

**6.11. Presentation on the conducive policy, legal and institutional framework that help to strengthen foundations for the development of private sector with a special focus on SMEs – a Sri-Lankan perspective by Mr. Ranel T. Wijesinha, Consultant**

<p><b>Unleashing Entrepreneurship: <i>Making Business Work for the Poor</i></b></p>
<p><b>Presentation on Conducive Policy, Legal and Institutional Framework that helps to strengthen foundations for the development of the Private Sector with special focus on SMEs</b></p> <p><i>- a Sri Lankan Perspective</i></p>
<p><b>Contents:</b></p> <ul style="list-style-type: none"> <li>• Key Considerations of the Report of the UN Commission on ‘Unleashing Entrepreneurship: Making Business Work for the Poor’ – <i>Viewed from a South Asian Perspective</i></li> <li>• The Report’s Relationship to The Global Challenge - <i>Millennium Development Goals</i></li> <li>• Leveraging the Market at the Bottom of the Pyramid</li> <li>• Framework to Evaluate Policy Legal and Institutional Environment <i>- At a South Asian Regional Level</i></li> <li>• Doing Business in South Asia <i>- A Review of a recent World Bank publication</i></li> <li>• Sri Lanka – <i>A macro overview from a poverty alleviation perspective</i></li> <li>• Sri Lanka – <i>An Overview of the SME Environment</i></li> <li>• Sri Lanka – <i>Recent Policy Developments and Actions</i></li> <li>• Unleashing Entrepreneurship through Empowerment of SMEs: <i>A possible framework for an Action Plan for Sri Lanka / South Asia</i></li> </ul>
<p><b>Framework to Evaluate Policy Legal and Institutional Environment</b> <i>- at a South Asian Regional Level</i></p> <ul style="list-style-type: none"> <li>• The purpose of a frame work is: <ul style="list-style-type: none"> <li>○ First, to help evaluate policy and strategy gaps, institutional and infrastructural gaps, statutory and regulatory deficiencies which constrain private sector development</li> <li>○ Secondly, the outcome of the evaluation can be used as a basis to strengthen foundations for a conducive environment</li> <li>○ Several frameworks and a variety of criteria have been adopted by several institutions such as the World Bank, ADB and the World Economic Forum – Global Competitiveness Rankings (WEF – GCR)</li> <li>○ The limited time for preparation of this presentation did not permit an evaluation of the merits and demerits of each approach</li> <li>○ The WEF – GCR conducted since year 2000, provide comprehensive basis</li> <li>○ These rankings however provide only a general indication of the Degree of Overall Competitiveness of Nations and gaps in ranking in relevant areas.</li> <li>○ A detailed review of such areas, will be necessary for development of national level strategies and action plans.</li> </ul> </li> </ul>
<p><b>Framework to Evaluate Policy Legal and Institutional Environment</b></p> <ul style="list-style-type: none"> <li>• The WEF – GCR recognizes that Competitiveness is the medium through which Nations will achieve economic progress. National Competitiveness however is a function of the macro and micro policy related environment and related Legal or Statutory and Regulatory Institutional environment <u>and</u> simultaneously the effectiveness of the Private Sector and SMEs</li> <li>• The simple version of WEF – GCR (year 2000 Trial Survey for Sri-Lanka) ) identifies eight broad factors of competitiveness</li> </ul>

- Openness
- Government
- Finance
- Infrastructure
- Technology
- Management
- Labour
- Institutions

**Framework to Evaluate Policy Legal and Institutional Environment**  
 - *Factors of Competitiveness*

- Openness:
  - Measures openness to foreign trade and investment, openness to foreign direct investment and financial flows, exchange rate policy and ease of exporting

**Framework to Evaluate Policy Legal and Institutional Environment**  
 - *Factors of Competitiveness (contd)*

- Government
  - Measures the role of the state in the economy. This includes the overall burden of Government expenditures, fiscal deficits, rates of public savings, marginal tax rates and the overall competence of the civil service

**Framework to Evaluate Policy Legal and Institutional Environment**  
 - *Factors of Competitiveness (contd)*

- Finance
  - Measures how efficiently the financial intermediaries channel savings into productive investment, the level of competition in financial markets, the perceived stability and solvency of key financial institutions, levels of national savings and investment, and credit ratings given by outside observers

**Framework to Evaluate Policy Legal and Institutional Environment**  
 - *Factors of Competitiveness (contd)*

- Infrastructure
  - Measures quality of roads, railway ports, telecommunications, cost of air transportation and overall infrastructure investment
- Technology
  - Measures computer usage, the spread of new technologies, the ability of the economy to absorb new technologies and the level and quality of research and development

**Framework to Evaluate Policy Legal and Institutional Environment**  
 - *Factors of Competitiveness (contd)*

- Management
  - Measures overall management quality, marketing, staff training and motivating practices, efficiency of compensation schemes and the quality of internal financial control systems

**Framework to Evaluate Policy Legal and Institutional Environment**  
 - *Factors of Competitiveness (contd)*

- Labour
  - Measures the efficiency and the competitiveness of the domestic labour market.

It combines a measure of the level of a country's labour costs relative to international norms, together with measures of labour market efficiency (e.g. obstacles to hiring and firing workers), the level of basic education and skills and the extent of distortionary labour taxes

**Framework to Evaluate Policy Legal and Institutional Environment**

- *Factors of Competitiveness (contd)*

- Institutions
  - Measures the extent of business competition, the quality of legal institutions and practices, the extent of corruption and vulnerability to organized crime

**Framework to Evaluate Policy Legal and Institutional Environment**

- *Factors of Competitiveness (contd)*

- Each of the above 8 Factors of Competitiveness has 10 - 15 specific sub-criteria under which each broad factor of competitiveness is then evaluated and ranked
- To facilitate discussion and to provide a basis for an Action Plan for the UNDP and Partner Institutions the Sub-Criteria used to evaluate the factor of Competitiveness – FINANCE are set out in the next slide as an example

**Framework to Evaluate Policy Legal and Institutional Environment**

- *Factors of Competitiveness (contd)*

FINANCE :

