

MICRO ENTERPRISE POLICY

[DRAFT]

**NATIONAL ENTERPRISE DEVELOPMENT
AUTHORITY**

Micro Enterprise Policy

1 Introduction

- 1.1 According to the Development Framework 2006-2016, about 500,000 new micro enterprises will be erected throughout the country and about 10% of the existing micro businesses will be promoted to the category of small industries. As a result of these developments, both unemployment and poverty in the country will drop by a 2%.
- 1.2 As the national apex agency for enterprise development in the country, it is the responsibility of National Enterprise Development Authority (NEDA) to monitor the progress of the achievement of those goals and ascertain constraints for the development of micro enterprises from the macro-(policy), meso-(financial and non financial structure-Micro Finance industry & BDS industry) and micro- (Retailer-Micro Finance Institutions and BDS providers) perspectives.
- 1.3 In the absence of a National Policy on Micro Enterprises, NEDA is not in a position to undertake the tasks assigned to it in the area of micro enterprise development especially the growth of micro enterprises as envisaged in the National Development Framework.
- 1.4 Micro Finance Strategy is the key component of the National Micro Enterprise Policy. Having observed that there is no micro finance strategy, the following salient points are also mentioned in the Development Framework referred to "At present a microfinance policy is not found in the country. In consequence, there is no institutional mechanism to coordinate the microfinance interventions with other policies, which have been formulated for rural development. In this environment the sector has been fragmented. Responsibilities in the sector are scattered among different agencies, which in part have quite different views of the role of the microfinance sector in the development process of Sri Lanka."

2 Micro Finance Strategy

- 2.1 We understand that a microfinance strategy is being formulated with a view to undertake effective supervision and regulation of microfinance agencies by the Central Bank and to create legal provision for enhancing the participation of non-governmental organizations (NGOs) and other private sector initiatives in microfinance.

- 2.2 It is also expected that the Government will undertake institutional reforms in National Development Trust Fund, Cooperative Rural Banks, Regional Development Banks and Samurdhi Banking Societies-the microfinance institutions operated by the Government under the proposed micro finance strategy to expand the outreach and increase the efficiency of those micro financing institutions.
- 2.3 Although micro finance is the key factor for development of micro enterprises and provision of abundant, sustainable and enduring sources of funding is vital for the survival of micro enterprises, micro enterprises policy is not exclusively confined to a micro finance strategy. Increasing access to micro finance and supporting entrepreneurship are equally important for sustainable development of micro enterprises. Hence a comprehensive micro enterprises policy has to be formulated to address both the financial and technical issues
- 2.4 Ministry of Enterprise Development & Investment Promotion (MED&IP) has already formulated the National Enterprise Policy. Within this policy framework SME Policy is being formulated by NEDA with JICA assistance. Formulation of Micro Enterprise Policy is the next step of Sub-sector Enterprise Policy Development process within the Framework of National enterprise Policy

3 *Micro Enterprise Policy*

- 3.1 Micro enterprises generally defined as very small businesses with five or fewer employees play an important role in the economy of Sri Lanka. Most of these enterprises are developed and managed by self-employed persons and located in non-urban areas. Those enterprises serve mainly the regional markets and add value to the resources available in the nearby areas
- 3.2 Community-based micro enterprise development programs initiated by Govt. Agencies (Janasaviya, Samurdhi and Rural Industries Development programs) and non-governmental organizations (NGOs) during the last twenty five years have been assisting emerging entrepreneurs start and operate micro enterprises. Those micro enterprise development programs provide training on business management and skills development, marketing advice, access to loans and develop peer networks like Societies of Samurdhi beneficiaries, Vidatha Entrepreneurs Associations, Sanasa Societies and Nucleus- the associations of Producers of similar products and services...
- 3.3 These micro enterprise development programs have not brought out the expected economic changes and rural poverty and regional economic

imbalance continues to prevail. Hence there is a felt need to review and revisit strategies advocated in those micro enterprise development programs and introduce a new micro enterprise policy with innovative development strategies.

4 Objective

- 4.1 The objective is to provide the conditions necessary for the growth and development of the micro enterprises sector by developing a favourable policy and regulatory environment, strong and sustainable institutions providing financial and non-financial services to meet the demand of micro enterprises, improved access of low-income and disadvantaged micro entrepreneurs (including disabled and victims of the civil conflict) to financial and business services and expanded regular and permanent flows of resources for investment in micro enterprises.

5 Goal

- 5.1 The overall goal of the New Micro Enterprise Policy is to expand the economic opportunities through sustainable dynamic and compatible micro enterprise development and transfer 20% micro enterprises in the informal sector to formal sector within next three years.

6 Transformation Approach

- 6.1 The advocated development approach is transformation of micro enterprises from informal sector to the formal sector. It is a challenging task in the management of economic development. Hence innovative policy instruments have to be developed to suit the location specific and sector-specific factors to make the development approach successful.
- 6.2 The informal sector consists of minute-scale, self-employed activities with or without hired workers, in most cases family members. These activities are at a low level of technology and conduct in non-formal organizational setups escaping and avoiding the attention of the administrative machinery responsible for law and regulations.

6.3 All the self-employed persons are not entrepreneurs and those with entrepreneurial traits only can transform the activities from informal sector to formal sector, Hence appropriate public policy instruments as development strategies have to be developed taking into consideration the following characteristics of the informal sector to transform micro enterprises from informal sector to the formal sector as small enterprises.

