

TAR: SRI 36117

Technical Assistance to the  
Democratic Socialist Republic  
of Sri Lanka for Preparing the  
Small and Medium Enterprise  
Sector Development Program II  
(Financed by the Japan Special  
Fund)

August 2005

Asian Development Bank

## CURRENCY EQUIVALENTS

(as of 1 August 2005)

Currency Unit	–	Sri Lanka rupee/s (SLRe/SLRs)
SLRe1.00	=	\$0.0100
\$1.00	=	SLRs100.1550

## ABBREVIATIONS

ADB	–	Asian Development Bank
BDS	–	business development services
BSSF	–	business services support facility
ISO	–	International Standards Organization
GDP	–	gross domestic product
SME	–	small and medium enterprise
SMESDP	–	Small and Medium Enterprise Sector Development Program
TA	–	technical assistance
JBIC	–	Japan Bank of International Cooperation

## TECHNICAL ASSISTANCE CLASSIFICATION

Targeting Classification	–	General intervention
Sector	–	Finance, industry, and trade
Subsectors	–	Finance sector development, and small- and medium-scale enterprises
Themes	–	Private sector development, governance, and sustainable economic growth
Subthemes	–	Policy/institutional/legal/regulatory reforms, financial and economic governance, and promoting economic efficiency and enabling markets

## NOTE

In this report, "\$" refers to US dollars.

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## I. INTRODUCTION

1. On 20 December 2001, the Asian Development Bank (ADB) approved the Small and Medium Enterprise (SME)<sup>1</sup> Sector Development Program (SMESDP)<sup>2</sup> to (i) strengthen the enabling business environment for SMEs, (ii) catalyze investment by improving SMEs' access to commercial finance, and (iii) enhance the capacity of providers of business development services (BDS). The SMESDP included (i) a policy reform loan amounting to \$20 million equivalent, (ii) a credit assistance program loan amounting to \$60 million, (iii) a business support services facility (BSSF) amounting to \$6 million equivalent, and (iv) a technical assistance (TA) grant for enabling SME growth amounting to \$1.25 million.

2. Due to the satisfactory progress in implementing SMESDP<sup>3</sup>, the improved security situation resulting from the third year of a cease-fire agreement after two decades of civil war, and improved economic growth (real gross domestic product [GDP] growth rate has been in the range of 5.25–6.0% since mid-2002), the project preparatory TA<sup>4</sup> was included in the 2005–2006 country strategy and program update for Sri Lanka dated September 2004. Additionally, the economic growth strategy of the Government of Sri Lanka is to support SMEs, particularly SMEs in the non-urban/rural areas of the country. The growth strategy focuses on increased export trade as well as financial and legal reforms. The purpose of the TA is to assist the Government in preparing the overall design and principal components of a follow-on project for SMESDP, SME Sector Development Program II (SMESDP II). The fact-finding mission fielded to Colombo in February 2005 reached understanding with the Government on the objectives, scope, financing plan, and implementation arrangements for the TA. The TA is designed to build on ADB's earlier assistance, lessons learned, and support provided by SMESDP.

## II. ISSUES

3. Economic growth in Sri Lanka is primarily generated by the large, private enterprises and/or SMEs located in the major industrial areas in the western region of the country. In other parts of the country, SME growth is stagnant, characterized by relatively few new businesses and limited expansion of existing businesses.

4. **Policy Constraints.** Dynamic growth and development of SMEs are restricted by, among other things, the presence of regulatory constraints, weak skills base, limited market intelligence to compete in a global economy, and limited access to finance. Further policy reforms such as improving the business environment, facilitating export trade, and enhancing competition will support the growth and development of SMEs throughout the country.

5. **Export Trade.** As of end-2004, Sri Lanka was a net importer of goods. Exports grew by 12% compared with the 9% growth recorded in 2003 and amounted to approximately \$5.8 billion or 28% of GDP, while imports surged by 20% to \$8 billion or 39% of GDP, reflecting the impact, among other things, of the escalation of oil prices. The result is a widening of the trade

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<sup>1</sup> An SME is an enterprise having less than 100 employees.

<sup>2</sup> ADB. 2001. *Report and Recommendation of the President to the Board of Directors on a Proposed Loan to the Democratic Socialist Republic of Sri Lanka for the Small and Medium Enterprise Sector Development Program*. Manila.