- |  |  |
|--|--|
| 1. Sophistication of Financial Markets | 8. Interest Rate controls                |
| 2. Access to credit                    | 9. Interest Rates                        |
| 3. Domestic Banks                      | 10. Bond Markets                         |
| 4. Access to External Finance          | 11. Stock Markets                        |
| 5. Loan Availability                   | 12. Hostile Takeovers                    |
| 6. Soundness of Banks                  | 13. Venture Capital                      |
| 7. Entry into Banking Industry         | 14. Financial Regulation and Supervision |
|  | 15. Insider Trading                      |

**Framework to Evaluate Policy Legal and Institutional Environment**

- *at a South Asian Regional Level (contd)*

- Comments on the framework adopted by the WEF to evaluate National Business Environments
  - This framework has a number of sub items of criteria at National Level and also firm level since it is firms who compete in local and global markets
  - The framework is a comprehensive basis for strengthening foundations at National Level for Private Sector Development and Entrepreneurship as well as Repositioning National or Resident Multinational Enterprises to compete in global markets
  - A discussion of all of these and / or adoption of these exhaustive criteria is outside the scope of this presentation.
  - Research conducted for the purpose of this presentation reveals that a parallel focus on private sector development regardless of size combined with SME development through overall National Level Policy, Strategy, Institutional and Legal and Regulatory reform – will be a complex and formidable task.
  - Accordingly it is recommended that SME development through Unleashing Entrepreneurship at SME level be undertaken under a separate Agenda. This will enable early results and credibility for the Initiatives by achievement of necessary milestones on the challenging journey to achieve Millennium Development Goals relating to Poverty Alleviation.

**Doing Business in South Asia**

- A Review of a recent World Bank publication

- Doing Business in 2005: Removing Obstacles to Growth, a World Bank publication investigates the scope and manner of regulations that enhance business activity and those that constrain it.
- Two types of indicators:
  - First, measures of actual regulations
  - Second, measures of regulatory outcomes
- The analysis has direct relevance for policy reform
- Enables policy makers to understand better how particular laws and regulations affect employment, access to credit, the size of the informal economy, entry of new firms, corruption, and poverty.

**Doing Business in South Asia**

- A Review of a recent World Bank publication

- Starting a Business: Entry Regulations
- Hiring and Firing Workers: Employment Regulations
- Registering Property: Regulations of Property Transfers
- Getting Credit: Legal Rights and Credit Information
- Protecting Investors: Corporate Governance
- Enforcing a Contract: Court Efficiency
  
- Closing a Business: Bankruptcy
- The data set covers 145 economies

**Doing business – Entry Regulations**

South Asia compared to the Global Best

- Time taken to start a business:
  - India – 89
  - Bhutan – 63
  - Sri Lanka – 50
  - Bangladesh – 35
  - Pakistan – 24
  - Nepal – 21
  - Australia – 2

**Doing business – Entry Regulations**

South Asia compared to the Global Best

- Cost to start a business (Percentage of GNIpc):
  - Bangladesh – 91
  - Nepal – 74.1
  - India – 49.5
  - Pakistan – 36
  - Bhutan – 11
  - Sri Lanka – 10.7
  - Denmark – 0

**Doing business – Employment Regulations**

South Asia compared to the Global Best

- Rigidity of Employment Index:
  - Bhutan – 49
  - Pakistan – 49
  - India – 48
  - Nepal – 44

- Sri Lanka – 40
- Bangladesh – 24
- Hong Kong, China – 0

**Doing business – Employment Regulations**

South Asia compared to the Global Best

- Firing Cost (Weeks):
  - Sri Lanka – 108
  - Bhutan – 99
  - Nepal – 90
  - Pakistan – 90
  - India – 79
  - Bangladesh – 47
  - New Zealand – 0

**Doing business – Registering Property**

South Asia compared to the Global Best

- Time to register property (days):
  - Bangladesh – No data
  - Nepal – No data
  - India – 67
  - Sri Lanka – 63
  - Pakistan – 49
  - Bhutan – 44
  - Norway – 1

**Doing business – Registering Property**

South Asia compared to the Global Best

- Cost to register property (Percentage of property value):
  - Bangladesh – No data
  - Nepal – No data
  - India – 13.9
  - Sri Lanka – 5.1
  - Pakistan – 4.2
  - Bhutan – 1
  - Saudi Arabia – 0

**Doing Business – Getting Credit: Legal Rights & Credit Information**

- Legal Rights Index
  - Bangladesh – No data
  - Bhutan – No data
  - Sri Lanka – 3
  - India – 4
  - Nepal – 4
  - Pakistan – 4
  - UK – 10

**Doing Business – Corporate Governance**

- Disclosure Index
  - Bhutan – 1
  - Bangladesh – 3
  - Nepal – 3
  - India – 4
  - Pakistan – 4
  - Sri Lanka – 4
  - UK – 7

**Doing Business – Enforcing Contracts: Court Efficiency**

- Time to enforce a contract (days):
  - Sri Lanka – 440
  - India – 425
  - Pakistan – 395
  - Bangladesh – 365
  - Nepal – 350
  - Bhutan – 275
  - Tunisia – 27

**Doing Business – Enforcing Contracts:**

- Cost to enforce a contract (Percentage of GNIpc):
  - Bhutan – 113.8
  - India – 43.1
  - Pakistan – 35.2
  - Nepal – 25.8
  - Sri Lanka – 21.3
  - Bangladesh – 21.3
  - Norway – 4.2

**Closing a Business – Bankruptcy:**

- Time to go through insolvency (years)
  - Bhutan – no practice
  - India – 10
  - Nepal – 5
  - Bangladesh – 4
  - Pakistan – 2.8
  - Sri Lanka – 2.2
  - Ireland – 0.4

**Closing a Business – Bankruptcy:**

- Recovery Rate (Cents on the Dollar)
  - Bhutan – 0
  - India – 12.5
  - Bangladesh – 23.2
  - Nepal – 25.8
  - Sri Lanka – 33.1
  - Pakistan – 38.1
  - Japan – 92.4

