Sector Road Map

1. Sector Performance, Problems, and Opportunities
   a. Sector Performance

1. Private businesses in the Maldives largely depend on tourism-related activities, construction, fisheries, agricultural commercialization, handicrafts, and associated sectors. Although the Maldives has one of the most liberal trade, labor, and investment regimes in South Asia, the Government of the Maldives plays a large role in the economy, indirectly limiting the scope for private participation. The businesses are concentrated in and around Malé, the capital of the country. The government has been intent on tapping the potential of the micro, small, and medium-sized enterprises (MSMEs) to create more jobs, particularly in the outer atolls, thereby achieving a more resilient and diversified economic base.

2. Overall sector profile of MSMEs. MSMEs are mostly engaged in retail trade. MSME participation in other service industries which contribute 79% of the GDP and include real estate, wholesale and retail trade, transport and communication, and financial services is limited. While a vast majority of MSMEs remain unregistered and operate informally, collectively they play a key role in providing goods and services in the local economy, and represent the backbone of the domestic labor force. However, the sector's contribution to gross domestic product has not shown any improvement.

3. Business ownership structure. Most MSMEs in the islands operate on a very small scale. Higher business concentration in the retail trade reflects its lower labor absorption capacity and expansion capabilities. 54.7% of the entrepreneurs are single operators, while 36.2% operate as family business units. This is partly due to the fact that small entrepreneurs are often compelled to adjust the scale of their business operation to suit the financial capacity in the absence of banking faculties for investment. Although the relationship between the family-operated business and the size or scale is not very clear, most MSMEs operate without external business partnerships or labor absorption.

4. Gender representation and distribution of economic opportunities. On most of the smaller islands there are relatively few women entrepreneurs. Women in the active age groups are restricted to businesses within the household social boundaries due to the responsibilities that large families entail. Women's entrepreneurial involvement is also largely restricted to the opportunities within their island because family bonds curb their mobility.

   b. Problems and Opportunities

5. Limited access to financial services. MSMEs face special challenges in tapping financial institutions because an enabling environment for access to finance is lacking—collateral requirements are stringent and capacity of financial institutions for lending to the MSME is limited.

6. A key reason for the difficulty of access is the absence of institutionally organized credit information, which causes the financial institutions to be conservative in their lending, charge high interest rates, and base lending decisions on collateral instead of cash flow.

---

1 In other sectors, MSME activities are primarily restricted to agriculture (2.6%), fishing (2.9%), business services (1.1%), art and handicrafts, and low-end tourism. Figures in Bracket indicate percentage contribution to GDP projected for the year 2011. No data is available for the Art and Handicrafts, and Low-end Tourism; and their contribution is negligible (Source: Department of National Planning, Republic of the Maldives).
7. The finance sector in the Maldives is underdeveloped and too small to provide enough financing for MSMEs. Total banking assets amount to Rf9.1 billion ($710 million) in five banks: Bank of Maldives (BML), State Bank of India, Habib Bank, Bank of Ceylon, and Hong Kong Shanghai Banking Corporation. The Maldives Islamic Bank was established last year but is still in its infancy. Nonbank financial institutions in the Maldives consist of (i) Allied Insurance Corporation, a local insurance company, and the offices of two Sri Lankan insurance companies; (ii) Maldives Finance Leasing Company; and (iii) Housing Development Finance Corporation, a specialized housing finance institution.

8. Lack of business support. Most private enterprises on the atolls are very small, often with three or fewer employees. Those running them often have no formal training in business or business management. The market for business development services is in its infancy, and the few services that exist are provided by the public sector in Malé and consist of skills-related training courses that do not necessarily target entrepreneurial activity.

9. Access to markets is a particular challenge in MSME development because of the nation’s remoteness, small domestic (island) markets, and scattered settlements. It is expected that gradual consolidation of the population on fewer islands, well served by maritime and civil aviation links, will greatly improve MSMEs' access to markets. In the interim, improving the quality of accessible market information can alleviate the situation.

10. Enabling technologies for MSME development. The combination of a dispersed geography and a poor network of banking and business development services causes the MSMEs outside Malé considerable logistical difficulties, and significant time and transport costs in accessing government, educational, technical support, and banking services. This is compounded by the fact that island communities have limited access to the internet.

11. To a limited extent, these difficulties may be ameliorated by (i) the government’s decentralization program, whereby some public services will be provided through province and atoll offices; (ii) the availability of BML mobile banking services; and (iii) the BML community banking service proposed to be established in a few of the island communities.

12. Against this background, the project will facilitate and enable (i) the use of innovative technologies to promote information and knowledge sharing between MSMEs, their business partners and customers, and with the government, and to create a platform for delivery of e-government and e-banking services; (ii) the implementation of a pilot project to demonstrate the use of information and communication technology and renewable energy in creating revenue streams for business development service centers (BDSCs) through a public-private partnership (PPP) model; and (iii) the establishment of a centralized and publicly accessible online database for judgment debts.

