

Policy Note 4

Delivering a Strong Ecosystem for MSMEs



Maldives Partnership Forum 2019

Investing in a Resilient & Sustainable Maldives

Small and Medium Enterprises (SME) make up over 93% of all businesses in the Maldives' economy. Given that SMEs are vulnerable and yet critical for the robust growth of the economy, the Government recognizes the importance for the policy regime to be facilitative of the growth and development of this sector.

Traditionally, economic development policies were geared towards broad-based development of key industrial sectors such as tourism and fisheries. Up until recently, SMEs did not make it into the radar of economic development as a priority sector that is distinct from large enterprises. In fact, Micro, Small and Medium Enterprises (MSME) was not formally defined until the SME Act came into existence in 2013.

The SME Act aims to formalize the sector and outline a systematic framework of support for SME development. It lays the bedrock for institutional support for the advancement of SMEs. Under the SME Act, an SME Council has been established as a high-level cross-sectoral body with representation from the Government and non-government sector to advise the Minister of Economic Development on developing and implementing a progressive SME framework. Furthermore, the SME Act calls for the establishment of business support centers across the country, and to earmark funds from the Government budget annually to provide financial assistance to SMEs.

The existing framework of support for SME development consists of the following key initiatives:

- An SME Development Finance Corporation (SDFC) was recently established as one of the initiatives under the 100 day pledges of the Government. It is to be noted that this is the first of its kind in the country, dedicating its financial products specifically for SMEs.
- The Business Centre Corporation (BCC) provides business advisory services and handholding support through a network of 7 Business Centers established across the country.
- A central department established under the Ministry of Economic Development to drive SME policy.

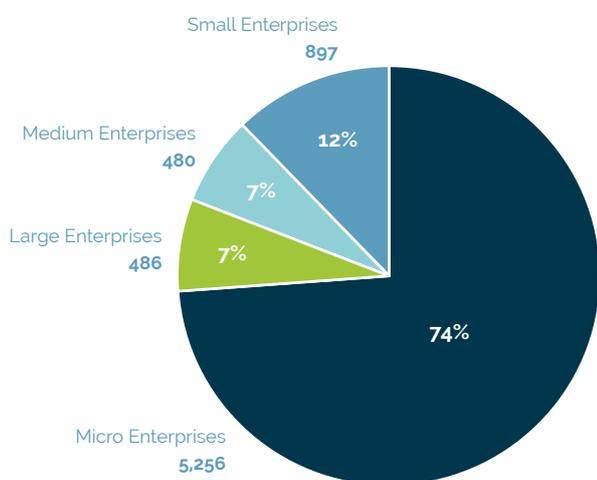


Figure 1: Number of businesses based on declared revenue (MIRA BPT 2016 data)

Challenges

SMEs are faced with a number of challenges, which can be broadly grouped into five main areas:

Entrepreneurship and Human Capital:

The main issues and challenges for SME development with regard to entrepreneurship and human capital are:

- An underdeveloped entrepreneurial culture with low awareness and motivation for entrepreneurship.
- Limited education and training opportunities for developing entrepreneurship and technical skills.
- Limitations in the TVET system in terms of resources, capacity and reach, combined with low attractiveness of vocational education.
- Low uptake on lifelong-learning, stemming from lack of demonstrated relevance and high opportunity cost of attending training.

Productivity, Technology and Innovation:

There are many reasons for poor productivity and barriers to the use of technology and innovation by SMEs. These include:

- Limited understanding among SMEs on productivity measures and how it links to innovation, competitiveness and financial performance.
- Low level of capital investment, primarily resulting from limited access to finance and lack of attention to productivity improvement measures.
- Lack of financial incentives to encourage innovation in SMEs and lack of adequate financial support for innovative high-growth SMEs.
- Weak industrial linkages among SMEs, between SMEs and large enterprises, hindering technology transfer and industry clustering.
- Limited funding for R&D and innovation activities in universities and research institutes, particularly for commercialization.
- Limited collaboration between industry and academia, with no networks for transfer of technology from R&D to realize commercial possibilities.