**Sri Lanka**

*Key Considerations – from a poverty alleviation perspective*

- Since 1977 we began several strategies to introduce a market economy -27 years ago.
- Export Processing Zones were established
- We adopted an export led growth strategy given our small domestic market and attracted FDI
- In 1989 a major programme of privatisation began
- Per Capita Income at US\$947 and literacy rates today are higher than other countries in South Asia
- However, income and wealth disparities are high
- Regional disparities of income and wealth are a challenge to any Government

**Sri Lanka**

*Key Considerations (contd)*

- For example the Western Province generates 46% of GDP while other provinces contribute less than 10% except North Western Province which contributes 11%
- The North Central Province and the Uva Province generate only 4%.
- While the contribution or dependence on agriculture (with its attendant exposure to commodity price cycles) has reduced from 42% in 1960 to 20% in 2003 and the contribution of Industry to GDP improved from 17% in 1960 to 26% in 2003, the neglect of agriculture and agri-business has deprived a large number of persons at district and village level from realizing their full potential

**Sri Lanka***Key Considerations (contd)*

- The country is substantially dependent on textile, wearing apparel, leather products and tourism for export earnings and employment.
- But yet 35% of those in employment are in the agricultural sector
- A significant proportion of foreign inward remittances essential for stability of exchange rates, interest and inflation rates, are from low skilled workers in the Middle East
- Government investment in Economic and Social Infrastructure – as a percentage of GDP has declined
- The country does not have a National Social Security system.
- Economic growth and expansion in investment on currently projected scales will be insufficient to absorb the new entrants to the labour market of about 125,000 persons in 2004 and will not help appreciably reduce the existing unemployment of about 650,000 persons.

**Sri Lanka***Key Considerations (contd)*

- Recruiting to the public sector which is already overstuffed will only increase fiscal deficits and public debt
- The resulting socio-political tension creates political instability discontinuity in economic policy, particularly with reference to State Owned Enterprise reform and areas where privatization is desirable.
- The solution therefore will lie in accelerating the pace of development of the private sector with a simultaneous focus on state owned enterprise restructuring and eventual privatization
- But the continuity and sustainability of such policies, as we have seen at the General Elections in April this year, will only be possible if there is a robust parallel, tangible focus on bridging the 'Income and Opportunity Gap' between the village and the city – in essence a strategy of 'Economic Growth with Equity'.
- Thus a compelling case is made for 'Unleashing Entrepreneurship' through a: SMALL AND MEDIUM ENTERPRISE EMPOWERMENT INITIATIVE.

**Sri Lanka***–An Overview of the SME Environment*

- The Market economy introduced in 1977 has positively contributed towards the development of SMEs due to higher utilization of capacities, expansion and setting up of new industries.
- However, growth is constrained due to:
  - Collateral lending vs. Lending based on project viability.
  - The high cost of financing for working capital as well as desirable modernization and expansion
  - Delays in processing of loans
  - Limited knowledge and skill in project concept development and design, feasibility preparation, technical, managerial and financial inputs, market access and development
  - Unfair competition due to smuggling and dumping, under-invoicing, leakage of duty-free goods from export oriented and BOI enterprises.

**Sri Lanka***–An Overview of the SME Environment*

- However, growth is constrained due to (contd):
  - Limited access to project related technical knowledge and know-how and the costs associated therewith
  - State sponsored development institutions not having adequate regional and rural

presence

- Limited infrastructure in locations where SMEs have the potential to locate
- Poor transport facilities, absence of or delays in obtaining connections for electricity, water and telecommunications
- High cost of raw materials and components of machinery inputs arising from a rising exchange rate, customs duty and other levies

### **Sri Lanka**

*–An Overview of the SME Environment*

- However, growth is constrained due to (contd):
  - Taxes at National and Local Government level, which may not necessarily be re-invested to upgrade enterprise demand-driven rural infrastructure
  - Constraints to the implementation of cost reductions, process improvement and product improvement and related quality issues due to limited access to know-how, technology and related financing requirements
  - Limited information in sourcing inputs at competitive prices
  - A multiplicity of institutions, Government sponsored, NGOs and Bilateral and Multilateral donor funded projects, which while duplicating assistance in some areas have yet to address, policy, strategy and institutional gaps

### **Sri Lanka**

*–An Overview of the SME Environment*

- However, growth is constrained due to (contd):
  - Complexity and delays in Government approval procedures
  - Limited availability of skilled manpower
  - Out migration of workers in regional plantation areas and village areas, which constrain the realization of the potential of agricultural and agro-industrial ventures
  - Inadequate investment and fiscal incentives
  - Absence of a National Apex body for coordination
  - Absence of a National Policy and strategy with identified public and private sector executing institutions to catalyze the realization of the full potential of the SMEs

### **Sri Lanka**

*–Recent Policy Developments and Actions*

- A Task force for Small and Medium Enterprise Development was established in October 2001
- A White Paper on a National Strategy for SME Development was presented in December 2002. The following are selected key recommendations of the White Paper:
  - SMEs have been defined as enterprises with Asset Values Rs 50m (US\$500,000) excluding Land and Buildings
  - Small Scale Enterprises are defined as those with Asset Values not exceeding Rs 20m (US\$200,000) and Medium Scale Enterprises with Assets Values not in excess of Rs 50m (US\$500,000)
  - An SME Policy Unit to be established within the recently established Ministry of SME Development.

### **Sri Lanka**

*–Recent Policy Developments and Actions*

- Key recommendations of White Paper (contd)
  - An SME Authority to be established
  - The Industrial Development Board (IDB) to be restructured with necessary funding and administrative support

- The IDB to engage in low cost credit negotiation and project monitoring
- A possibility of introducing Credit Guarantee and Equity Capital Schemes to be explored
- Venture Capital Companies and Leasing Companies to provide credit support to SMEs
- Loan disbursements and allied facilities to be undertaken with assistance of BDS providers
- The Loan Recoveries Act to be amended to provide opportunities to restructure sick industries

**Sri Lanka**

*–Recent Policy Developments and Actions*

- Key recommendations of White Paper (contd)
  - Technical Service Centres to be established at District Level
  - A Technology Development Fund to be established
  - A voucher scheme to be established for SMEs to be engaged in R&D work
  - A website for SMEs to be created
  - Opportunities for SMEs to participate in trade promotion exhibitions to be provided
  - Access to foreign markets to be provided
  - A voucher scheme to be introduced for SMEs to use BDSs
  - Business incubator programmes to be promoted
  - A simplified tax system to be introduced for SMEs

