

SME access to financing: capacities matter as much as resources

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Hervé Gallèpe and Grégoire Chauvière Le Drian work on mechanisms to support private sector development in Sub-Saharan Africa at Agence Française de Développement. In this article they present possible intervention methods for public fund donors that can help improve SME access to financing.

Donors must not simply focus on adopting strategies based on providing financing, they must also focus on demand. One of the reasons why it is difficult for SMEs to access financing is they are unable to attract investors and bankers. Donors can help improve the business environment and directly support SMEs in order to help them upgrade and make them eligible for financing.

Over the past twenty years, SSA countries have been liberalizing their economies within the framework of structural adjustment and/or following their World Trade Organization membership. The fact that they find themselves facing international markets constitutes both an opportunity and a challenge. Indeed, the liberalization of capital flows provides new growth opportunities for these countries because they gain access to new markets and can attract FDI flows. However, countries which are ill-prepared for this opening up or cannot develop their productive sectors risk being left on the sideline in terms of trade flows and may fall so far behind that they will never catch up. Yet SSA countries are in unequal positions in the face of this opening up and development will be difficult for many countries where productive sectors are uncompetitive. This is one of the reasons why an effective SME fabric needs to be developed in these countries.

SMEs must upgrade

Official development assistance supports this process by helping to modernize the productive sector, particularly for SMEs. There are three main reasons to justify this SME strategy: SMEs are factors of growth, they have considerable positive social and environmental impacts and they can, in some cases, supplement the role of the State in the provision of public goods. Financing is, of course, needed to develop SME fabric – and AFD provides financing (lines of credit, guarantees, equity investments) – but

SMEs must above all be eligible for this financing, i.e. they must be capable of taking it on board. Demand must be worked on in addition to supply and one of the first ways to work on demand is to help create a favourable business environment for investment and develop the productive sector. Indeed, private sector development must be supported by efficient markets, skilled human resources and, finally, by good governance at all political and economic levels. More generally speaking, it must be supported by a favourable investment climate. Such a climate can only emerge in most SSA countries if macroeconomic and institutional environments are improved, transaction costs are lowered, investment regulations are reformed, infrastructure is developed... There are also more direct ways to act on demand via business upgrading programs comprising vocational training programs, capacity building for marketing analysis, technology upgrading and financial restructuring. This support for demand can also involve chambers of commerce, chambers of trade or consular chambers. All these operations must make SMEs more competitive and thus more likely to attract bankers and other investors.

The role of donors

Interventions by public authorities with donor support can remove a number of stumbling blocks to SME development. They can, indeed, improve the investment climate via regulatory, legal or institutional measures in terms of taxation, certification, trade promotion... Donors can also play a more direct role in supporting businesses. Their operations today appear to focus on two main areas: firstly, they provide direct aid to businesses so that they can meet the demands of the banking sector and have easier access to formal financial systems and, secondly, they strengthen ties between SMEs by creating business clusters (competitiveness hubs) and promoting exchanges with major groups (industrial partnerships, subcontracting,...). The aim is to upgrade SMEs via specific programs and make them eligible for financing available on the market.

AFD strategy

AFD is convinced that the problem of corporate access to financing is as important as the problem of the availability of the financing itself. Its strategy is consequently based on two additional approaches focusing on its range of financing and on strengthening players to make them eligible for this financing. AFD has supported a number of projects which have shown conclusive results. Projects focusing on demand can be broken down into two categories: projects that focus on the SME environment and projects that directly focus on businesses. The first type involves projects to organize industries, support intermediate organizations and strengthen competitiveness hubs or local productive systems. The second mainly involves trade capacity building programs, technical assistance, restructuring (productive or financial) and upgrading. Thanks to these programs businesses can upgrade, attract capital investors and make an efficient use of the financing available for their growth. AFD is also developing its range of SME financing in line with its strategies to strengthen SMEs. The ARIZ guarantee fund (insurance for private investment financing risks in AFD's areas of activity) is one tool that AFD promotes for risk sharing mechanisms. Moreover, AFD has implemented a mesofinance program to provide financing to SMEs that do not have sufficient guarantees to meet the requirements of traditional banking circuits and are outside the capacities of microfinance institutions. These loan programs are completed by equity investments that provide capital resources and support businesses in their development via technical assistance. Finally, AFD provides banks with subsidized refinancing with the concessional element designed to help the final recipients, SMEs, strengthen their capacities.

All AFD activities have a cross-cutting focus on environmental and social responsibility policies that also applies to its partners (working conditions, waste management, environmental preservation...). Allocated aid must boost incentives to develop in a sustainable manner and refinancing allocated by AFD to banks for SMEs is subject to environmental and social requirements. AFD also considers that major groups – including banks – can be vehicles to disseminate this social and environmental responsibility process and can consequently help transfer best practices.

Madagascar's SME Solution Center

The SME solution center project (CSPME) which was set up in 2005 met AFD's objective to support Malagasy exports without creating new structures. AFD consequently used this existing structure that IFC set up and financed during its first three years before it reached financial autonomy. The CSPME gathers all the services required for SME development in the same place: information, training, access to financing (IFC particularly promoted an SME assistance fund with technical assistance from Business Partners – South Africa). AFD made a proposal to CSPME to add a specific component for exporting businesses. The aim was to provide these businesses with technical assistance in order to fill a gap identified during a preliminary diagnostic. AFD consequently financed part of the center's operating costs for this component.

Website: http://www.ifc.org/ifcext/africa.nsf/Content/SME_Solutions_Centers

Biography

<p>Hervé Gallèpe has been following issues relating to private sector support since 2002 (corporate upgrading programs, trade capacity building...). He also has extensive experience of France's representation to the European Union. Hervé Gallèpe is a graduate in public law and political science.</p>	<p>Grégoire Chauvière Le Drian is an economist and has been a member of AFD's <i>Financial and Private Sector Division</i> since 2007. He contributed to the definition of AFD's strategy to support the private sector. Grégoire Chauvière Le Drian is a graduate of the <i>École normale supérieure</i>, holds an <i>agrégation</i> and a DEA postgraduate diploma and is a graduate of the IEP in Paris.</p>
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