



# Financial System Strategy 2020



## **FSS 2020 International Conference** **“SME Issues, Challenges and Prospects”**

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# SMEs – The Issues

**Two Dynamic Indicators are of particular interest:**

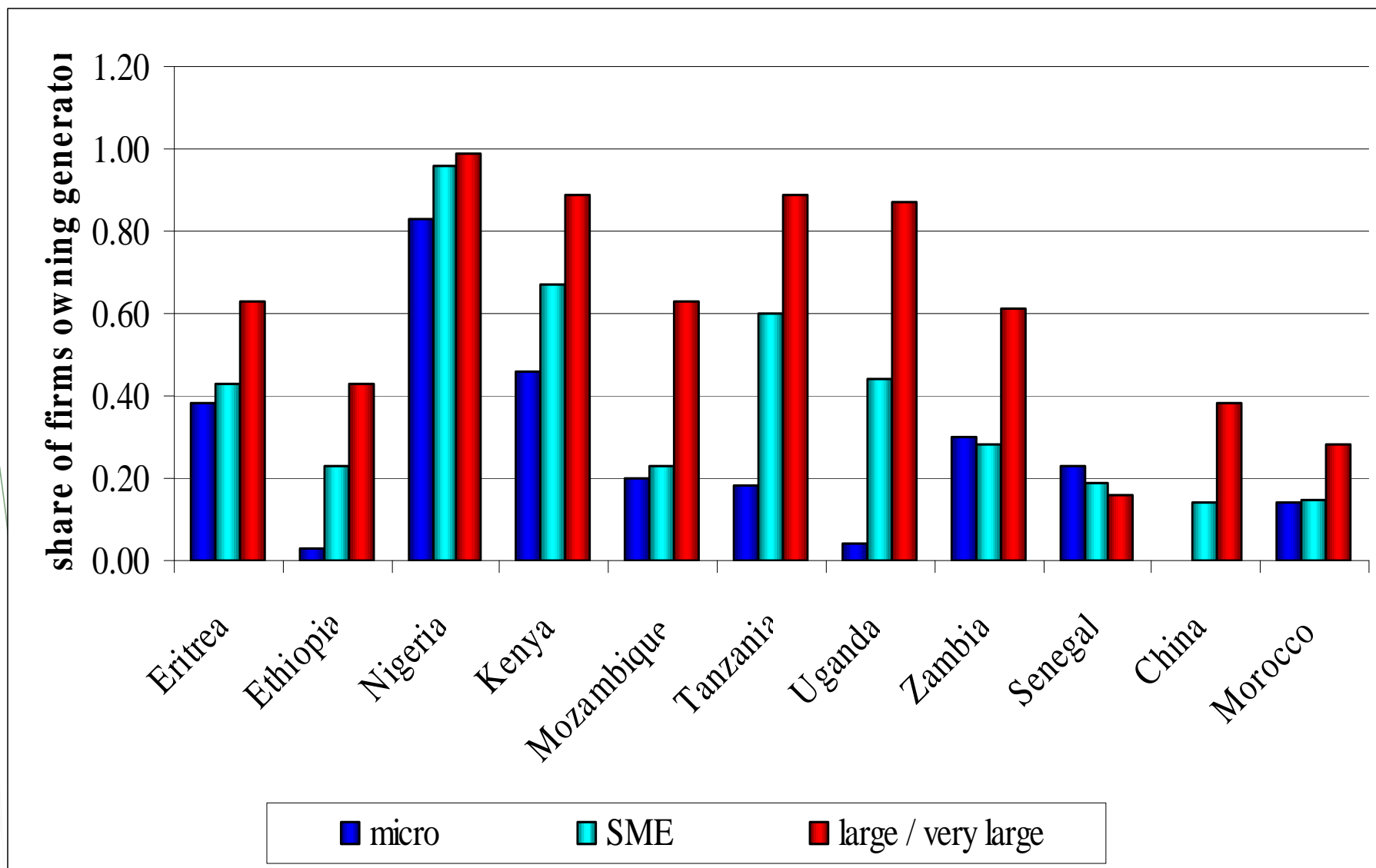
- **Transformation** of micro and informal firms in formal firms
- **Growth** of small and medium firms into globally competitive firms
- Why do these measures matter:
  - ✓ SMEs are the single largest source of employment in economies. Formalisation increases SME access to services and capacity for employment creation
  - ✓ Firms that grow or link to international value chains increase technology absorption and create major spillover effects in the economy
  - ✓ SMEs play a key social inclusion role in strengthening stakeholding and voice in the economy.
- But what **Constrains** transformation and growth ?



