

## Lessons from Past Support to Micro, Small, and Medium-Sized Enterprises in the Pacific

### I. INTRODUCTION

1. **The coronavirus disease (COVID-19) is causing a devastating impact on small, already vulnerable island countries.** The COVID-19 pandemic has created socioeconomic upheaval across the Pacific developing member countries (DMCs). It has been destroying jobs and livelihoods in small island developing states where employment and economic opportunities are already limited, mainly due to constraints on the private sector. ADB estimates that total global economic losses from the COVID-19 pandemic could range from \$5.8 trillion to \$8.8 trillion—equivalent to 6.4%–9.7% of global gross domestic product.<sup>1</sup> The proportionate impact could conceivably be worse in the Pacific DMCs due to their remoteness, small size, wide geographic dispersion, and narrow economic bases. Their inherent exposure to disasters triggered by natural hazards has already exacerbated the pandemic's damaging effects.<sup>2</sup> Most Pacific DMCs generally have less capacity and resources to cope with shocks on multiple fronts, thus putting society's poor and most vulnerable to an elevated socioeconomic risk. This will potentially set back recent hard-won development gains and drive more households into poverty.

2. **Pacific micro, small, and medium-sized enterprises are the hardest hit.** Micro, small, and medium-sized enterprises (MSMEs) in the Pacific are critical to employment and livelihoods, but their ability to outlast the pandemic's effects is limited. They lack the capital or finance to withstand the effects of prolonged border closures, tourism shutdowns, and lockdowns. About 89% of businesses in Pacific DMCs, most of which are MSMEs, reported adverse effects from the pandemic, with 91% faced with reduced revenues.<sup>3</sup> About 66% of the businesses have lowered operational costs to counter a drop in income levels.<sup>4</sup> The economic disruption caused by the pandemic has also affected MSME access to supply chains and markets. By August 2020, 31% of businesses had closed (30% temporarily and 1% permanently), and 36% reported a partial reduction in operations (footnote 4).

3. **Targeted responses to help affected MSMEs survive and recover from the crisis can still be learned from past programs.** In collaboration with development and other stakeholders, Pacific governments have announced measures such as concessional loans and moratoriums on financial obligations to help keep businesses solvent. This support is likely to drain quickly, given the uncertain length of the COVID-19 outbreak, ongoing restrictions, and possibly second and third waves of the pandemic. During this period, MSMEs will continue to have acute needs, which goes beyond financial support and involves consumers' well-being, disruptions to supply chains, and evaporating business opportunities. It is imperative that the limited support is targeted, well-utilized, and reaches the intended MSMEs. Lessons from past programs targeting MSME and finance sector development in the Pacific can inform the design of Asian Development Bank (ADB) operations in relation to the COVID-19 pandemic, including the proposed regional technical assistance (TA) on Supporting Recovery by Micro, Small, and Medium-Sized Enterprises in the

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<sup>1</sup> ADB. 2020. [COVID-19 Economic Impact Could Reach \\$8.8 Trillion Globally](#)—New ADB Report. News release. 15 May.

<sup>2</sup> Fiji, Solomon Islands, Tonga, and Vanuatu were struggling to cushion the impact of COVID-19 when tropical cyclone Harold struck in April 2020 and caused them widespread physical and economic damage. Vanuatu was also affected by floods and ashfall from the Tanna volcano. The national economic response plans of these countries had to deal with disasters of multiple kinds. Pre-COVID-19, Samoa has been fighting a severe measles outbreak in late 2019.

<sup>3</sup> Pacific Trade Invest. 2020. [Impacts on Businesses in the Pacific](#). *PTI Pacific Business Monitor*. Survey 5—August 2020.

<sup>4</sup> By August 2020 about 49% of the businesses, including MSMEs have reduced work hours, 43% have reduced staff numbers, and 33% have reduced their employees' wages.

Pacific from the Effects of the COVID-19 Pandemic. This summary will focus on: (i) lessons learned from ADB MSME operations in the Pacific; (ii) relevant lessons learned from the thematic evaluation of ADBs broader MSME operation; and (iii) relevant lessons learned from other development partners MSME operations in the Pacific.

