which, while profit-orientated, also provide goods or services to the poor, such as social enterprises (see the Philippines case study). Overall, the right balance must be found between providing an enabling environment for SMEs and the need for governments to find substantial sources of taxation.²⁰⁵



Photo: Jars of honey produced by Bairunya Bee Keepers Association, Mount Kenya National Park. Christian Aid/Matthew Gonzalez-Noda

5. LESSONS LEARNED AND RECOMMENDATIONS

7. POLICIES THAT *COMBINE* DIFFERENT TYPES OF SME SUPPORT TEND TO WORK BETTER THAN SINGLE POLICIES

The need to combine policies, rather than regarding any single policy as a magic bullet, is a common finding in the literature on SME support programmes. For example, a report for Sweden's SIDA notes:

'The evidence in favour of providing support for entrepreneurship and investment in micro, small and medium enterprises suggests that providing non-financial business development services results in modest gains that are strengthened if dovetailed with access to finance initiatives and by targeting transformative enterprises'.²⁰⁶

CAFOD's *Thinking Small* work similarly found that successful NGO projects to support micro-entrepreneurs and small businesses did not focus simply on one improvement, but tackled all factors affecting the viability of such businesses – economic, social, political and human. CAFOD's rural livelihood projects not only identified market opportunities and supported viable economic activities, but organised communities to build and maintain local roads, generating shared ownership, social capital and political voice, as well as essential local infrastructure. CAFOD notes that successful projects tend to start with an analysis of what assets – natural, capital, social, human, economic – could be built on locally, rather than helicoptering in new, unrelated activities.²⁰⁷

CAFOD has outlined five guiding principles to address the priorities of small businesses:

- proactive interventions, rather than regulatory reform
- specific targeting of funds, advice or support interventions to small businesses
- understanding the role of society and power and the context in which people live

- being comprehensive and multi-dimensional rather than operating in silos
- undertaking locally appropriate interventions based on consultation and participation.²⁰⁸

8. ACCESS TO FINANCE NEEDS TO BE MORE COMPREHENSIVE

Some access-to-finance programmes for SMEs tend to have a narrow focus, simply providing credit lines to companies, yet a more comprehensive approach is often required. Access to credit is only one of the financial services that many SMEs require. Often just as important is physical access to financial services and banks and access to forms of insurance such as health insurance or, for farmers, weather insurance, but these may be unavailable or unaffordable, with women-led SMEs again the most disadvantaged.²⁰⁹

An IFAD review of support to rural enterprises notes a number of lessons learned as regards increasing access to finance. Alongside credit, the inclusion of savings instruments in financial packages can often better address the risk mitigation needs of MSEs by improving their access to capital and increasing resources available for further financial intermediation. Incorporating savings products into financial service delivery enables clients to accumulate internally generated funds for use in the future to allow them to become self-sufficient. Often, the provision of financial services must also be complemented with financial literacy education.²¹⁰ An important aspect of this is often tax literacy.

The importance of combining access to finance with other services is recognised in other reviews:

- A recent IFC meta-evaluation of projects supporting farmers concludes that most of the projects combined credit with training and technical advice, and sometimes with other interventions such as organising farmers to transport and market their crops to an exporter. 'The pattern suggests that provision of credit combined with training for the credit recipients is becoming a standard way of ensuring success'.²¹¹
- The ILO notes that interventions promoting entrepreneurship development through financial and non-financial support services can contribute to the creation of more and better jobs, and providing packages that combine access to finance with non-financial services

works better than standalone interventions, despite the latter still being common.²¹²

It is worth reiterating that many governments should prioritise SMEs in providing access to finance. The UN's Economic Commission for Latin America and the Caribbean (ECLAC) says that access to finance 'should target sustained productivity increases in small and medium-sized enterprises'. It adds that, since private banks tend either to favour larger enterprises or offer mostly short-term credit – to the detriment of long-term financing – for small companies, the strengthening of 'public development banking' is required. Public banks, ECLAC states, are 'in a better position to focus on financing investment and working capital for companies that do not have ready access to credit'.²¹³