<sup>3</sup> Program implementation is discussed in ADB. 2003. *Small and Medium Enterprise Sector Development Program Progress Report: Release of Second Tranche*. Manila. Loan 1894-SRI was closed on 18 April 2005. The Business Services Support Facility Loan (1895-SRI) is being implemented (para. 14), and the \$60 million credit assistance (Loan 1896-SRI) is fully committed.

<sup>4</sup> The TA first appeared in *ADB Business Opportunities* (internet edition) on 25 February 2005.

balance by \$704 million to \$2.2 billion. The Government has a strong interest in increasing export trade, but success depends on the production and distribution of competitively priced, high-quality products that would satisfy the demands in the international market.

6. **Industry Sector.** The industry sector, of which approximately 90% consists of SMEs in Sri Lanka, represents approximately 26% of GDP, and comprises primarily production and sale of raw materials and semifinished goods. If the sector were to produce high-value finished goods, impact on real income growth in the country would be higher. Production of high-value finished goods would also indirectly stimulate the demand for raw materials as well as for semifinished goods, thereby further fostering overall economic growth. Additionally, further emphasis on product design would enhance export demand for finished goods.

7. **Quality Standards.** Because of limited quality control in the production of goods as well as limited quality standards in the sale of goods (e.g., there are no mandatory food safety standards) foreign manufacturers have gained a share of the domestic market.

8. **Agro-industry.** Agriculture is the primary industry in the rural areas of the country, representing approximately 20% of GDP. The agro-industry sector contributes nearly one fourth to the value of industrial production. Yet, agro-industrial exports account for only about 3% of total industrial exports, implying that a major portion of agro-industrial goods produced in Sri Lanka are consumed by the domestic market. The greatest potential for value-addition lies in the processed foods and beverages category and the scope for increased exports is considerable, given the nation's varied agroclimatic zones, fertile soils, and rich agricultural potential. Historically, limited efforts have been made in promoting strong bonds with the small farmers to develop agro-industry, such as development of mechanisms for outgrower schemes (i.e., linked to processing activities) and forward sales agreements. Improved marketing and postharvest systems are needed to generate significant rural growth and increased prosperity led by agro-industry.

9. **Technology.** Improved quality, reduced production costs, and increased productivity yields in Sri Lanka's industries should be improved through the development and use of more modern technologies. Historically, most technologies developed in state-owned research and development institutes have not been integrated into the manufacturing processes. Industry would be better served if technology were developed in joint collaboration with industrial users (e.g., SMEs) and transferred to the private sector through joint venture programs, public-private partnerships, etc.

10. **ISO Certification.** Many locally produced goods do not meet the quality and/or environmental standards established by the International Standards Organization (ISO). Furthermore, the state-owned Sri Lanka Standards Institute, which is responsible for issuing ISO certificates, lacks some of the necessary skills and testing equipment to issue such certificates. To promote export trade, the Sri Lanka Standards Institute must be enhanced, and the industry sector must be encouraged to obtain ISO certification for its products.

11. **Infrastructure.** Lack of suitable industrial sites and specialized infrastructure (e.g., manufacturing facilities, warehouses, waste management disposal facilities, offices etc.) contributes to inefficient processing and production, wastage, spoilage, and higher transportation costs in manufacturing process. The Investment Climate Study<sup>5</sup> identified poor

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<sup>5</sup> ADB and World Bank. 2004. *Sri Lanka: Improving the Rural and Urban Investment Climate*. Sri Lanka.

roads and lack of reliable power as the two primary hindrances to private sector development in the country. The feasibility of establishing industrial zones with an efficient logistic distribution system for SMEs should be reviewed.

12. **SME Financing.** A major impediment to SME growth is limited access to commercial financing (footnote 5). Cash-flow lending rather than collateral lending as well as alternative financial instruments to encourage banks and other financial institutions to fund sound SME projects will improve the ability of SMEs to obtain credit. Also, a conducive business environment (e.g., well-functioning credit bureau and small claims court) will stimulate financing to SMEs.

13. The Colombo Stock Exchange (CSE) has not been successful in attracting investors to provide risk capital for SME growth. A well-functioning capital market would better serve the financial needs and economic growth of SMEs.