**Sri Lanka**

*–Recent Policy Developments and Actions*

- Key recommendations of White Paper (contd)
  - WTO concessions to be sought for SMEs
  - Implement effective anti-dumping laws
  - Skill development programmes to be conducted – private sector participation to be invited
  - Universities and other training institutions to be encouraged to provide training support
  - Industrial Parks for SMEs to be established in rural areas
  - Sub-contracting to be promoted
  - Industry clusters to be formed
  - Productivity enhancement programmes to be launched
  - Awareness programmes to be launched on cleaner production with a focus on cost savings and efficiency
  - SMEs to be released from labour and tax obligations for the first three years of business
  - A SME Bank is to be established

**Sri Lanka**

*–Recent Policy Developments and Actions*

- The recently established Ministry of Small and Medium Enterprise Development is expected to bring together all key agencies responsible for SMEs
- Key Institutions under the purview of the Ministry will include
  - Sri Lanka Export Development Board
  - Sri Lanka Export Credit Insurance Cooperation
- Ministry will work closely with the National Council for Economic Development (NCED). The SME cluster of the NCED will execute plans through various private and public sector institutions.

**Sri Lanka***–Recent Policy Developments and Actions*

- There are two Donor Funded Projects of the Ministry.
  1. *Business Service Support Facility (BSSF)*.
    - BSSF includes technical assistance, training and a matching grant programme
    - The BSSF has entered into cooperation agreements with three lead partner organisations – SLBDC, ISB and Sarvodaya Economic Enterprises Development Services, to create a network of six regional Business Development Centres (BDC). In August 2004 six BDCs have been established. Thirty One (31) professionals have been recruited.
    - Under its Matching Grant Programme BSSF is currently providing assistance through two types of grants
      - BDS Capacity Building Grants
      - BDS User Grants

**Sri Lanka***–Recent Policy Developments and Actions*

- There are two Donor Funded Projects of the Ministry (cont'd).
  2. *The Small and Medium Enterprise Sector Development Programme (SMESDP)*
    - SMESDP includes a Line of Credit of US\$60m to PCIs to improve SME Access to Finance – This Line of Credit is known as the Sahanya Loan Scheme (SLS)
    - The PCIs of the SLS are two development banks and two commercial banks.
    - Under this programme SMEs are defined as those with investment in Fixed Assets, excluding Land and Buildings at original book value not exceeding Rs 35m and not exceeding Rs70m on project completion
    - Maximum loan to a single enterprise Rs35m; Repayment period of ten years; Grace period 24 months; Interest Rate AWDR.

**Sri Lanka***–Recent Policy Developments and Actions*

- There are two Donor Funded Projects of the Ministry (contd).  
*The Small and Medium Enterprise Sector Development Programme (SMESDP) contd.....*
  - The Scheme commenced September 2002 and by end March 2004 the funds committed exceeded the allocated US\$60m
  - 2201 loans were approved – 1798 existing projects; 403 new projects
  - 54% are in the Proprietorship category, 22% in Partnerships and 24% in Limited Liability Companies.

**Sri Lanka***–Recent Policy Developments and Actions*

- The ADB is assisting with financing for the following:
  - Project 1 – Policy and Enabling Environment – US\$20m
  - Project 2 – Technical Assistance Grant – US\$1.25m
    - Establishment of a SME Policy Unit
    - SME Baseline Survey
    - SME Website
    - Secured Transactions Act
  - Project 3 – Financing SMEs
    - Credit Component – US\$60m

- Partial Credit Guarantee – US\$90m
- Project 4 – Facilitating Business Development Services (BDCs) – US\$6m
- BSSFs

**Sri Lanka***–Recent Policy Developments and Actions*

- Future Projects:
  - i. ADB has agreed with the Government of Sri Lanka to include the second stage of SMESDP (Phase II) in their Country Programme for the Year 2005.
  - ii. The Government of Sri Lanka also requested the Japan Bank for International Cooperation (JBIC) for a credit facility of approximately US\$ 100m to continue the assistance provided under the Small and Micro Industries Leader and Entrepreneur Promotions Projects (SMILE I & II) and the Environmentally Friendly Solutions Fund (E-Friends I) through which the Government has assisted a number of SMEs and Environmentally Friendly projects.

**Sri Lanka***–Recent Policy Developments and Actions*

- Pilot Project on SME Credit Facilitation:
  - The project purpose is to test the added value of mobilizing regional Chambers of Commerce to generate significantly increased credit flows to local Small & Medium Enterprises (SMEs) across Sri Lanka.
  - Project Sponsors-The BSSF of the Ministry of SME Development (MSMED) and the UNDP Invest-in-Peace Project, supporting the Business-for-Peace Alliance (BPA) of Regional Chambers of Commerce.

**Unleashing Entrepreneurship through Empowerment of SMEs:***A possible framework for an Action Plan for Sri Lanka / South Asia***A possible framework for an Action Plan.....**

- Bridge technical gaps in project concept evaluation, preliminary project evaluation, project feasibility study preparation and the need for existing SMEs to diagnose business problems and engage in strategic redirection:
  - *Establish a National Level “SME – Business Development Support Service (SME – BDSS)” Link to Regional Level*
- Bridge Technology and Related Finance Gaps
  - *Establish an SME –Technology Support Fund (SME – TSF) at National and Regional level*
- Bridge Technical and Managerial Skill gaps which constrain SME growth and continuity
  - *Establish SME Technical and Managerial Skill Development Fund (SME – TMSDF)*

**A possible framework for an Action Plan.....**

- Bridge Market Access and Market Development strategy gaps, relating to the domestic market as well as global export markets
  - *Establish a SME – Market Development Assistance Fund (SME – MDAF)*
- Catalyze the launching of several sector specific and project specific New Ventures.
  - *Establish SME New Venture Initiation Partnerships -This will be the platform for SME New Venture initiation*
  - *MNC – SME Partnerships (with resident MNCs)*
  - *LLC – SME Partnerships (Top 20 on the CMB Stock Exchange)*
  - *NGO – SME Partnerships (consolidate existing activity)*
  - *Women Entrepreneur Empowerment Initiatives (Women's Chambers)*
  - *Young Entrepreneur Empowerment initiatives (YESL/JA)*