A key is to promote systemic reforms of financial services. The IFC estimates that the World Bank's annual expenditure on financial on-lending is less than half of 1% of what is needed globally. Therefore, it is simply not credible to argue that donors can play a significant global role just by channelling finance through intermediaries or directly to SMEs. The key is to help build the capacity and sustained activity of a country's financial sector to supply SME credit demand. Projects should be designed to fix market failures – whether by building capacity, creating a demonstration effect, or stimulating competition, and focus on countries where the financial sector is weakest.²¹⁴

9. WORKER AND MANAGEMENT TRAINING AND LABOUR CONDITIONS NEED TO BE IMPROVED

A key aspect of the business enabling environment is labour conditions and skills, since these affect the ability of a society to create jobs, especially jobs that are well-paid, and improve firm productivity.

The importance of management training is a key aspect of the literature on supporting SME development.²¹⁵ For example, the UN Economic Commission for Africa's important 2005 report, *Unleashing the Private Sector in Africa*, calls not only for improving the business and investment climate and increasing access to finance but for enhancing management and business development in Africa through training and development programmes

(improving education, enhancing managerial skills, and promoting apprenticeships, and so on) and the creation of SME Development Centres.²¹⁶

A recent report for the UN Industrial Development Organisation identifies the following four reasons why MSEs in Africa do not grow: lack of knowledge of book-keeping skills and market analysis, leading to weak business plans; lack of planning; lack of market information; and the absence of market research in establishing a business (with many established based simply on personal experience). It concludes by calling for greater investment in human capital and management and technical training, notably by targeting education and training support to indigenous firms (for example, in business management techniques), alongside providing greater access to finance and business development services.²¹⁷

There is a growing literature evaluating the impacts of business training. The ILO has noted that few studies have been able to provide persuasive evidence that training leads to improved performance such as increased productivity.²¹⁸ In its review of what works, the ILO states that, of the training interventions in developing countries that it assessed, 40% showed significant positive effects on employment, while the remaining 60% did not. It also points out that combining entrepreneurship training with access to finance works better than standalone interventions. Programmes for young people are more likely to have positive results, possibly because there is a greater shortage of entrepreneurial skills in this age group than in others, so the impact is higher.²¹⁹

Regarding programmes to improve working conditions and SME productivity, the same ILO review's key finding is that a systemic approach is needed that integrates working conditions into the core operations of a business; this produces better results than standalone interventions that seek to improve a single aspect of working conditions. The ILO adds that there is considerable evidence that the introduction of modern management practices leads to higher firm productivity, and ultimately to better working conditions.²²⁰

Businesses, including SMEs, play an important role in promoting corporate accountability and

5. LESSONS LEARNED AND RECOMMENDATIONS

responsible business behaviour in line with the *UN Guiding Principles on business and human rights* (UNGP). Adhering to these guidelines contributes to preventing, managing and mitigating negative human rights impacts on their operations, including in their supply chains. The European Commission has published a guide for SMEs on how to implement the *UNGP* (2012) and a toolkit for integrating CSR in practice (2013) to provide practical guidance.²²¹ The guide sets out six steps for respecting human rights and outlines the key questions to consider, in terms of human rights in various business activities.