# **The SME Challenges – Africa and The World**

- **Evidence drawn world-wide from Enterprise Surveys, “Doing Business” assessments and value chain analysis suggest the following:**
  - ✓ **“factory-floor” productivity in Africa is not that low compared with China**
  - ✓ **When broader set of investment climate variables are factored into costs, Africa’s productivity falls to very low levels**
  - ✓ **Small and indigenous firms face greater constraints**
- **Four key aspects of the “broader” investment climate in Africa are consistently highlighted as constraints to productivity improvements and growth:**
  - ✓ **Infrastructure**
  - ✓ **Access to Finance**
  - ✓ **The Regulatory Burden**
  - ✓ **Training and Education**

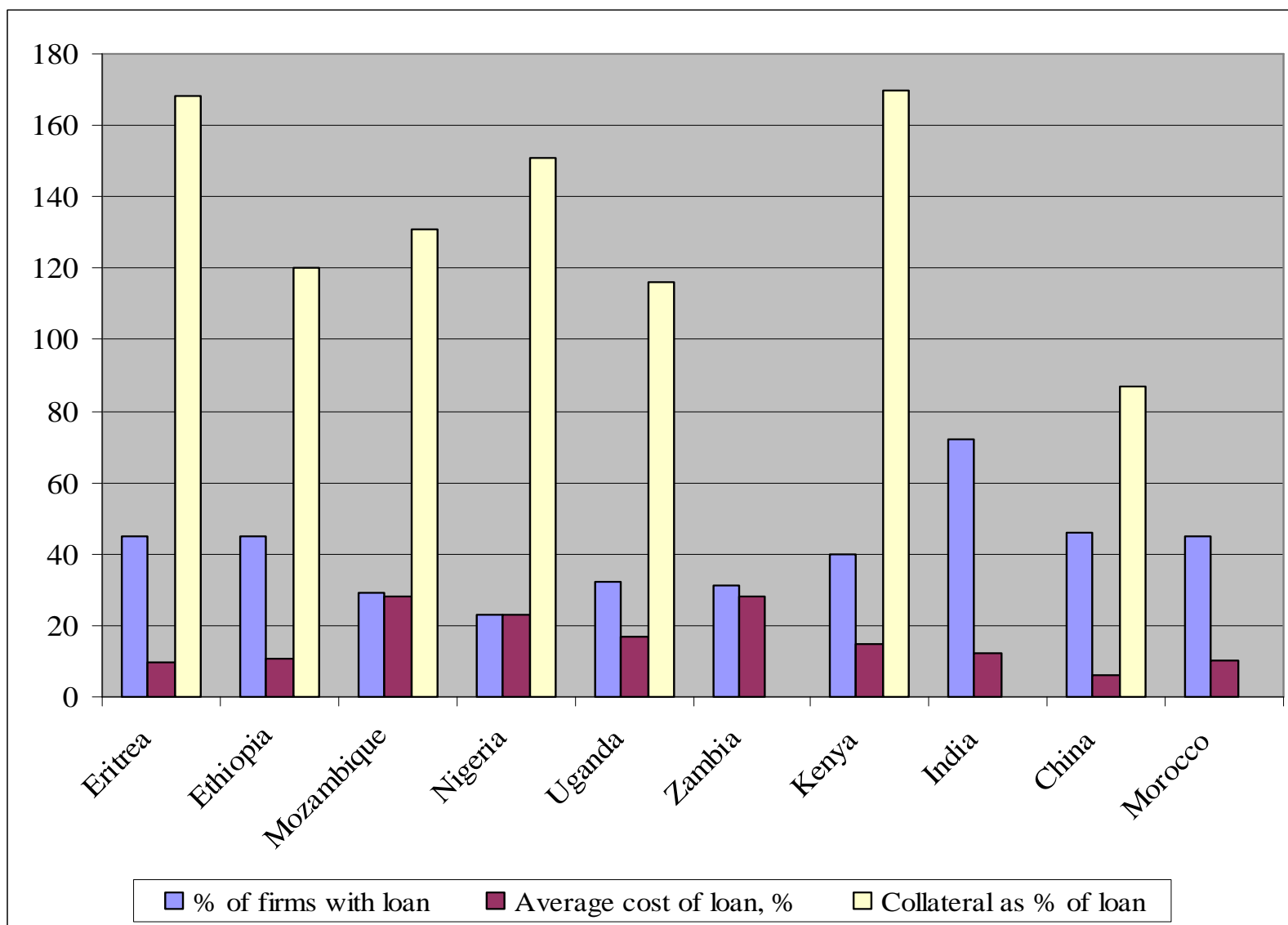
## Infrastructure - and small firms are less likely to own generators



