

TC ABSTRACT

I. Basic Project Data

▪ Country/Region:	REGIONAL/IDB
▪ TC Name:	Facility to Boost Private Sector Growth in Small and Island Countries
▪ TC Number:	RG-T3502
▪ Team Leader/Members:	STEVENSON, CLAUDIA (IFD/CTI) Team Leader; PELAEZ ZAMBRANO, PAULA (INO/NFP) Alternate Team Leader; SMALL, CHARLENE MARIE (INO/SMC); ROBBERECHTS, ELIZABETH M. (INO/IEN); GRECO, MARIA SOFIA (LEG/SGO); GONZALEZ ALZUALDE, YOHANA BEATRIZ (IFD/CTI); PETERS, MARK CHRISTOPHER (NFP/CGY)
▪ Taxonomy:	Research and Dissemination
▪ Number and name of operation supported by the TC:	N/A
▪ Date of TC Abstract:	17 Jun 2019
▪ Beneficiary:	SMEs in Small and Island Countries, Business Support Organizations
▪ Executing Agency:	INTER-AMERICAN DEVELOPMENT BANK
▪ IDB funding requested:	\$ 1,250,000.00
▪ Local counterpart funding:	\$ 0.00
▪ Disbursement period:	36 months
▪ Types of consultants:	Firms
▪ Prepared by Unit:	Competitiveness, Technology and Innovation Division
▪ Unit of Disbursement Responsibility:	Institutions for Development Sector
▪ TC included in Country Strategy (y/n):	No
▪ TC included in CPD (y/n):	No
▪ Alignment to the Update to the Institutional Strategy 2010-2020:	Productivity and innovation

II. Objective and Justification

- 2.1 The objective of this TC is to increase competitiveness and accelerate economic development in Small & Island Countries (S&I) by lowering transactions costs for private sector activity. The specific objectives are to (i) build capacity in SMEs for project preparation related to access to finance; (ii) lower access to finance preparation costs and (iii) share relevant knowledge related to SME access to finance.
- 2.2 S&I Countries face common challenges to sustainable and economic growth, including small internal markets, low levels of innovation and productivity, and limited regional integration. These economies are small and open economies that depend mainly on tourism or on the exploitation of natural resources and show not only persistent declining growth rates over time but high levels of volatility. In most of the countries, the top three exports account for 70% of total exports, and merchandise exports have typically been unsophisticated, ubiquitous and low value-added commodities like bauxite, oil and sugar. Although, in previous decades many of the countries had moved away from agriculture to more service based economies, in per capita terms, growth in the region had declined from 3.71% in 2007 to 1.43 in 2017. Public debt also increased for most the S&I countries, exceeding 90% of GDP on average. Constrained by this debt overhang, the region's level of investment/GDP is currently around 26 %, half of that of the rest of the world. The resulting fiscal context underscores the importance of export-oriented private sector development as an engine of growth for the region.

- 2.3 The main challenges that firms in S&IC face are: (i) small markets that hinder scaling up. While the lack of large markets hinders the decision to undergo large, indivisible investments and achieve greater economies of scale, small markets also imply higher fixed costs with more concentration and less competition. In addition, the existing political economy of some of the larger, existing firms and vested interests hinder the possibilities for expansion of newer and more dynamic firms; (ii) vulnerability to external shocks. Smaller economies are more vulnerable to external shocks, heightened by the lack of economic diversification showing a need for private sector led activity and development of new economic sectors; (iii) Fragmentation and adverse geographical conditions. The geographic conditions of these countries further contribute to its economic vulnerability as the region is one of the most exposed to natural disasters in the world. This increases the risk premium for both public and private investments; (iv) Low technological readiness and innovation. Most of the S&IC have low scores for innovation and technology and the technological adoption of new technologies is weak; as well as the use of traditional technologies; (v) weak institutional capacity. The public institutions in charge of supporting SME growth are generally weak in the region and are not able to provide the services that MSME need to access to finance; and (vi) weak capacity of the SMEs. This challenge are reflected in the relatively low rankings in the Doing Business Ranking for the S&IC countries of 56 in average for Doing Business (100 being the optimal) and for access to credit of 38, reflecting the difficulties of doing business and accessing credit in these countries.
- 2.4 To overcome these challenges, actions to support private sector investment and access to finance are critical to boost employment and skill development, upgrade value chains, and bring innovation to increase productivity, connectedness and competitiveness. Most of the S&CI countries have public or private institutions that support capacity building for MSMEs, but they are usually underfunded or not able to address the specific requirements needed by the MSMEs to access credit.