14. **Business Support Services Facility.** The BSSF component of SMESDP supported a matching grant program to partially fund BDS for SMEs, and the establishment of five regional business development centers to develop the capacity of BDS providers. Further outreach is needed (i) especially in the non-urban/rural areas of the country, and (ii) for the development of women entrepreneurship to stimulate SME growth.

15. **Market Research and Marketing.** SMESDP provided TA<sup>6</sup> to develop a website to improve SMEs' access to market research and marketing in the domestic market. The website needs further improvement to include the global market.

16. **Lessons Learned.** The SMESDP credit assistance loan amounting to \$60 million was available to all SMEs throughout the country. However, (i) over 50% was disbursed to SMEs located in the four major industrial areas in the western region rather than reaching out to the lesser developed, non-urban/rural areas of the country; and (ii) almost 80% of the loans were used for refinancing existing loans rather than for expansion purposes. Other SME credit assistance loans at favorable rates have been introduced in the market. The Japan Bank of International Cooperation (JBIC) has provided three credit assistance SME loans, and an SME Bank was recently established by the Government to provide loans to SMEs. Therefore, no credit assistance loan is included in the TA.

### III. THE TECHNICAL ASSISTANCE

#### A. Impact and Outcome

17. Taking into account ongoing reforms in the SME sector, in part supported by SMESDP, the proposed TA will further support as well as assist in implementing reforms and removing barriers (paras. 3–15) to SME sector development.

18. The TA will prepare the overall design and principal implementation components of SMESDP II. The major components will (i) further support policy reforms for growth and development of SMEs, especially in the non-urban/rural areas; (ii) improve export trade, and in so doing, support improved quality, productivity, design and quality standards of Sri Lankan goods; (iii) increase the availability and methods of financing and decrease the cost of financing

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<sup>6</sup> ADB. 2001. *Technical Assistance to the Democratic Socialist Republic of Sri Lanka for Enabling Small and Medium Enterprises (SME) Growth*. Manila (TA3822-SRI).

for SMEs; and (iv) further strengthen the enabling business environment for SMEs. The TA design and monitoring framework is in Appendix 1. The initial poverty and social analysis is in Appendix 2.

19. The announced policy of the present Government elected in 2004 is to focus on SMEs. Many funding agencies have expressed interest in supporting SMEs. Except for JBIC, most other funding agencies have provided TA support and capacity building. As a collaborative effort, the TA and the structuring of the SMESDP II program loan will be implemented in close consultation with stakeholders.<sup>7</sup> The results of the Investment Climate Study (footnote 5) will also be used as a basis for strengthening the enabling environment for SMEs.

## **B. Methodology and Key Activities**

20. The TA will engage international and domestic consultants who will work closely with the executing and implementing agencies, market participants, and ADB in the four areas:

### **1. Policy Reforms**

21. The TA will evaluate the regulatory constraints that negatively affect SME economic growth and recommend further policy reforms that can significantly improve the growth and development of SMEs. Areas to be addressed include (i) taxes, (ii) alternate dispute resolution procedures, (iii) deregulation, (iv) the regulatory environment, and (v) Government services available to SMEs. The TA will also evaluate possible assistance to the Government to improve the implementation of SME policy and reform.

### **2. Increased Export Trade**

22. The TA will (i) evaluate the major constraints in export trade, (ii) recommend methods of increasing international exposure for SMEs, (iii) develop a plan to expand the usage of ISO certification including ISO 14000 by Sri Lankan industry, (iv) recommend reforms to improve the quality and design of goods for domestic consumption and export trade, and (v) recommend methods of implementing best-practice productivity on a sustainable basis.

### **3. Financing for Small and Medium Enterprises**

23. Taking into account work already done by the Government, ADB, and other funding agencies, the TA will (i) explore how to improve SME access to finance especially in the non-urban/rural areas of the country; (ii) recommend methods, products and/or services that can be used as incentives for banks and other financial institutions to increase financing to SMEs; (iii) recommend reforms to increase the availability of investment capital for SMEs, including the introduction of modern insolvency provisions, strengthening the financial industry, harmonization of taxes and laws between various financial institutes and/or financial instruments; and (iv) analyze trade financing activities of banks and other financial institutions and recommend changes to support export trade.