- *SME – Opportunity Data Bank (to facilitate matchmaking of equity partners; technical alliances and marketing alliances). A sub-contracting exchange can be one of the components of this Opportunity Data Bank*
- *Contractual and / or equity linked formal new mergers and alliances between MNCs and SMEs; Large Local Companies (LLCs) and SMEs etc. The focus will be on partnering along the value chain of business from production at district and village level, with technical assistance and domestic and export marketing capability of MNCs and LLCs*

**A possible framework for an Action Plan.....**

- Bridge equity financing gaps of SMEs
  - *Facilitate the establishment of new National Level and South Asian Regional Level Venture Capital Funds*
- Bridge National Level physical infrastructure gaps which constrain growth of SMEs at District and Village Level (where demand driven)
  - *Establish a South Asian Region Infrastructure Development Bank (SA – IDB)*
- Enhance Capacity to incrementally build External Reserves
  - *Evaluate merits and demerits of and if feasible Establish a South Asian Barter and Countertrade Exchange*
- Unleash the potential of agronomic compatibility of presently unexploited lands and national mineral resources
- Establish an Apex Level body to develop project profiles for possible agribusiness and mineral resource based ventures
- Expand coverage of the previously recommended initiatives and institutions by presence at district and village level

## 6.12. Presentation by Ms. Anuradha Rajivan, UNDP Colombo Regional Centre

<p><b>Micro Insurance</b></p> <p><b>IS IT WORTHWHILE FOR BOTH SIDES?</b> Feedback from a consultation in rural India</p> <p><i>Anuradha Rajivan, UNDP</i></p>
<p><b>Current Situation in India: Supply Driven</b> Most rural insurance products aim at protecting bank loans to the poor</p> <ul style="list-style-type: none"><li>• Supply driven</li><li>• Very little attempt to assess needs/perceptions of Bottom of Pyramid</li><li>• Standard and limited insurance products</li></ul> <p>Operational issues</p> <ul style="list-style-type: none"><li>• Eg, under crop insurance the system for assessing yields, unit area, found unsatisfactory</li></ul>
<p><b>Element of Compulsion</b></p> <ul style="list-style-type: none"><li>• Farmers do not get crop loans unless they also take insurance cover</li><li>• So also for animals</li><li>• Though two independent m-Fin products (loan and insurance) borrowers factor it (premium) in as an additional interest burden</li></ul>
<p><b>Contrasting Perceptions</b></p> <ul style="list-style-type: none"><li>• Insurance companies<ul style="list-style-type: none"><li>○ View farmers as beneficiaries – recipients of a service</li></ul></li><li>• Commercial banks<ul style="list-style-type: none"><li>○ Think farmers will default</li><li>○ Insist on insurance of crops, animals</li></ul></li><li>• Poor farmers<ul style="list-style-type: none"><li>○ Think of themselves as victims – facing higher cost of accessing finance</li></ul></li><li>• Inherent tension among stakeholders ...</li></ul>
<p><b>Is there a potential for m-Insurance?</b></p> <ul style="list-style-type: none"><li>• Very little rural insurance is de-linked from loans</li><li>• Indicates that, unless compulsory, rural insurance is not a viable market in its present form</li><li>• Yet, rural HHs face risks, with substantial income fluctuations - that is well known<ul style="list-style-type: none"><li>○ Seasonality</li><li>○ Local disasters (fire accidents, pests, floods)</li><li>○ Limited capacity to buffer effects of shocks</li></ul></li></ul>
<p><b>Is a win-win situation possible?</b></p> <ul style="list-style-type: none"><li>• With insurance products matching rural needs</li></ul> <p>And</p> <ul style="list-style-type: none"><li>• Insurance companies making profits</li><li>• Given that risk sharing arrangements are incomplete</li></ul>
<p><b>A Missing market?</b> Is this a lost opportunity?</p>
<p><b>Or is behaviour different among BoP population?</b></p> <ul style="list-style-type: none"><li>• Are rural BoP risk lovers?</li><li>• Are rural BoP fatalists?<ul style="list-style-type: none"><li>○ Perhaps, up to a point – as part of a coping strategy for stress</li></ul></li></ul>

<ul style="list-style-type: none"> <li>• Could the problem be with the supply driven approach? <ul style="list-style-type: none"> <li>○ Very likely</li> </ul> </li> </ul>
<p><b>Rural HHs also have risk aversion &amp; risk management strategies</b></p> <ul style="list-style-type: none"> <li>• No reason to believe that behaviour here is any different from elsewhere Multiple economic activities (e.g., agri with a few goats, chickens, rope making, mulberry cultivation, labour...) This is often at the expense of specialisation / more profitable work Mutual support – neighbours, relatives, SHGs Mostly local, informal risk management</li> </ul>
<p><b>Experience from the field – Rural TN Case</b></p> <ul style="list-style-type: none"> <li>• Women’s SHG members invited for a face-to-face discussion with insurance companies</li> <li>• One day interaction session</li> <li>• Among savvy city-slickers and semi-literate rural women</li> </ul>
<p><b>Concept of insurance explained to rural women</b></p> <ul style="list-style-type: none"> <li>• In TN lotteries are very popular <ul style="list-style-type: none"> <li>○ Very low probability of a very high gain</li> <li>○ Probabilities very well understood</li> </ul> </li> <li>• Insurance explained in those terms <ul style="list-style-type: none"> <li>○ Very low probability of a very high loss</li> <li>○ Inverse of a lottery</li> <li>○ It was immediately understood</li> </ul> </li> </ul>
<p><b>Feedback from the discussions</b></p> <ul style="list-style-type: none"> <li>• Insurance companies presented the range of products <ul style="list-style-type: none"> <li>○ Crop insurance</li> <li>○ Animal insurance</li> <li>○ Accidental death of borrower, including road accidents</li> <li>○ Some schemes for women – mostly designed for urban areas</li> </ul> </li> </ul>
<p><b>Feedback from the discussions</b></p> <ul style="list-style-type: none"> <li>• Rural women picked up the idea of insurance quickly</li> <li>• paying an small premium to cover against a large loss</li> <li>• were interested in protecting their lives &amp; assets</li> <li>• were comfortable with the idea of insurance companies making profits</li> <li>• saying they themselves would not get into an avoidable loss making situation voluntarily</li> <li>• But completely disagreed about the risks to be covered</li> </ul>
<p><b>Where are the road accidents?</b></p> <ul style="list-style-type: none"> <li>• There were no roads with heavy traffic <ul style="list-style-type: none"> <li>○ None of them drove cars</li> </ul> </li> <li>• They wanted cover for other risks - <ul style="list-style-type: none"> <li>○ Falling out of a cocoanut tree</li> <li>○ Death due to drowning in a well</li> <li>○ Snake bites</li> <li>○ Fire accidents</li> </ul> </li> </ul>
<p><b>Response from insurance companies...</b></p> <ul style="list-style-type: none"> <li>• There was surprise at the intelligent questions and suggestions</li> <li>• Payout of policy shd not be to husband</li> <li>• Wd create a financial incentive for eliminating wife and marrying again – a common occurrence</li> </ul>