13. Legal and regulatory constraints. An adequate legal and regulatory environment is crucial for MSME access to finance but is lacking in the Maldives. For instance, the absence of a fully functional credit information bureau (CIB) and secured transaction registry, limited protection by the current system for registering mortgages over land, weak enforceability of finance leases and other contracts, and lack of civil procedure laws and commercial laws make for a weak regulatory environment that is unable to safeguard the interests of both MSMEs and financial institutions.

14. Skills deficiencies among youths and low participation of women. Efforts to define and create entrepreneurial opportunities for the poor, including women and youths,
and to enable skills development through business and vocational training have been limited so far.\(^2\) This has created reliance on migrant labor from neighboring countries.

2. **Government’s Sector Strategy**

15. The strategic action plan for Anne Dhivehi Rajje is the National Framework for Development, 2009–2013 published by the Government of the Maldives.\(^3\) The strategic action plan focuses on the various policy guidelines for interventions in key areas such as decentralization of governance, connectivity, healthcare, education, and youth and women development and reiterates that the new administration recognizes the potential of the MSME sector to create a more resilient and diversified economy and to add jobs, in particular on the outer atolls. The Government of the Maldives has all along recognized the MSME sector as a key driver for changing the government’s role from a direct provider of services to a facilitator of private initiatives in the economy, one of the fundamental requirements for improving efficiency and effecting good governance.

3. **ADB Sector Experience and Assistance Program**

16. The operational strategy of the Asian Development Bank (ADB) in the 2002 country strategy and program for the Maldives focused on reviewing the policy framework and operational and legal environment for MSME development.\(^4\) ADB approved technical assistance in 2005 to support development of MSMEs on the atolls by devising new financing mechanisms and market accessibility plans, and establishing centers for entrepreneurial training.\(^5\)

17. ADB also approved a technical assistance loan in 2008 for the Private Sector Development Project (PSDP) to minimize the problems of and improve the enabling environment for MSMEs.\(^6\) Capacity-development support was aimed at building knowledge, strategies, action plans, and policies to support effective PPPs and to overcome key financial market constraints, improve market links and business services, and rationalize state-owned enterprises (SOEs) in an orderly manner.

18. Under its follow-up intervention—the Inclusive Micro, Small, and Medium-Sized Enterprises Development Project—ADB intends to provide a combination of investment support and capacity-development assistance to help the government establish business development services and MSME financing instruments—including extension of the CIB, establishment of a new secured transaction registry, introduction of a credit guarantee scheme—that are sustainable and will strengthen the enabling environment for the private sector, with particular attention to the financial inclusion constraints that MSMEs face. The BDSCs, coupled with the launch of a business incubator program, will bolster human resource development by providing training in entrepreneurship, management, and technical skills for MSMEs and helping locate commercial opportunities in specific sectors.

19. **Establishing and extending the credit information bureau.** The PSDP supported the establishment of a CIB. By the end of 2011, the eight-member institution had completed three cycles of loading data; of around 25,000 records of consumers and commercial loans (lending facilities) that were initially submitted. Seven of the eight members are already

---

\(^2\) According to the Seventh National Development Plan, the Maldives has one of the lowest labor force participation rates in South Asia (47.7%).


members. However, there is still a need to extend the CIB to capture data from later submissions, including from utility companies and newly established financial institutions.

20. **Line of credit facility and credit guarantee fund.** The PSDP provided a $3 million line-of-credit facility (LCF) to widen access to finance for MSMEs. The follow-up project will provide an additional LCF ($8.5 million), cofinanced by the Islamic Development Bank, along the lines of the first design. It will also support the government in setting up a credit guarantee fund that further boosts credit availability through partially guaranteeing credit facilities where MSMEs have collaterals that do not match the current lending norms.

21. **Start-up training through business development service centers.** The PSDP established two BDSCs. They will be the chief vehicle for the delivery of business development service products to MSMEs in a drive to create cluster development in targeted regions. Under the follow-up, all seven regions will have their BDSCs. About 60 MSMEs in fisheries, tourism, and arts and handicrafts have benefited from the $3 million LCF, which helped expand their business operation, develop their capacity for accessing finance from the banks, and formalize the MSME sector through government registration.

22. **Privatization support.** The PSDP assisted the government in the pilot privatization of three enterprises: Nasandhura Palace Hotel, Maldives National Shipping Corporation, and Maldives Industrial Fisheries Company. ADB helped develop criteria and procedures for privatizing these SOEs in a transparent, rules-based manner. ADB also assisted in the restructuring of State Electronic Company as a prelude to future privatizations. ADB’s holistic support will include recommendations for the design of a labor adjustment program to cushion the transient employment impact of SOE privatization. ADB will draw lessons from this experience to guide future assistance in widening the scope for SOE privatizations.

23. **Private–public partnerships.** Capacity-development assistance has been provided for strengthening the enabling environment for the private sector, for structuring PPPs, and for MSMEs, as well as for the use of this modality in the power and transport sectors. Under the follow-up project, it is proposed to set in place a suitable risk-sharing mechanism between public and private sector to establish the citizen service centers on a PPP format.