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<sup>7</sup> The World Bank, JBIC, European Commission, German Technical Cooperation (GTZ), Netherlands Government, Royal Norwegian Embassy (Norad), Swedish International Development Cooperation Agency (Sida), United Nations Industrial Development Organization (UNIDO), and United States Agency for International Development (USAID).

#### **4. Strengthening the Enabling Environment for Small and Medium Enterprises**

24. Taking into account work already performed by the Government, ADB, and other funding agencies, the TA will recommend how the enabling environment should be improved to stimulate SME growth, especially in the non-urban/rural areas of the country, and how the private sector can participate in implementing the recommendations.

#### **C. Cost and Financing**

25. The total cost of the TA is estimated at \$688,000 equivalent comprising \$495,000 in foreign exchange and \$193,000 equivalent in local currency. ADB will provide \$550,000 equivalent to cover the entire foreign exchange cost and \$55,000 equivalent of the local currency cost. The Government will contribute \$138,000 equivalent to fund counterpart staff, office facilities, and administrative services. The Government has been informed that approval of the TA does not commit ADB to finance any ensuing project. The TA will be financed on a grant basis by the Japan Special Fund, funded by the Government of Japan. The cost estimates and financing plan are in Appendix 3.

#### **D. Implementation Arrangements**

26. The Ministry of Finance and Planning will be the Executing Agency for the TA. The Ministry of Advanced Technology and National Enterprise Development will be the Implementing Agency. The TA will be implemented over 5 months, from November 2005 to April 2006. A team of five international consultants and five domestic consultants will provide a total of 21 person-months of consulting services. A team of international consultants from a firm will be engaged by ADB in accordance with its *Guidelines on the Use of Consultants*. Domestic consultants will be engaged in accordance with procedures satisfactory to ADB. The selection of the consultant firm will be based on the submission of a simplified technical proposal and effected by the quality- and cost-based selection process. An outline of the terms of reference is in Appendix 4.

27. In support of the TA activities, the Implementing Agency will provide (i) furnished office space for the consultants, and access to a conference room; (ii) secretarial support; and (iii) local communication facilities for the consultants in Colombo. The Government will provide counterpart staff, available on a part-time basis, as necessary.

28. The consultants will submit an inception report to the Government and ADB within 2 weeks of the start of work; an interim report—midway through the engagement—which would incorporate a draft policy matrix; and a draft final report 2 weeks before the end of the engagement. The interim and draft final reports will be discussed at a tripartite meeting involving the Government, the consultants, and ADB. The final report will incorporate results from the meeting and be made available 2 weeks from the date of the meeting.

### **V. THE PRESIDENT'S DECISION**

29. The President, acting under the authority delegated by the Board, has approved the provision of technical assistance not exceeding the equivalent of \$550,000 on a grant basis to the Government of Sri Lanka for preparing the Small and Medium Enterprise Sector Development Program II, and hereby reports this action to the Board.