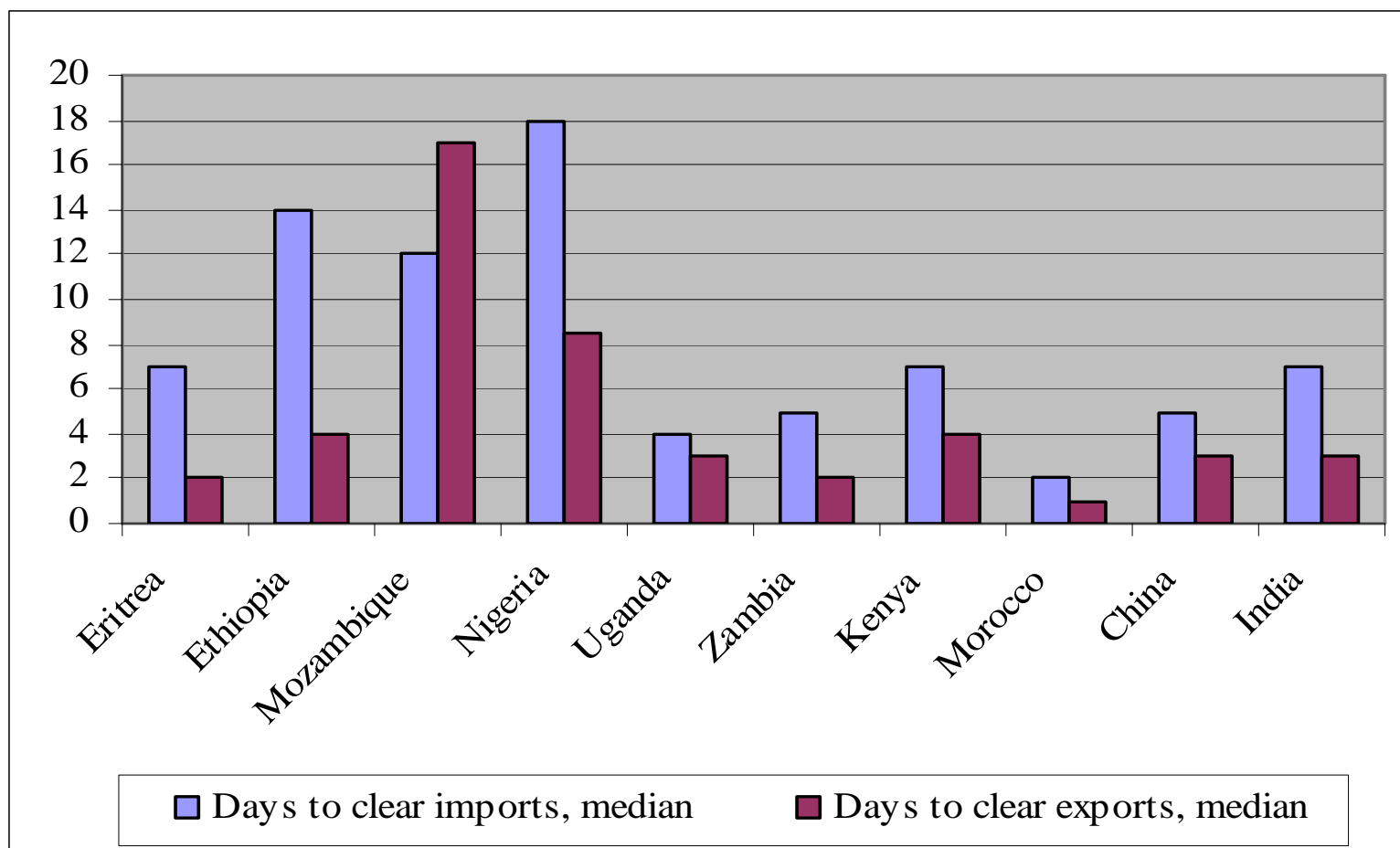


# Access to Finance (A2F)

## Cost and Collateral Constraints

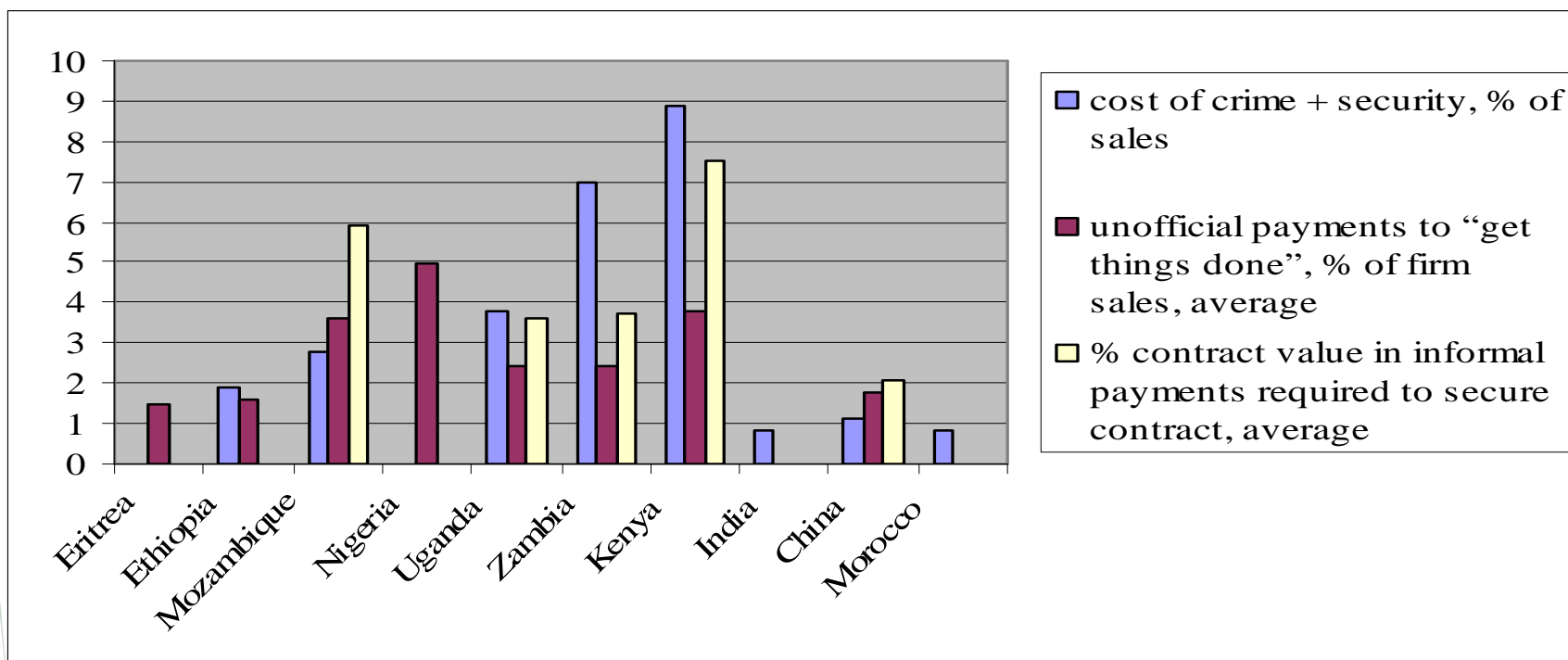


## Regulatory Environment – Port clearance is several days in many countries in Africa



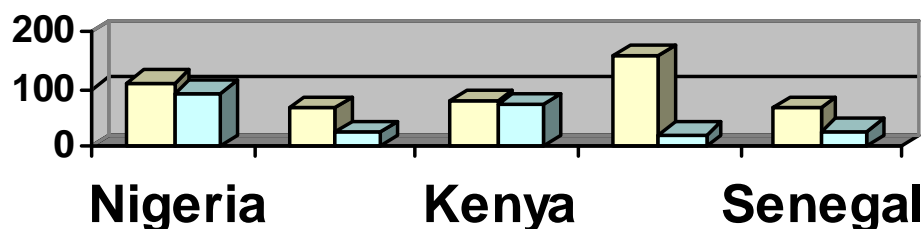
# Regulatory Environment - The cost of “getting things done” and “preventing things from happening”

## Unofficial and Informal Payments



## EDUCATION AND TRAINING

Indigenous entrepreneurs with a university education are more successful in business, but many do not have access to this type of education.. And there is minimal on-the-job training to compensate...