<ul style="list-style-type: none"> <li>• Solution – daughter to receive</li> </ul>
<p><b>Response from insurance companies...</b></p> <ul style="list-style-type: none"> <li>• Wanted ideas for <ul style="list-style-type: none"> <li>○ reducing transactions costs</li> <li>○ coping with private information (information asymmetry) not available to insurance company</li> <li>○ moral hazard (risky behaviour, knowing that there is insurance cover)</li> <li>○ adverse selection (higher risk agents accept insurance)</li> </ul> </li> </ul>
<p><b>Women’s inputs to insurance companies...</b></p> <ul style="list-style-type: none"> <li>• SHGs, their federations, other m-Fin institutions - reduce transactions costs</li> <li>• Village communities – information asymmetry is small, especially in SHGs</li> <li>• SHGs also address the issue of moral hazard and to an extent</li> <li>• disincentive could be increased premium in subsequent years</li> <li>• Group approach and group insurance also helps spread risks</li> </ul>
<p><b>Other Operational Ideas</b></p> <ul style="list-style-type: none"> <li>• Bulk membership – can reduce premiums through group insurance (additional input)</li> <li>• Premia can be collected through groups &amp; their federations</li> <li>• Payouts also can follow the same route</li> </ul>
<p><b>Conclusion</b></p> <ul style="list-style-type: none"> <li>• For m-Insurance to succeed <ul style="list-style-type: none"> <li>○ Companies must understand the client population</li> <li>○ Respond to their particular concerns regarding risks</li> <li>○ Standard city based schemes will not attract rural clients voluntarily</li> <li>○ Local variations essential (not national standard package)</li> <li>○ Interactions with client representatives can provide valuable insights for win-win solutions</li> <li>○ Also helps m-credit as borrower risks are better managed</li> </ul> </li> </ul>
<p><b>Hope that this helps trigger a mutually productive risk management partnership!!</b></p>

### 6.13. Presentation by Mr. Arun Kashyap, Advisor, Public Private Partnerships/BDP, UNDP

<p><b>Promoting Public Private Partnerships for Micro-insurance</b></p> <p>Sub-Regional Launch          Unleashing Entrepreneurship – Making Business Work for the Poor &amp;          Workshop on SME Development in South Asia</p> <p>16-17 December 2004</p>
<p><b>Underlying Principle</b></p> <ul style="list-style-type: none"> <li>• Informal economy             <ul style="list-style-type: none"> <li>○ Significant proportion of the labor force (up to 40%)</li> <li>○ Majority women entrepreneurs</li> </ul> </li> <li>• Characteristics             <ul style="list-style-type: none"> <li>○ low incomes and low productivity</li> <li>○ lack of formal means to manage risk</li> <li>○ Lack of life and livelihoods security</li> </ul> </li> </ul>
<p><b>Underlying Principles</b></p> <ul style="list-style-type: none"> <li>• Need             <ul style="list-style-type: none"> <li>○ Access to financial and non financial services</li> <li>○ Access market based viable safety net products</li> </ul> </li> <li>• Microfinance             <ul style="list-style-type: none"> <li>○ Cover the financial needs</li> </ul> </li> <li>• Micro-insurance             <ul style="list-style-type: none"> <li>○ Life, Health, Crop, etc.</li> </ul> </li> <li>• Separate management mechanisms</li> </ul>
<p><b>Access to Micro-insurance</b></p> <ul style="list-style-type: none"> <li>• Micro-insurance is a nascent market that can thrive under PPP</li> <li>• Highly technical operation</li> <li>• Hypothesis             <ul style="list-style-type: none"> <li>○ Benefit development of micro and small enterprises and strengthen livelihoods</li> <li>○ Access to insurance by entrepreneurs will draw private sector investments</li> </ul> </li> </ul>
<p><b>Proposed Market Intelligence Activity</b></p> <ul style="list-style-type: none"> <li>• Lack of any form of micro-insurance market potential analysis to examine             <ul style="list-style-type: none"> <li>○ Demand and acceptability of products</li> <li>○ Development costs, cost of premiums</li> <li>○ Affordability based on a sustainable business model</li> <li>○ Education of clients, insurance service providers and other stakeholders</li> </ul> </li> <li>• Partnership             <ul style="list-style-type: none"> <li>○ UNDP, Allianz, GTZ</li> </ul> </li> </ul>
<p><b>Basis for Market Intelligence Analysis</b></p> <ul style="list-style-type: none"> <li>• Product design in close consultation with the stakeholders</li> <li>• Include qualitative consumer surveys</li> <li>• Communicate information and knowledge of the products to the potential customers;</li> <li>• Strategy to settle the claims as quickly as possible</li> <li>• Understanding, appropriately allocating and minimizing the transaction costs</li> </ul>
<p><b>Next Steps &amp; Follow Up</b></p> <ul style="list-style-type: none"> <li>• Selected Countries             <ul style="list-style-type: none"> <li>○ India, Indonesia, and Lao PDR</li> </ul> </li> <li>• Follow up             <ul style="list-style-type: none"> <li>○ The provider must have a depth of knowledge and experience in the actuarial</li> </ul> </li> </ul>

side of insurance provision;