- Informal sector enterprises usually employ fewer than five workers, mostly immediate family members

The informal sector is heterogeneous: major activities are retail trade, transport, repair, maintenance, construction, personal and domestic services and manufacturing

- Entry and exit are easier than in the formal sector
- Capital investment is generally minimal
- Work is mostly labor intensive, requiring low-level of skills
- Workers learn the skills on the job
- The employer-employee relationship is often unwritten and informal
- The informal sector works in conjunction with, rather than in isolation from the formal economy

7 Strategies

7.1 The following series of development strategies will be implemented to transform micro enterprises from informal sector to formal sector

- Rationalize use of resources of the existing institutional infrastructure of community-based micro enterprise programs/projects that provide technical assistance and financial assistances for micro enterprises
- Enable low-income people to use entrepreneurship as a pathway out of poverty
- Introduce group guarantee, credit guarantee, matched savings accounts for business capitalization and other cost sharing mechanism and other innovative micro finance products and grant exemptions from the provisions made in the Debt Recovery Act for the applications made by micro enterprises through Credit Guarantee Funds
- Grant exemptions from the provisions made the Termination of Employment Act for micro enterprises for a limited period
- Encourage micro enterprise as re-entry strategy for prisoners and rehabilitated youths
- Introduce sub-contracting arrangements as a means to enter formal sector

- Provide exit strategies for micro enterprises to discontinue non-viable business operations
 - Formulate a micro finance strategy to outreach potential micro entrepreneurs and to develop regulatory framework for providers of micro finance to promote competition and discourage malpractices of informal money lender
- 7.2 Over the last three decades the Govt. allocated funds through Janasaviya, Samurdhi and similar other programs like Gama Neguma, Janapubuduwa that help low-income people to start and sustain micro enterprises
- 7.3 NGOs like Sarvodaya program also funded livelihood projects to start micro enterprises. Recently Mercy Corps and other INGOs and International Agencies such as IOM also provided technical and financial assistances to develop micro enterprises.
- 7.4 Advocating principles of cooperative movement Sanasa through its development finance arm also provide technical and financial assistance to micro enterprises Thus we have a diverse institutional framework for development of micro enterprises, but most of the micro enterprises still remain in the informal sector...
- 7.5 Hence, there is a felt need to undertake post-evaluation and progress review of all those programs through a comprehensive study with a view to devise a mechanism for rational use of funds allocated for micro enterprise development
- 7.6 Samurdhi Program and Jana Pubuwa focus on entrepreneurship development as a pathway out of poverty. A series of entrepreneurship development products are available in the market. Govt. authorities like IDB, NYC Samurdhi Authority have introduced entrepreneurship development programs. Bi-lateral donors like GTZ have introduced CEFE and Multi-lateral donors like ILO have introduced SIYB as entrepreneurship development products... There are no standards developed for those products and no rating mechanism to evaluate those products and delivers of those products generally introduced as business development service (BDS) providers .is established..
- 7.7 Low-income people using entrepreneurship as path way out of poverty should be given the freedom to select the product and the provider. For this purpose they should be given vouchers to procure entrepreneurship development service products
- 7.8 Loans are the only financial service products offered to micro enterprises, and most of them have caught in the debt trap. Hence there

- is a pressing need to introduce alternative financial tools such as match savings accounts, credit guarantee scheme have to introduce.
- 7.9 Micro enterprises reluctant to increase their workforce and offer regular work and permanent jobs because of the provisions made in the Termination of Employment Act. Hence, exemptions under this Act have to be provided for a limited period to the micro enterprises to expand the employment opportunities.
 - 7.10 Micro Enterprise Policy should encourage micro enterprises as a prisoner re-entry strategy and as a means for gainful employment for rehabilitated youths . Finding employment for released prisoners has become a problem. Many employers refuse to provide jobs for those have a prison record. Most of the released prisoners have limited job experience. Self-employment can be a natural fit for released prisoners and rehabilitated youths.
 - 7.11 By introducing sub-contracting arrangements relationship will be developed between enterprises in the formal sector and the micro enterprises in the informal sector and thereby facilitating latter's entry to the formal sector
 - 7.12 Most of the business development service providers hardly mention the exit strategy for entrepreneurs. Demise of enterprise is sometimes unavoidable. Hence entrepreneurs have to be given options to start alternative enterprises when it is clear that his present enterprise is not viable. Hence introducing exit strategy is important especially for micro enterprises as it may be the livelihood of the entrepreneur...

8 *Implementation*

Implementation of micro enterprises policy has to be undertaken by the public institutions come under the purview of respective line ministries and by the Provincial Councils as micro enterprise is also a devolved subject.

9 *Monitoring & Evaluation*

MED&IP may undertake monitoring of all micro enterprise development programs conducted by public agencies, NGOs, INGOs, Cooperative entities, Business Chambers and other private sector BDS providers. The new monitoring mechanism developed by NEDA consisting of Nucleus, Enterprise Forums, Policy Advocacy Committee, Enterprise Facilitation

Forum may be the appropriate institutional mechanism to monitor and evaluate the Micro Enterprise Policy.

10 Policy Review

Micro Enterprise Policy review may be undertaken by the National Enterprise Council come under the purview of MED&IP and the Parliamentary Advisory Committee on MED&IP.