## II. LESSONS LEARNED FROM ADB's MSME OPERATIONS IN THE PACIFIC

### A. TA 8729-Regional: Establishment of the Pacific Business Investment Trust Fund and Technical Assistance for the Pacific Business Investment Facility<sup>5</sup>—Closed

4. Engaging local talent instead of engaging international consultants to identify local businesses for TA support can result in more effective business development. Building the capacity of local consultants, trainers, and business associations over time will contribute to greater efficiency and sustainability of TA interventions. It takes significant time and effort to establish relationships and trust with local small and medium-sized enterprises (SMEs) and financial institutions in the Pacific region. As such, the Business Investment Facility was able to field missions in 7 of the 13 countries and hold 650 business meetings, utilizing 79% (\$4.8 million) of the allocated funding of \$6.1 million. A total of 277 businesses received formal business advice against the target of 185.<sup>6</sup> Expansion of support to all 13 countries would have required more funding to mobilize a greater number of consultants.

5. Besides SME advisory support, future ADB interventions should address financial institutions' capacity constraints and SME industry value chain impediments. A holistic approach in designing SME support programs that includes capacity building of local consultants, trainers, and business associations, and establishing relationships and trust with key stakeholders is important to ensure effectiveness and sustainability.

### B. Grant 0392 and 0539-Samoa: Samoa AgriBusiness Support Project<sup>7</sup>—Ongoing

6. There will be a stronger case at the project closure to consider applying the project's lessons more widely across relevant future ADB interventions in the Pacific. However, there are observations and recommendations from the mid-term review mission and the follow-up mission that should be considered in designing any future support to MSMEs in the Pacific.

7. Coordination efforts between ongoing programs in-country need to be strengthened. The change proposed to the project's collateral coverage brings it more into competition with the New Zealand Ministry of Foreign Affairs and Trade-supported Samoa Small Business Enterprise Centre programme. The midterm review noted the strong need for ADB, Australian Department of Foreign Affairs and Trade, and New Zealand Ministry of Foreign Affairs and Trade to consult among themselves and find a solution to avoid potential conflict and competition between Samoa Agribusiness Support Project and Samoa Small Business Enterprise Centre.

<sup>5</sup> ADB. 2014. [Technical Assistance for Establishment of the Pacific Business Investment Trust Fund and Technical Assistance for the Pacific Business Investment Facility](#). Manila.

<sup>6</sup> ADB. 2019. [Technical Assistance Completion Report: Establishment of the Pacific Business Investment Trust Fund and Technical Assistance for the Pacific Business Investment Facility](#). Manila.

<sup>7</sup> ADB. 2014. [Report and Recommendation of the President to the Board of Directors: Samoa Agribusiness Support Project](#). Manila

### C. Loan 2686/Grants 0226 and 0425-Papua New Guinea: Microfinance Expansion Project<sup>8</sup>—Closed

8. The project provided capacity-building support to participating financial institutions and gathered extensive data on their performance. Still, this data was never analyzed either to determine the impact of the capacity building activities or to help identify a further capacity building intervention that may have improved participating financial institutions performance. It was also evident that the financial institutions' capacity-building needs varied, requiring the project to move away from generic capacity-building support and tailor it to the financial institutions' identified needs.

9. Training provided to financial institutions, clients, staff, and others should focus on impact (behavior change) rather than outputs (number of people trained). For example, while the project financial literacy program provided training to more than 200,000 people and was considered successful, little impact on the financial behaviors of those who received the financial literacy training has been demonstrated.<sup>9</sup>

### III. RELEVANT LESSONS LEARNED FROM THEMATIC EVALUATION OF ADB'S BROADER MSME OPERATION

10. A thematic evaluation of the ADB's support for SMEs during 2005–2017 found these operations to have been less successful on average than ADB's operations overall.<sup>10</sup> The findings showed that the many operations focused on providing SMEs access to financing through credit lines and on-lending often did not benefit the underserved SMEs. As a result, there was little evidence that these operations helped improve SME sector financing.

11. In the Pacific, there are no ADB projects that support financing through credit lines, mainly due to financial institutions being highly liquid. However, the study made a number of recommendations for improving ADB's institutional approach to SME operations, which can inform project design in the Pacific. Among the factors identified as key to optimizing success in projects that aims to improve SME access to finance were (i) the selection of the right participating financial institutions—those with a commitment to serve SMEs; (ii) capacity development of participating financial institutions and SMEs; (iii) sub-loans designed with a focus on reaching underserved SMEs; (iv) good performance indicators and collection of monitoring data on targeted groups; and (v) regular monitoring for possible mid-course adjustments.