24. **Bolstering the legal and institutional framework.** MSME development is premised to a large extent on an enabling legal, regulatory, and institutional framework. ADB will assist the government in further strengthening the institutional framework in the Maldives by initiating new legislations and amending existing ones to secure the confidence of both lenders and investors in the enforcement of their rights. Legal support will be provided to draft various financial and commercial laws, including the civil procedure code and personal and corporate insolvency laws, and new electronic commerce and data protection laws.
Problem Tree for Micro, Small, and Medium-Sized Enterprises

Effect:
- Non-inclusive economic growth
- Crowding and migration in Malé

Causes:
- Constrained growth of MSMEs in the atolls
- Insufficient training and market links
- Inadequate access to finance
- Inefficiencies of scale due to lack of adequate information
- Poor legal and regulatory framework and weak legal enforcement
- Insufficient training and market links
- Lack of credit information, lack of collateral
- Lack of environment-friendly initiatives
- Insufficient training and market links, limited innovation
- Poor coordination, weak market links, limited innovation
- Lack of internal capacity, inadequate training and skills development
- High cost of finance, lack of credit information, lack of collateral
- Poor information sharing, lack of environment-friendly initiatives

Proposed Private Sector Development Project, phase 2 interventions (MSMEDP):
- Component A: Strengthening building business support infrastructure
- Component B: Improved access to finance
- Component C: Enabling technologies for MSME development

MSMEs = micro, small, and medium-sized enterprises.
## Sector Results Framework (Micro, Small, and Medium-Sized Enterprises Development)

<table>
<thead>
<tr>
<th>Country Sector Outcomes</th>
<th>Country Sector Outputs</th>
<th>ADB Sector Operations</th>
<th>Planned and Ongoing ADB Interventions</th>
<th>Main Outputs Expected from ADB Interventions</th>
</tr>
</thead>
<tbody>
<tr>
<td><strong>Outcomes with ADB Contribution</strong></td>
<td><strong>Indicators with Targets and Baselines</strong></td>
<td><strong>Outputs with ADB Contribution</strong></td>
<td><strong>Indicators with Incremental Targets</strong></td>
<td><strong>Pipeline Project:</strong></td>
</tr>
<tr>
<td><strong>1. Mechanism for evidence-based SME policy formulation established</strong></td>
<td>Drafted and revised commercial laws and regulations, e.g., Credit Information Bureau Act and regulations, Secured Transaction Registry Act and regulations, draft Civil Procedure Code, draft insolvency laws.</td>
<td>Relevant legislation established to support MSMEs development and formalization of the sector</td>
<td>Implementation of the MSME Act (approval scheduled in 2011) with relevant regulations in 2012 and 2013</td>
<td><strong>Inclusive Micro, Small, and Medium-Sized Enterprises Development Project, to be approved in 2012 ($10.02 million, of which $5.57 million is loan and $4.45 million is grant)</strong></td>
</tr>
<tr>
<td><strong>2. Further expanded and strengthened MSMEs sector</strong></td>
<td>Reduction in unemployment by 1–2 percentage points</td>
<td>Low-cost financing scheme for supporting MSMEs developed and implemented</td>
<td>One scheme developed and implemented in 2012. Two other schemes developed and implemented in 2013.</td>
<td>Parallel cofinancing from the Islamic Development Bank with $10.3 million loan</td>
</tr>
<tr>
<td></td>
<td>Reduction in proportion of population whose income is less than $1 a day by 5%–10%</td>
<td>More women obtain self-help grants</td>
<td>15%–20% of LCF loan and cost-sharing facility to be targeted at women and young entrepreneurs</td>
<td><strong>Ongoing project:</strong></td>
</tr>
<tr>
<td></td>
<td>Number of MSMEs registered with the MED registry system increased by 20%–30%</td>
<td>Provinces operate business development service centers</td>
<td>BDSC operations established in all seven provinces</td>
<td><strong>Private Sector Development Project, approved in 2008 (technical assistance loan of $7.5 million), which is to be closed by the end of March 2012</strong></td>
</tr>
<tr>
<td></td>
<td>BDS capacity boosted and network of BDSCs strengthened, and approaching sustainability in business operations by providing client fee-based BDS to over 1,500 new or existing MSMEs</td>
<td>Introduction of new technologies for MSME development</td>
<td>MSME portal and judgment debt database, and solar-powered citizen service centers through PPP framework</td>
<td><strong>Greater capacity of women and the young to operate MSMEs</strong></td>
</tr>
</tbody>
</table>

**ADB** = Asian Development Bank; **BDS** = business development services; **BDSC** = business development services centers; **LCF** = line of credit facility; **MED** = Ministry of Economic Development; **MSMEs** = micro, small, and medium-sized enterprises; **PPP** = public–private partnership; **SMEs** = small and medium-sized enterprises.