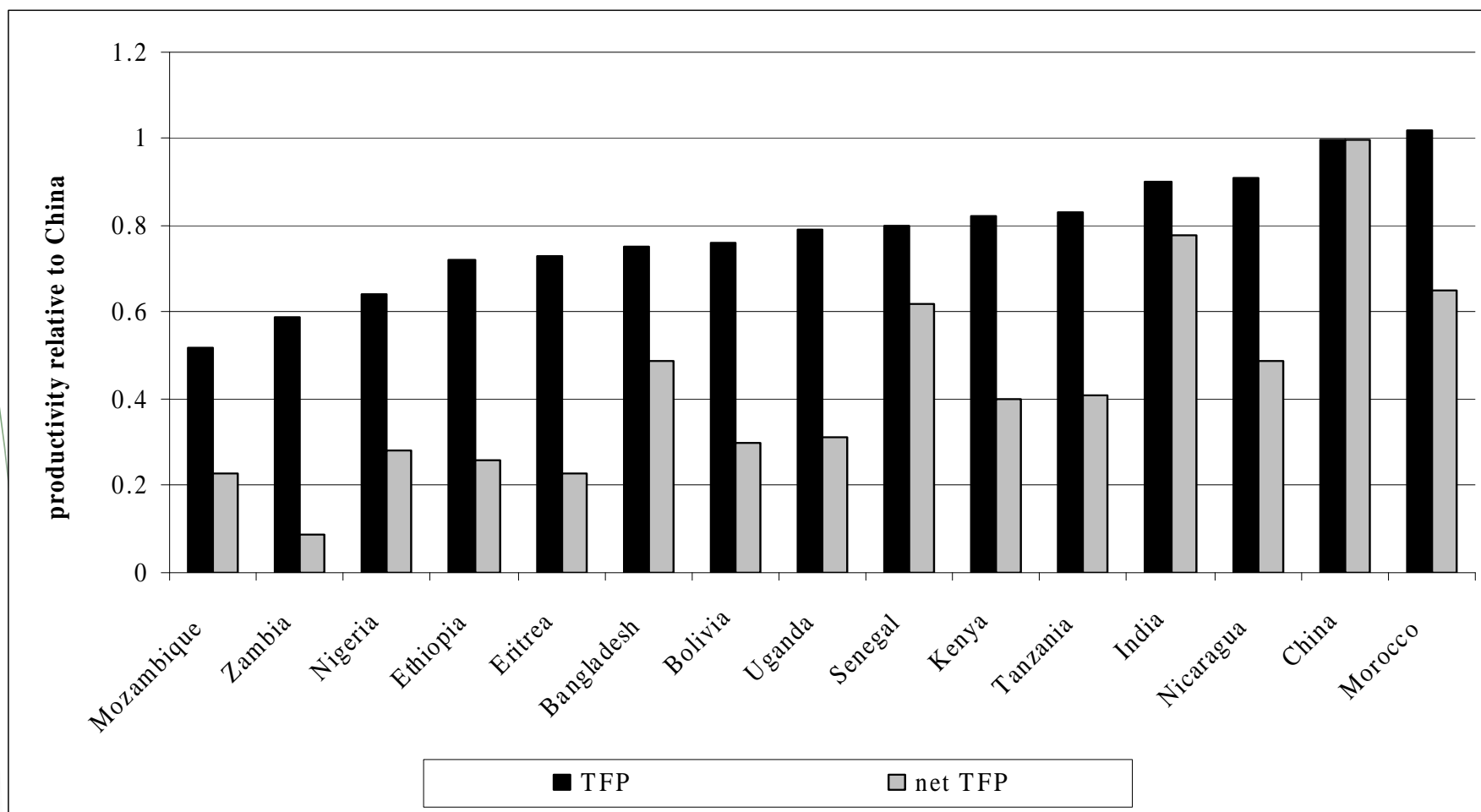


African w/ University degree
  African w/o University degree

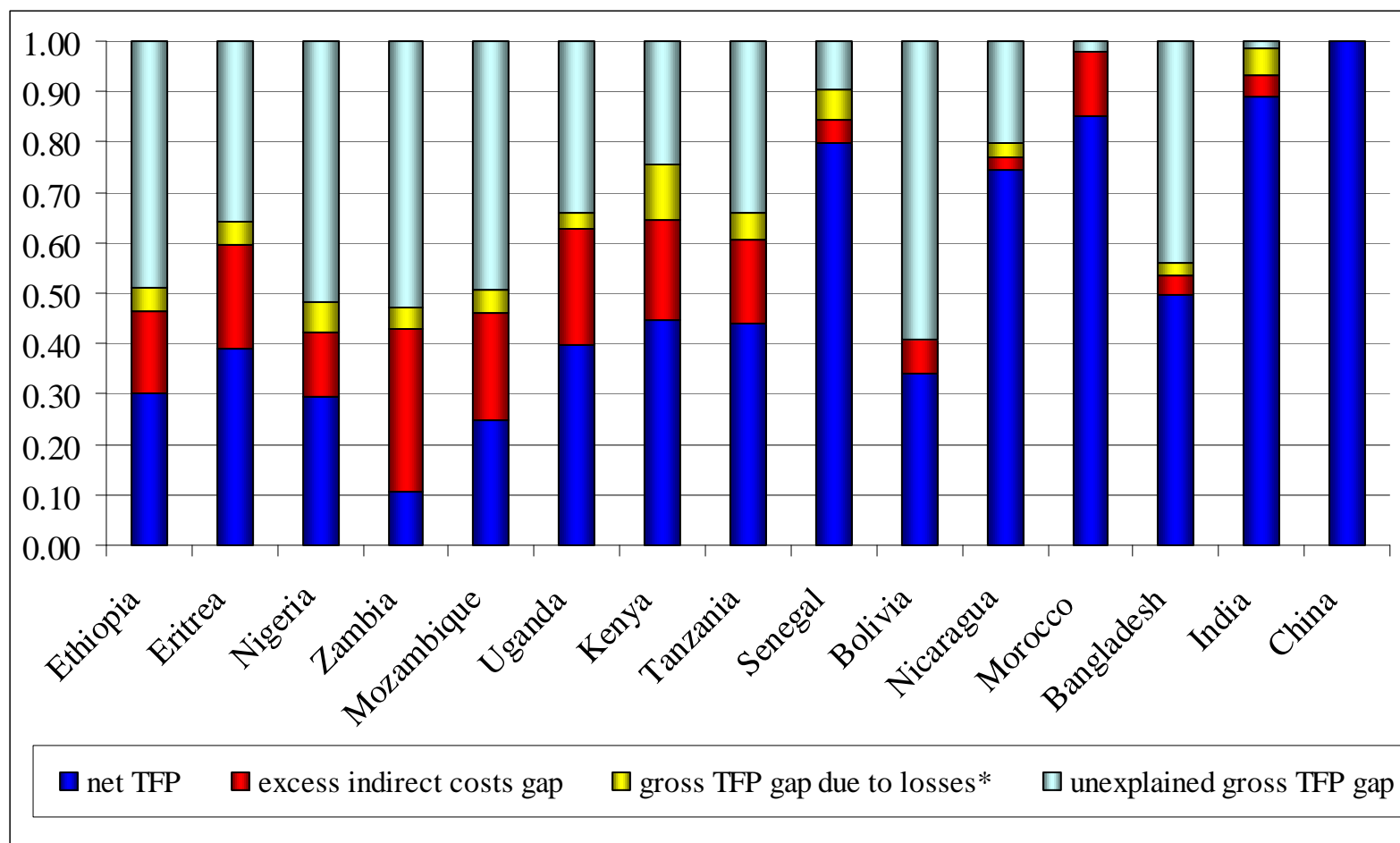


And “net” productivity is much lower than “factory floor” productivity due to high costs of doing business.

### Basic (factory floor) vs. Net TFP



## The decomposition of gaps in productivity shows that African firms are sharply disadvantaged relative to China due to higher indirect costs



\*due to power losses, delivery delays, shipment losses, crime



# The SME Sector Prospects

- **Overall Nigeria (2001) total productivity deficiency arising from indirect factors relative to China (2003) amount to approximately 70% (data- to be updated in 2007/8)**
- **And the situation for smaller and indigenous firms is consistently worst for the same set of constraints.**
- **The solutions rest in a combined set of actions along the lines presented in the FSS 2020 work on SME development:**
  - ✓ **policy and infrastructure - policies, laws, infrastructure**
  - ✓ **market development - market intermediaries that service the private sector**
  - ✓ **targeted interventions - value chain\clusters, enterprise**
- **The pitfalls revolve around choices to be made regarding implementation options, priorities\sequencing, coordination.**



# The SME Sector Prospects – Policy and Infrastructure Actions

- **Policy and infrastructure actions to mitigate risk and costs that SME sector cannot internalise:**