12. The same evaluation found that the SME operations' business environment aspects performed well overall, with criteria ratings of *relevant*, *effective*, and *efficient*. The success of the program was driven by (i) strong government and stakeholder ownership of the program; (ii) close consultations with stakeholders, including women and members of the private sector; (iii) sustained engagement in addressing key issues; (iv) policy actions that triggered long-lasting effects on the policy and institutional environment; and (v) technical assistance that supported the capacity development of implementing agencies and the achievement of policy actions that specifically address institutional constraints such as regulatory and administrative processes and procedures. ADB's Pacific Private Sector Development Initiative was not assessed specifically in

<sup>8</sup> ADB. 2010. [Report and Recommendation of the President to the Board of Directors: Microfinance Expansion Project for Papua New Guinea](#). Manila.

<sup>9</sup> ADB. 2018. [Report on the Impact Evaluation of a Financial Inclusion Program in Papua New Guinea](#). Consultant's report. Manila (TA 8993-REG).

<sup>10</sup> ADB Independent Evaluation. 2018. [Support for Small and Medium-Sized Enterprises, 2005–2017: Business Environment, Access to Finance, Value Chains, and Women in Business](#). Manila.

the evaluation, but its robust program to improve the region's broader business environment will greatly complement the activities and outputs of the proposed technical assistance that specifically focuses on MSMEs.

13. The Independent Evaluations Department's 2020 synthesis note also highlights important lessons learned from ADB supported MSME projects from the past.<sup>11</sup> The note takes a very pragmatic approach and captures lessons from past financing support provided to MSMEs to cope with the 1997–1998 Asian financial crisis and the 2008–2009 global financial crisis. The broader lessons around: (i) providing immediate support to microfinance operations; (ii) targeting the underserved MSME subsector to broaden the impact of MSME development support during a crisis; and (iii) accompanying interventions that support increased SME access to finance over the long- term with complementary policy and regulatory measures for sustained and optimal development of SMEs, is highly relevant to ADB programs designed for the Pacific in the aftermath of the COVID-19 pandemic.

#### **IV. RELEVANT LESSONS LEARNED FROM OTHER DEVELOPMENT PARTNERS MSME OPERATIONS IN THE PACIFIC**

##### **A. Enterprise Challenge Fund**

14. The Enterprise Challenge Fund was an A\$20.5 million program funded by the Australian Government and managed by AusAID. It offered a competitive opportunity for businesses to obtain grants from A\$100,000 to A\$1.5 million for commercializing business projects that addressed local market failures. In 2013, an assessment was done on the program and the relevant lessons learned<sup>12</sup> include:

- a. The need to review the management team's 'capital' when assessing the commercial viability and potential development impacts of projects submitted for funding support. Funding support for production improvements and marketing activities may not be sufficient for sustainable benefits to disadvantaged suppliers. Funding or technical support to strengthen the business's management capital should be determined either from the outset or at an early stage in its expansion.
- b. Improving access to finance for women and making this an explicit requirement under the program. Women entrepreneurs contribute to their economies, yet the International Finance Corporation found that cultural barriers limit access to finance for women. Women in developing economies are more likely to run smaller business operations but are disproportionately affected by the investment climate. Despite increasing efforts to improve women's access to finance, the assessments finding were aligned to the study undertaken by International Finance Corporation whereby it was found that the programs that focused on women business owners who have graduated from microfinance remain small and siloed and often lack targets or monitoring and evaluation frameworks.<sup>13</sup> Additional investment in access to finance, particularly for women, needs to be considered.

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<sup>11</sup> ADB. 2020. [Synthesis Note No. 3 \(COVID Series 1\): Responding to COVID-19: Lessons from Previous Support to Micro, Small, and Medium-Sized Enterprises](#). Manila.

<sup>12</sup> Australian Agency for International Development. 2013. [Learning from the Enterprise Challenge Fund: Accessing Finance in the Pacific Islands](#). Sydney.

<sup>13</sup> International Finance Corporation. 2011. [Strengthening Access to Finance for Women-Owned SMEs in Developing Countries](#). Washington, DC.

- c. The need to independently verify, review, and, if required, amend business plans proposed by relatively inexperienced SME owners. Technical support to suppliers may need to be implemented and, where appropriate, can be partly covered by the funding. Microfinance providers are likely to collaborate with business projects that offer a reliable market for rural suppliers. This facility could be built into the supported project from the outset.
- d. The timely and generous grant provided is only one element of a package of assistance for maximizing the pro-poor and broader impacts of a business project. Sufficient and flexible resources for tailoring financial and technical support activities for individual projects need to be developed along the way.