- Products must be launched sequentially starting with simple products and then moving into more sophisticated products
- Pilot (possibly India)

## 7. Media Coverage

### 7.1. UNDP Press Release No. 289, New Delhi, 15 December 2004

#### **Regional Conclave on Making Business Work For The Poor**

The two-day Sub-Regional Workshop on “Unleashing Entrepreneurship: Making Business Work for the Poor”, begins here, tomorrow. The Workshop, a joint initiative of the Confederation of Indian Industries (CII), the United Nations Development Programme (UNDP) and the United Nations Industrial Development Organization (UNIDO), is being held under the aegis of the India Partnership Forum (IPF) – a joint initiative of UNDP and Confederation of Indian Industry (CII) to promote and strengthen public private people partnership for development.□

Dr. Hafiz Pasha, UN Assistant Secretary General and UNDP Assistant Administrator, and Mr. Wlified Luetkenhorst, Director, UNIDO will address the workshop. Policy makers, business leaders and UN System partners from South Asian countries namely Bangladesh, Bhutan, Maldives, Nepal, Pakistan, Sri Lanka and the host India, will participate in the workshop.

The theme of the workshop is based on the Report of the UN Commission on Private Sector and Development, co-chaired by Prime Minister Paul Martin of Canada and Ernesto Zedillo, former President of Brazil.□Bringing the informal business sector into the legal and economic mainstream is the principal focus of the Report. One of the key recommendations of the Report is that international development policy must focus strongly on supporting reforms and professionalisation of the small scale sector, the primary engine of employment and domestic commerce in developing countries.

The Report will be launched by the former Finance Minister of Chile, Dr. Eduardo Aninat, who was a member of the UN Commission. Management Guru Professor C K Prahalad of the University of Michigan Business School and author of “The Fortune at the Bottom of the Pyramid” will be one of the star attractions at the workshop. Prof. Prahalad□and□Mr. Rajat Gupta, Senior Managing Director of Mckinsey Inc□were among the members□of the Commission.

The Regional Workshop will be preceded by the UNDP-CII Roundtable on Public-Private-Community Partnership in Developing Poorest Districts. The pilot initiative to explore this will be in the district of Dungarpur□in Rajasthan.□

The Dungarpur initiative encompasses the key principles outlined in the UN Report on “Unleashing Entrepreneurship – Making Business Work for the Poor”. A field assessment mission to Dungarpur comprising a team of corporates including Hindustan Lever Limited, ITC, ICICI -- three of the companies included in Prahalad’s book -- together with UNDP and CII nominees recently visited Dungarpur to identify the□opportunities and challenges for public-private-community partnership, and to delineate a suitable strategy for launching this initiative.

The UN Commission on Private Sector and Development was appointed by the UN Secretary General Kofi Annan in the backdrop of the Millennium Summit and the need to focus on meeting the challenge of achieving the Millennium Goals, particularly Goal 1 of halving poverty by 2015. Currently one-fifth of the world population continues to live on less than US\$ 1 a day.□The Commission looked at the role and potential of the private sector and entrepreneurship in developing countries in meeting the challenge of endemic poverty.

*[Kumar M Tiku](#), Information Officer, UNDP, New Delhi.*

### 7.2. Deepikaglobal.com, 16 December 2004, New Delhi

#### **Centre committed to provide timely inputs to SMEs: Elangovan**

New Delhi, Dec 16 (UNI) Stressing the importance of small and medium enterprises, Minister of

State for Commerce and Industry E V K S Elagovan today assured that the Centre was committed to provide timely inputs like credit facilities and technological up gradation to the sector.

"The SME sector has a crucial role to play in terms of job creation, poverty alleviation, removal of income disparities, value addition to GDP and export earnings," he said while releasing the UN Report on "Unleashing Entrepreneurship - Making Business Work for the Poor" here.

The government was also helping in the up gradation of entrepreneurial skills through advanced training and was committed to encourage micro finance and entrepreneurship in women.

"The Centre was keen to improve the competitiveness of the small scale sector in light of rapid globalization," he said.

Mr Elagovan pointed out that the Human Development Index is intimately related to the overall development and poverty.

Referring to various statistical data, he said life expectancy in the SAARC region varied from maximum 72.1 years for Sri Lanka to minimum 58.6 years for Nepal against the world average of 66.9 years and India's 63.3 years.

"This shows that industrial development can play a vital role in bridging the inter-regional economic gap," he said.

Management guru C K Prahlad in his address stressed on innovative approaches to convert poverty into an opportunity for all concerned.

### **7.3. Team India, 17 December 2004, New Delhi**

#### **Private sector must reach out to bottom of Pyramid: Prahalad :**

New Delhi, Dec 16 : The private sector had been left out of the process of eradicating poverty in rural India for too long, management guru C K Prahalad said today.

The whole process of reaching out to the bottom of the 'pyramid' was confined to NGOs, government or multilateral agencies, leaving out the private sector, Prahalad said at a Planning Commission-UNDP-CII-sponsored discussion on public-private-community partnership here.

This was despite the fact that private players were active in rural India, albeit in the unorganized sector, the eminent author of 'The Fortune at the Bottom of Pyramid -- Eradicating Poverty Through Profits', said.

"Private sector is active in rural India. Only we don't recognize them," he said.

He observed, however, that the private sector, including money lenders, was not transparent in their dealings.

This asymmetry of dissemination of information had to be broken by initiating more and more private-public partnership in these areas.

However, before doing this it should be kept in mind that Indian poor are not monolith. They are segregated and live in specific circumstances, he said. "There cannot be one model to solve the problems of Indian poor." Instead of wealth distribution, emphasis should be laid on wealth creation, he said.