A finding from some research is that the economic sector in which an SME operates has a stronger influence on the quality of employment than the size of the enterprise.²²² Thus, it might be more effective to focus support policies on specific sectors rather than on enterprise-size segments when designing interventions to improve the quality of employment. But, as the ILO has argued, the finding that the quality of employment is lower in SMEs should not lead to abandoning SME promotion; SMEs' contribution to job creation is too important. Instead, the objective should be to support SMEs to increase productivity and improve the quality of jobs.²²³

An ILO literature review evaluating the state of knowledge on the relationship between practices relating to employee voice, working conditions, safety and health, skills development and to positive outcomes in SMEs, notes that much evidence confirms a link between provision of operational safety and health and positive firm outcomes. This includes many studies that focus on practices, tools and techniques, that treat operational safety and health as an essential aspect of good business practice and quality management.²²⁴

More generally, a recent report for the UN notes that evidence suggests that to be effective at creating more good jobs, targeted programmes would need to act in one or more of the following ways: by increasing the survival rate of small firms; by accelerating the growth rate of surviving firms; or by closing the wage gap between small and large enterprises.²²⁵

10. APPROPRIATE INFRASTRUCTURE IS CRITICAL AND NEEDS TO BE PROVIDED - INCLUDING IN RURAL AREAS

Lack of electricity is often identified as a constraint to the growth of SMEs. In CAFOD's research with micro- and small-business owners, participants also mentioned the need for good roads and transport services, access to water and irrigation, telecommunications, storage facilities and toilet and hygiene services. They highlighted the need for physical markets that are properly equipped and well located to meet business needs. These infrastructure and public services need to be provided within a 'thinking small' framework that specifically targets the needs of small businesses, since too often services such as this are size-blind.²²⁶

One estimate is that closing Africa's infrastructure gap will require around \$93bn a year, around 15% of the region's entire GDP;²²⁷ however, it is not clear whether this includes the 'small' and rural infrastructure needed by many SMEs, as noted above. Until quite recently, Africa's traditional donors have shown little willingness to finance infrastructure, although China is financing many projects building large roads.²²⁸ Many governments prioritise urban areas in their infrastructure investments, yet improvements in rural infrastructure are critical to farming cooperatives and rural-based enterprises. More, and better, feeder roads are especially important in rural areas, linking farmers to markets.²²⁹

11. THE VOICE AND INFLUENCE OF SMEs IN POLICY MAKING MUST BE INCREASED

It is critical for governments to support the organisation of SMEs into associations and to listen more to, and actively seek to consult with, SMEs in order to involve them more in policy making. Often, business associations, including Chambers of Commerce, are dominated by large companies that subsequently have the ear of government. SMEs can sometimes partner with trade unions, and civil society organisations, to strengthen their bargaining position on issues of common interest.²³⁰

12. CURBING CORRUPTION HAS PARTICULAR BENEFITS FOR SMEs AND SHOULD BE ADDRESSED

While improvements in the fight against corruption help businesses of all sizes, some policy measures have particular relevance to SMEs. As DANIDA has noted, certain funds could be made available to allow SMEs to go to court and claim damages caused by corrupt practices involving public officials. In cases where SMEs suffer financial or other economic damage as a result of corruption, measures must be taken to ensure they can initiate legal proceedings against those responsible to obtain compensation. These, and other measures that assist SMEs in funding legal processes, constitute an incentive to SMEs to use existing mechanisms in the justice system.²³¹



Photo: Dried hibiscus petals produced by members of the Hibiscus cooperative in Nicaragua. Christian Aid/Paula Plaza

IN SUMMARY, OUR RECOMMENDATIONS ARE:

1. Proactive government policies are needed, not simply regulatory reform of the business environment
2. Local-level policies are critical and support policies should be based on local needs
3. Governments must step up public procurement and local content policies and enshrine these in legislation
4. Value chains need to be improved to benefit SMEs
5. Governments must promote a step change in support to women-led SMEs
6. Tax policies must help, and not disadvantage, domestic, small companies
7. Policies that combine different types of SME support tend to work better than single policies
8. Access to finance needs to be more comprehensive
9. Worker and management training and labour conditions need to be improved
10. Appropriate infrastructure is critical and needs to be provided – including in rural areas
11. The voice and influence of SMEs in policy making must be increased
12. Curbing corruption has particular benefits for SMEs and should be addressed.

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