## DESIGN AND MONITORING FRAMEWORK

Design Summary	Performance Targets	Data Sources/Reporting Mechanism	Assumption and Risks
<p><b>Impact</b> Increased economic growth and development</p>	<ul style="list-style-type: none"> <li>• Improved quality, production yields, design of products, and reduced production costs</li> <li>• Increased profitability of small and medium enterprises (SMEs)</li> <li>• Increased number of established SMEs throughout the country including in non-urban/rural area</li> </ul>	<ul style="list-style-type: none"> <li>• Periodic reports from the Central Bank of Sri Lanka</li> <li>• Periodic reports from Bureau of Statistics of Sri Lanka</li> </ul>	<p><b>Assumptions</b></p> <ul style="list-style-type: none"> <li>• Project design in implemented effectively.</li> <li>• Government and Asian Development Bank (ADB) sign loan agreement.</li> </ul>
<p><b>Outcome</b></p> <ul style="list-style-type: none"> <li>• Improved productivity and profitability of SMEs, including SMEs located in the non-urban/ rural areas of the country</li> <li>• Project design for SME Sector Development Program II agreed upon by Government and ADB</li> </ul>	<ul style="list-style-type: none"> <li>• Memorandum of understanding signed by Government and ADB during Loan Fact Finding and Appraisal Missions in the 2<sup>nd</sup> half of 2006</li> </ul>	<ul style="list-style-type: none"> <li>• Memorandum of understanding</li> </ul>	<p><b>Assumption</b></p> <ul style="list-style-type: none"> <li>• Effective stakeholder participation and sense of ownership are developed.</li> </ul> <p><b>Risks</b></p> <ul style="list-style-type: none"> <li>• Government priorities change.</li> <li>• Government seeks other sources of funding.</li> </ul>
<p><b>Outputs</b></p> <ul style="list-style-type: none"> <li>• Technical assessment and recommendations completed</li> <li>• Project design requirements accomplished</li> <li>• Design of a mutually agreed upon SME Sector Development Program II</li> </ul>	<ul style="list-style-type: none"> <li>• Technical assistance final report submitted to the Government and ADB by April 2006</li> </ul>	<ul style="list-style-type: none"> <li>• ADB document registration</li> <li>• Government document registration</li> </ul>	<p><b>Risk</b></p> <ul style="list-style-type: none"> <li>• Restricted availability of and access to information and government personnel</li> </ul>
<p><b>Activities and Milestones</b></p> <ol style="list-style-type: none"> <li>1. Analyze policy reform and areas of deregulation and recommend how to further enhance SME growth (by February 2006)</li> <li>2. Assess the adequacy of business development services, and propose measures for further improvement (by January 2006)</li> <li>3. Evaluate information technology systems available for SMEs and recommend initiatives and improvements to further improve market research and SME access to domestic and international markets (by December 2005)</li> <li>4. Develop a plan to implement a broad-based ISO certification program for goods produced in Sri Lanka (by January 2006)</li> <li>5. Assess barriers faced by SMEs and propose measures to improve export trade (by January 2006)</li> <li>6. Develop investment incentives to encourage financial institutions to lend to SMEs (by February 2006)</li> <li>7. Access the activities of state-owned research and development institutes and recommend methods to encourage private sector participation through technology transfer, joint ventures, etc. (by December 2005)</li> <li>8. Prioritize and recommend how to improve productivity in certain industries on a sustainable basis (by February 2006)</li> </ol>			<p><b>Inputs</b></p> <ul style="list-style-type: none"> <li>• ADB: \$550,000</li> <li>• Government: \$138,000</li> </ul>

## INITIAL POVERTY AND SOCIAL ANALYSIS

### A. Linkages to the Country Poverty Analysis

<b>Is the sector identified as a national priority in country poverty analysis?</b>	<input checked="" type="checkbox"/> Yes  <input type="checkbox"/> No	<b>Is the sector identified as a national priority in country poverty partnership agreement?</b>	<input checked="" type="checkbox"/> Yes  <input type="checkbox"/> No
<p><b>Contribution of the sector or subsector to reduce poverty in Sri Lanka:</b></p> <p>The project preparatory technical assistance (TA) for the Small and Medium Enterprise (SME) Sector Development Program (SMESDP) II will reinforce the achievements of SMESDP and assist in implementing reforms and removing barriers to SME sector development. The TA will focus on further support of policy reforms for growth and development of SMEs, especially in the non-urban/rural areas. Reforms will involve improving export trade, increasing the availability and reducing the cost of financial sources, and further strengthening the enabling environment, thereby reducing the vulnerability of the poor.</p>			

### B. Poverty Analysis

#### Targeting Classification: General intervention

<p><b>What type of poverty analysis is needed?</b></p> <p>The Program is indirectly pro-poor in supporting the three components of ADB's poverty reduction strategy: pro-poor sustainable economic growth, good governance, and social development. Pro-poor sustainable economic growth is to be achieved through the Program's focus on measures to improve SME economic growth and development, including the non-urban/rural areas, with the highest incidence of poverty in the country. Economic growth and development have been stagnant in the non-urban/rural areas. To support good governance, the Program will focus on policy reforms and improving the enabling environment, which will ultimately support sustainable economic development. Also, by focusing on the availability and cost of financing, it will be easier for more people, including women who generally receive no wages as household workers, to establish new SMEs or expand existing SMEs, thereby improving livelihood, employment possibilities, and social development.</p>
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### C. Participation Process