Access to Finance:

Access to finance has been singled out as the most difficult challenge by SMEs in Maldives. The obstacles in this area include:

- High collateral requirements and interest rates for bank loans.
- Absence of an SME bank or a development bank that would offer cash-flow based lending – this has recently been addressed through the establishment of SDFC. However, SDFC needs assistance in the development of a comprehensive lending portfolio, systems development and capital injections to expand its reach.
- Low financial literacy and poor financial record maintenance among SMEs undermines SMEs' credit worthiness and access to finance.
- Limited availability of alternative non-bank and equity financing mechanisms.

Market Access:

Market access is a critical area where SMEs are facing growth challenges. Main obstacles in this area include:

- Limited focus and know-how on marketing and branding as a means to communicate value, and to stand out in a competitive market.
- Underutilization of ICT and e-commerce platforms and payment methods.
- Inefficient and costly transport and logistics limiting market access.
- Limited collaboration between SMEs and large enterprises for market access.
- Underdeveloped middlemen in the value chain network.

Policy and Regulatory Environment:

A number of advances are being made on the policy and regulatory front to facilitate SMEs. However, there remain a number of challenges in this arena, including:

- Absence of widespread awareness and use of a common definition of SMEs.
- Virtually non-existent targeted data collection on SMEs, which undermines the ability to monitor and evaluate the impact of SME support policies.
- Ad-hoc SME policy coordination among government agencies and limited public-private consultation mechanisms.
- Lack of formal regulatory impact assessment mechanisms for SME related legislations, and frequent and short-notice policy and regulatory changes.
- A one-size-fits-all tax regime, which undermines survival and growth of SMEs.
- Public procurement not used as a path to support SME and women's business.

Policy priorities

Promote Entrepreneurship & Human Capital Development

Promoting entrepreneurship and human capital development is indispensable for SME development because human capital is increasingly considered to be the key ingredient to survive and prosper in an ever more competitive and converging world. Entrepreneurship and business skills development is essential for advancing economic participation and employability for women and youth.

The two key initiatives under this policy are to foster an entrepreneurial culture and enhance human capital development, particularly for women and youth. The existing framework of Business Centers will be utilized to enhance the range of business advisory support services provided. Additionally, importance will be given to entrepreneurship education at all levels of the education system from schools to universities and beyond.

Improve Access to Finance

Improving access to finance will invariably go a long way in developing a robust SME sector by assisting SMEs in overcoming one of their greatest challenges.

Greater availability of credit and alternative financing options are important for the development and growth of small businesses for greater financial inclusion, and expanding economic and employment opportunities for more inclusive growth.

The Government has identified 3 key initiatives towards the goal of improving access to finance – promoting financial literacy and sound financial management practices, increasing and promoting SME focused lending, and fostering alternative financing through non-traditional sources.

Of these initiatives, Government recently established the SDFC towards addressing access to finance.

Promote Productivity, Technology & Innovation

Poor SME performance is often attributed to their relatively low productivity compared to large enterprises. While SMEs may not achieve the same economies of scale, there is ample room for SMEs to improve their performance by attentively managing their productivity through innovation and adoption of appropriate technology.

Key initiatives under this goal are targeted at enhancing SMEs' productivity management capacity, promoting capital investment, technology improvement and pursuing innovation as a source of competitive advantage. The establishment of business and technology incubators will be promoted to assist entrepreneurs, technology-oriented and otherwise in their start-up and early development stages.

Improve Market Access and Internationalisation

Key initiatives under this policy are strengthening marketing capabilities of SMEs, improving reach to markets outside of home island, and facilitating pursuit of export markets. Strengthening linkages with the tourism industry is perceived to have great potential in this regard.

Enhance Policy and Regulatory Environment

It is important that trade related regulatory and trade policy coordinating bodies recognize that SMEs are inherently more vulnerable than large enterprises and therefore SMEs need special arrangements and support beyond broad-based enterprise development and trade facilitation measures.

Key initiatives under this goal focuses on strengthening institutional support framework for SME development, strengthening data collection framework and data-driven policy making, and simplifying regulatory and procedural hindrances facing SMEs.