This also made business sense as the rich would come if assets were built for the poor, but if assets were built for the rich, the poor would not be able to afford them, Prahalad, who teaches at Michigan University, said. PTI

#### **7.4. Making business for the poor, 12/2/2005**

##### **Innovative approaches can convert poverty into opportunity, says Ferdaus Ara Begum**

RECENTLY a sub-regional launch of the UN Report on "Unleashing Entrepreneurship Making Business Work for the Poor" was organized in New Delhi by the UNDP in collaboration with UNIDO and Confederation of Indian Industry (CII), India. The first sub-regional launch of an UN report in Asia and the Pacific was organized to reflect on the many successful examples of private sector initiatives in providing high quality, affordable goods and services to the poor. UNDP advocates for the partnerships to generate creative locally-tailored solutions to most pressing development problems. Millennium Development Goals (MDGs) can be achieved only in partnership among key stakeholders. UN Commission on the private sector and developments believes that any approach to private sector development should be grounded in the realization that savings, investment and innovation that lead to development are undertaken largely by private sector individuals, corporations and communities.

The private sector is central to the lives of the poor and all poor are consumers. The report says that across the globe poor consumers pay more than the rich. In Mumbai, slum-dwellers in Dharavi pay 1.2 times more for rice, 10 times more for medicine and 3.5 times more for water than do middle class people living at the other end of the city. An innovative private sector can find ways to deliver, low-cost goods and services to demanding consumer across all income ranges.

The report said that 4 billion bottom of the pyramid (BOP) people with a per capita income of less than \$1500 a year provides multinationals and large local companies with an alternative market for their goods and services. A good example of a business ecosystem at work is Hindustan Lever Ltd., a major producer of personal care and food products in India. Its ecosystem includes 80 manufacturing factories, 150 small and medium enterprise suppliers employing up to 40,000 people, 7,250 people exclusive stockists, 12,000 wholesalers and small retailers, 0.3 million shop owners and 1.5 million industrial entrepreneurs in remote villages who sell its products, a number to grow to 1 million on current expectation.

The report tried to get the reply of two questions: these are about how the potential of the private sector and entrepreneurship can be unleashed in the developing countries and how can the existing private sector be engaged in meeting that challenge. The report was first launched in NY, USA. It was felt that launching the report in South Asia could help entrepreneurs to gear up their efforts and help development of private sector and the reach goal of MDG. Eduardo Aninat, former Minister, Ministry of Finance, Chile and member UN Commission on the Private Sector & Development (PSD) said it will help to build capacity of the private sector. It has got a number of examples of private sector activities. Following the examples of the report, entrepreneurs can come forward with new and innovative ideas by mobilizing local resources. He said the report has given a number of successful examples on how market for the poor can be expanded who are at the bottom of the pyramid in respect of housing, cultural issues, consumption etc. For creating an enabling environment the report recommended for private-public partnership and gave emphasis on creating enabling environment for the private sector. He said the report could help achieving of the MDG goals, welfare of the poor and alleviation of poverty.

Professor C. N. Prahalad, the University of Michigan Business School, author of the book "The Fortune at the Bottom of the Pyramid-Eradicating Poverty through profits" presented some cases for all innovative approach to convert the poverty into an opportunity for all concerned. He said, what is needed is an approach that involves partnering with the poor to innovate and achieve sustainable win-win scenarios where the poor are actively engaged and, at the same time, the companies providing products and services to them are profitable. The market at the BOP with more than 4 billion people living on less than US \$2 per day presents tremendous opportunity for the private sector.

These opportunities can be unleashed if large and small firms, government, civil society organizations, development agencies, and the poor themselves work together with a shared agenda.

Large-scale and widespread entrepreneurship is at the heart of the solution to poverty. Prahalad has tried to show that at the top of the pyramid are the wealthy, with numerous opportunities for generating high levels of income. The distribution of wealth and the capacity to generate incomes in the world can be captured in the form of an economic pyramid. The quality, efficacy, potency, and usability of solutions developed for the BOP markets are very attractive for the top of the pyramid.

The traditional MNC approach and the approach suggested by Prahalad here -- top of the pyramid to BOP and from the BOP to the top of the pyramid could work. He presented some successful examples and tried to prove that innovative approaches can "convert the poverty into an opportunity for all concerned", including the poor and the private companies. As per his opinion, we should not be seeing the poor just as the target beneficiaries of development assistance, but as creative entrepreneurs who take initiative, often for the basic survival. An innovative private sector can find ways to deliver low cost (even sophisticated) goods and services to demanding consumers across all income ranges. It can sell to the urban distressed areas as well as the poor rural villages or towns. Innovation might arise from the focus on the lower quintile market which creates cost advantages from economies of scale, or the firm may have developed distribution links to the end consumer in the village and so are able to better harness knowledge of the actual needs of this segment of the market. Firms might keep costs low through outsourcing, for greater flexibility. The private sector can thus alleviate poverty by contributing to economic growth, empowering the poor by providing them with services and consumer products, increasing choices and reducing the prices. The first creates employment and income growth. The second improves the quality of life for the poor. The greater interaction between those at the bottom of the pyramid and the private sector creates opportunities for direct involvement in the market economy.

With broad recommendations for action developed by the UN Commission on Private Sector and Development (namely: to collaborate and mobilize capabilities of the private sector, to drive innovation and use of IT: to engage in public-private partnerships for sustainable development; and to form ecosystems and build networks of companies), it said these should be translated into concrete actionable initiatives at the country and regional levels. Some potential ideas like women entrepreneurship development; pro-small entrepreneur reforms; kiosks/one stop shops for registration; single business permit; alternative dispute resolution; automated assignment of cases; specialized debt collection courts; collateralizing real estate assets; business plan competition; in-country monitoring; ISO certification support; hands-on educational programmes; and micro-insurance schemes etc. are also helpful as recommended by the report. Efforts to design innovative project initiatives should, however, go further and beyond what has worked successfully to-date in terms of SME development and promotion of micro-enterprises. There is an immense opportunity to maximize the use of the private sector market-based forces to fight poverty at the BOP. In the light of the above, a potential role of UNDP could be in providing market intelligence to identify profitable initiative that help satisfy the needs of the poor while paying by the rules of the market. UNDP may help Bangladesh by taking specific role which in turn would help developing SMEs. SME representative organization can take lessons from the report of the commission on how to integrate large companies with SMEs through well defined ecosystem to make market for the poor and help them sustain the market.