<p><b>Is there a stakeholder analysis?</b>                      <input checked="" type="checkbox"/> Yes                      <input type="checkbox"/> No</p> <p>Roundtable discussions will be held with the Ministry of Finance and Planning, the Ministry of Advanced Technology and National Enterprise Development, Sri Lanka's Standards Institute, Sri Lanka's Research and Development Institutes, Central Bank of Sri Lanka, and other relevant stakeholders including selected multilateral and bilateral organizations, to ensure participation of stakeholders in proposing quality action plans and recommendations.</p> <p><b>Is there a participation strategy?</b>                      <input checked="" type="checkbox"/> Yes                      <input type="checkbox"/> No</p> <p>During TA implementation, workshops will be held, with the representation and participation of key players in the SME sector.</p>
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### D. Gender Development

<p><b>Strategy to maximize impacts on women:</b></p> <p>By increasing the availability of SME financing, particularly in the rural area, women, who generally receive no wages as household workers, would be given the opportunity to establish their own business. Additionally, the services of skills business development centers should extend to the non-urban/rural areas of the country and focus on skills development for women entrepreneurs.</p> <p><b>Has an output been prepared?</b>                      <input type="checkbox"/> Yes                      <input checked="" type="checkbox"/> No</p>
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**E. Social Safeguards and Other Social Risks**

Item	Significant/ Not Significant/ None	Strategy to Address Issues	Plan Required
<b>Resettlement</b>	<input type="checkbox"/> Significant <input type="checkbox"/> Not significant <input checked="" type="checkbox"/> None		<input type="checkbox"/> Full <input type="checkbox"/> Short <input checked="" type="checkbox"/> None
<b>Affordability</b>	<input type="checkbox"/> Significant <input type="checkbox"/> Not significant <input checked="" type="checkbox"/> None		<input type="checkbox"/> Yes <input checked="" type="checkbox"/> No
<b>Labor</b>	<input type="checkbox"/> Significant <input type="checkbox"/> Not significant <input checked="" type="checkbox"/> None		<input type="checkbox"/> Yes <input checked="" type="checkbox"/> No
<b>Indigenous Peoples</b>	<input type="checkbox"/> Significant <input type="checkbox"/> Not significant <input checked="" type="checkbox"/> None		<input type="checkbox"/> Yes <input checked="" type="checkbox"/> No
<b>Other Risks and/or Vulnerabilities</b>	<input type="checkbox"/> Significant <input type="checkbox"/> Not significant <input checked="" type="checkbox"/> None		<input type="checkbox"/> Yes <input checked="" type="checkbox"/> No

**COST ESTIMATES AND FINANCING PLAN**  
(**\$**)

<b>Item</b>	<b>Foreign Exchange</b>	<b>Local Currency</b>	<b>Total Cost</b>
<b>A. Asian Development Bank Financing<sup>a</sup></b>			
1. Consultants			
a. Remuneration and Per Diem			
(i) International Consultants	345,000	0	345,000
(ii) Domestic Consultants	45,000	0	45,000
b. International and Local Travel	30,000	15,000	45,000
c. Communication, Translations and Reports	5,000	2,000	7,000
2. Seminars/Workshops	0	18,000	18,000
3. Miscellaneous Administration and Support Costs <sup>b</sup>	10,000	0	10,000
4. Contingencies	60,000	20,000	80,000
<b>Subtotal (A)</b>	<b>495,000</b>	<b>55,000</b>	<b>550,000</b>
<b>B. Government Financing</b>			
1. Counterpart Staff	0	58,000	58,000
2. Office Facilities and Equipment	0	50,000	50,000
3. Supplies, Utilities and Other Logistical Support	0	30,000	30,000
<b>Subtotal (B)</b>	<b>0</b>	<b>138,000</b>	<b>138,000</b>
<b>Total</b>	<b>495,000</b>	<b>193,000</b>	<b>688,000</b>

<sup>a</sup> Financed by the Japan Special Fund, funded by the Government of Japan.

<sup>b</sup> Includes office utilities, supplies, and secretarial expenses.

Source: Asian Development Bank estimates.

## OUTLINE TERMS OF REFERENCE

1. The team of consultants will consist of five international and five domestic consultants led by the international small and medium enterprise (SME) expert as team leader.

**A. SME Experts** (one international, 4 person-months; one domestic, 3 person-months)

2. The international expert will have an advanced degree in economics, finance, engineering, or business administration and a minimum of 15 years relevant experience in the SME sector of developing countries. The expert should also have relevant experience in Sri Lanka and/or other developing Asian countries.

3. The domestic expert will have a degree in economics, finance, or business administration and a minimum of 8 years relevant experience in the SME sector.