  - ✓ **Macro-economic stability and predictability - including market interest and exchange rate**
  - ✓ **Infrastructure and regulatory oversight - prices, service standards**
  - ✓ **Legal and administrative – including tax administration and licensing, secured transactions, market information - credit bureaus and property titling**
- **Pitfalls in achieving anticipated outcomes:**
  - ✓ **implementation options: government capacity and political will**
  - ✓ **coordination: public sector departmental cooperation and public-private partnerships for relevance, ownership and sustainability**



# The SME Sector Prospects – Market Development

- **Market development work**
  - ✓ **Best-practice knowledge transfer** - to develop commercial intermediaries to provide different financial and non-financial services (eg downscaling commercial banks, launch MFIs)
  - ✓ **Technology innovations** - eg mobile banking, on-line government e-services (customs) to reduce costs and rent-seeking
  - ✓ **Product Innovation** – market solutions to market failures (partial credit guarantees for banks, upstream performance grants for new MFIs, angel capital mechanisms for enterprise start-ups)
- **Pitfalls:**
  - ✓ **implementation options:** delegate to the private sector
  - ✓ **priorities\sequencing:** Respect the incentive and cost environment created by policy and infrastructure platform
  - ✓ **coordination:** making market work for enterprises requires demand-driven interventions to avoid dependency and ensure sustainability



# The SME Sector Prospects – Targeted Interventions

## ➤ Targeted interventions:

- ✓ Industry value chains with viable commercial potential (eg: Indian IT industry)
  - ✓ Business linkages and outsourcing
  - ✓ Financial products – “factoring” and “embedded” financing
  - ✓ Training and skills development – industry-based
- ✓ Special Enterprise Zones and Export-Free Zones

## ➤ Pitfalls:

- ✓ implementation options: Tendency to be public sector led and supply driven.
- ✓ priorities\sequencing: targeted interventions is not alternative to longer term policy and market development challenges.
- ✓ coordination: Has potential to build vested interests that are not in the broader economy or public interest



# The SME Sector Prospects – Concluding Remarks

- **Identifying solutions is the easier part. Implementation is the key challenge.**
- **Implementation, Sequencing and Coordination in circumstances of government or market failure - which characterizes the SME sector - requires heightened monitoring:**
  - ✓ **Benchmarking and metrics is key to performance and results**
  - ✓ **The indicators need to be measurable and carry incentives and sanctions linked to performance**
- **If you cannot identify clear measures for results and accountabilities for action, probably will not be implemented successfully.**