III. Description of Activities and Outputs

- 3.1 To achieve the stated objective, the TC will be structured in 3 mutually reinforcing components:
- 3.2 • **Component 1. Market information and product feasibility.** The objective of this component is to provide public and private stakeholders with tools to facilitate informed decision making and increased knowledge on products, markets and the use of new technologies. Under this component the TC will finance: (i) consultant services to analyze the demand and feasibility of economic sectors and industries, products and technologies; and (ii) studies and tools that will facilitate access to credit, enhance the availability of credit information with data analytics and reduce related risks in the S&IC countries. Examples of the studies to be undertaken are studies of export market potential of a nontraditional agribusiness product, application of a new digital technology on an established service or market, and the creation of an SME portal to gather SME information and develop SME Credit Risk Scoring.
- 3.3 • **Component 2. Capacity Building and Project Preparation to facilitate access to finance for SMEs and strategic projects in S&I.** under this component the TC provide technical support to SMEs to build capacity for accessing financial markets and for due diligence preparation of strategic projects, either directly or through business support organizations. In this regard, this component will: (i) Identify relevant public or private business support organizations in the S&IC, identify current gaps to service the potential beneficiaries and provide technical assistance to strengthen their services; (ii) support MSMEs and strategic projects to acquire the required environmental, social, legal, technical, financial and governance standards in line with local, international and multinational requirements. In order to promote sustainability and build capacity at the local level, the TC will seek to work with business or industry associations to leverage

and support their ongoing capacity building efforts. The selection process of the beneficiaries from this component will require that (i) the firm is currently undertaking a financing process for a high growth potential project with economic impact; (ii) that there is an identified gap in the firm's capacity to achieve the required environmental, social, legal, technical and financial standards; (iii) that the proposed project has a positive impact in development (iv) that the service provided increases the capacity of the firm or of the business support organization in a sustainable manner; and (v) the intervention has a demonstrative effect and scalability.

- 3.4 • **Component 3. Knowledge generation and diffusion.** this component will support: (i) the generation and dissemination of knowledge stemming from the other components as a public good accessible to other firms in the region and other stakeholders that work with capacity building for private sector; (ii) monitoring and evaluation of activities including data collection from the beneficiaries.

IV. Budget

Indicative Budget

Activity/Component	IDB/Fund Funding	Counterpart Funding	Total Funding
Market information and product feasibility	\$ 200,000.00	\$ 0.00	\$ 200,000.00
Capacity Building and Project Preparation	\$ 850,000.00	\$ 0.00	\$ 850,000.00
Knowledge generation and diffusion	\$ 200,000.00	\$ 0.00	\$ 200,000.00

V. Executing Agency and Execution Structure

- 5.1 The execution of this TC will be carried out by the Bank through the Competitiveness and Innovation Division (IFD/CTI) in coordination with BID Invest.
- 5.2 Prospective projects to be supported by the TC will be demand driven and will be identified either directly or through business support organizations.
- 5.3 As the proposed TC will be carried out across 9 countries in two different regions and will deal with different public and private stakeholders in these countries, the coordination of activities is more efficient when is executed by the Bank.

VI. Project Risks and Issues

- 6.1 The main risks identified are low demand for the services to be provided. This risk will be mitigated by: (i) working closely with business support organizations; (ii) proactively identify potential industries and services with high impact and (iii) dissemination of knowledge and lessons learned.

VII. Environmental and Social Classification

- 7.1 The ESG classification for this operation is "undefined".