4. The SME international and domestic experts will work as a team to perform the **following tasks:**

- (i) After a review of studies, analysis, and discussion with major stakeholders, including the Asian Development Bank (ADB) and World Bank's Investment Climate Study for Sri Lanka<sup>1</sup> assess the strengths and weaknesses of the SME sector in the urban as well as non-urban/rural areas and lessons learned from past and ongoing interventions:
  - (a) Suggest policy reforms in the areas of taxes, the regulatory environment, and other areas that would significantly impact on the growth and development of SMEs throughout the country; and
  - (b) Recommend industries where deregulation could enhance SME growth.
- (ii) Recommend activities and interventions that are needed in the area of business development services, which would improve the growth and development of SMEs on a sustainable basis, especially in the non-urban/rural areas of the country.
- (iii) Assess the business support service facility activities financed through ADB's Small and Medium Enterprise Sector Development Program (Loan 1895-SRI):
  - (a) Substantiate which activities should continue to obtain further support and/or which activities should be added; and
  - (b) Design a program to increase women entrepreneurship, especially in the non-urban/rural areas of the country.
- (iv) Assess the information technology services offered by the Government to support SME growth and development, and recommend how to improve market information and market intelligence for SMEs, recommend additional support to improve SME access to the domestic and international markets.
- (v) Assess the SME sector to identify industries, geographical areas and strategies that have the greatest potential for growth on a sustainable basis.
- (vi) Evaluate the feasibility of establishing SME industrial zones to provide necessary infrastructure in specified regions of the country.
- (vii) Conduct a supply-chain analysis to determine constraints to the production and distribution of goods and services.

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<sup>1</sup> ADB and World Bank. 2004. *Sri Lanka: Improving the Rural and Urban Investment Climate*. Sri Lanka.

**B. Export Trade/Industrial Technology Experts** (one international, 3 person-months; one domestic, 2 person-months)

5. The international expert will have an advanced degree in engineering or a related field and a minimum of 15 years relevant experience in working with export trade, industrial and environmental technology, and International Standards Organization (ISO) standards. The expert should also have relevant experience in Sri Lanka and/or other developing Asian countries.

6. The domestic expert will have a degree in engineering or a related field, and a minimum of 8 years relevant experience in the areas of export trade and industrial technology.

7. The international and domestic experts will work as a team to perform the following tasks:

- (i) Evaluate the major constraints on export trade and recommend solutions on how to improve export trade, including policy reforms.
- (ii) Assess the technology presently used in manufacturing processes, evaluate why Sri Lanka SMEs do not adopt best practice productivity improvements, and recommend such improvements. Prioritize and substantiate which potential industries should be modernized to increase productivity yields, improve the quality and production of finished goods, reduce production costs, improve environmental standards, and provide Sri Lankan products with an export competitive edge.
- (iii) Assess the activities of state-owned research and development institutes and recommend (a) how technology can be developed to better suit market demand; (b) technology that should be developed and which will have the greatest positive impact on SME growth and development, and (iii) how the private sector can become involved with research and development in state-owned research institutes.
- (iv) Assess and prioritize which industries should be encouraged to focus on producing more value-added goods; develop a strategy and plan for implementing recommended changes.
- (v) Identify available technologies that should be introduced to support SME sustained development.
- (vi) Identify public sector investment priorities to support improved technology.
- (vii) Recommend modifications to the existing quality standards testing and certification system provided by the state-owned Sri Lankan Standards Institute, transform it into a modern testing and ISO certification institute meeting international standards.
- (viii) Assess the testing and certification of quality standards for goods produced in Sri Lanka to (a) recommend improvements in the Sri Lanka Standards Institute's methods and the scope of its presently testing standards, and (b) develop a plan to encourage industries to obtain ISO certification.

**B. Financial Markets Experts**

8. There will be two international and two domestic financial market experts.

- 1. **Business Financial Market Experts** (one international, 2 person-months; one domestic, 1 person-month)

9. The international expert will have an advanced degree in finance, economics, business, or a related field, and a minimum of 15 years relevant experience in working with finance and SMEs. The expert will have relevant experience in developing SMEs in other Asian countries.

10. The domestic expert will have a degree in finance, economics, business, or a related field, and a minimum of 10 years relevant experience in working with finance and SMEs.

11. The international and domestic experts will perform the following tasks:

- (i) Review products and services provided by the financial markets (i.e., bond and equity markets, bank, leasing, and other financial credit institutes and insurance companies) and recommend (a) improvement and/or introduction of methods, products, or services that can be offered as incentive to banks and other credit institutions to better serve the financial needs of SMEs (e.g., mezzanine financing, etc); (b) policy reforms and changes in the enabling environment to stimulate lending and investments (e.g., well-functioning credit bureau and small claims court); and (c) improved awareness of various commercial financial alternatives to SMEs.
- (ii) Closely coordinate with the consultants for the ongoing TA 4421-SRI Implementing Products and Services for the Domestic Debt Market.
- (iii) Assess the skills and needs of banks and other financial institutions to increase lending to SMEs, and provide recommendations on how skills development can be implemented.
- (iv) Recommend policy changes that will improve the quality of financial alternatives offered by credit institutes, including leasing companies and increase their availability to SMEs.
- (v) Assess the trade financing activities of commercial banks and evaluate (a) products and services offered and recommend changes to increase the availability of trade financing to SMEs; and (b) internal trade processing, assessment of pricing, risks and consequent pricing disciplines of commercial banks and make recommendations to improve the systems they currently use.

**2. Legal Financial Market Experts** (one international, 1 person-month; one domestic, 1 person-month)

12. The international expert will have a law degree, and a minimum of 15 years relevant experience working with commercial law, including debt recovery. The expert should also have relevant experience in commercial legal reforms in Sri Lanka and/or other developing Asian countries.

13. The domestic expert will have a law degree, and a minimum of 10 years relevant experience working with commercial law, including debt recovery. The expert should also have relevant experience in commercial legal reforms in Sri Lanka.

14. The legal experts will perform the following tasks:

- (i) Review present laws and planned reforms pertaining to debt recovery.
- (ii) Identify key issues for streamlining debt recovery actions.
- (iii) Recommend improvements to alternate dispute resolutions, which will improve the debt recovery system in Sri Lanka in general, and in SMEs, in particular.

**D. Postharvest and Agribusiness Development Specialist** (one international, 2 person-months)

15. The expert will have an advanced degree in agribusiness, agricultural economics, or a related field. The expert should have at least 10 years practical experience in working with agricultural input supply, especially technology transfer, mechanization, business investment, and supply chain management. Experience with policies on tariffs and duties for agriculture imports and bans of imports of agricultural raw materials, and fiscal policies for export-oriented agribusinesses is required. Prior experience working with South Asian countries and understanding of the business environment will be an advantage.

16. The expert will perform the following tasks:

- (i) Review past and ongoing interventions and existing sector studies—including the joint ADB-World Bank investment climate study for Sri Lanka (footnote 1)—particularly those dealing with agricultural diversification and agroprocessing, SMEs, agribusiness and horticulture development, to determine performance, reasons for success or failure, and lessons learned.
- (ii) Assess the agribusiness sector to identify crops and commodities, geographical areas, strategies and approaches with the greatest potential for growth and development.
- (iii) Identify key quality issues in high-potential crops and commodities and recommend assistance to overcome the constraints.
- (iv) Identify the priority subsectors for agribusiness development led by the private sector, and identify public sector investment priorities and a supporting agenda.
- (v) After a review of studies, analyses, and discussions with major stakeholders in agricultural policy issues, propose specific policy areas for further detailed study and analysis.
- (vi) Assess the status of postharvest systems and recommend improvements.

**E. Agricultural Marketing Specialist** (one domestic, 2 person-months)

17. The expert should have a degree in agriculture or agricultural economics with specialization in agricultural/livestock marketing and a minimum of 10 years in the field. Experience in market analysis, marketing infrastructure, and marketing policies for agricultural products is required.

18. The expert will perform the following tasks:

- (i) Assess the status of marketing systems and infrastructure, and recommend improvements.
- (ii) Examine the supply-and-demand situation and trends for key crops and commodities in the domestic market, taking into consideration competition from imports.
- (iii) Examine the market structure for key crops and commodities in the international market and evaluate current and future demand for exports.
- (iv) Assess the effectiveness of market information and market intelligence systems and recommend measures for improvement.
- (v) Determine the need for commodity marketing studies and assess the need for a key value chain.