



Innovative Financing Mechanism for MSMEs: Jamaica

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Innovative Financing Mechanism for MSMEs

Overview

- Creative and innovative Micro, Small and Medium-Sized Enterprises (MSMEs) are important drivers of economic growth, equity in income distribution and sustained development in Jamaica. While several countries use the term 'SMEs' (Small and Medium Enterprises),
- The portfolio Ministry in Jamaica uses the standard term 'MSMEs' signaling the need to include "micro" enterprises the policy development process.
- MSMEs enterprises collectively play a significant role in the creation and retention of wealth while generating significant opportunities for employment and sustenance as well as providing the support needed for private sector growth and expansion

Country Background

- Population of 2.7 million
- Labour Force 1.3 million
- Unemployment rate 13.1%
- Growth Rate – 1.3%
- In February 2017, Fitch confirmed Jamaica's sovereign credit rating of B (stable outlook).
- Economic Activity
 - Services : 64% - Tourism, banking, data processing
 - Industry : 29% - manufacturing, commerce, mining
 - Agriculture: 6.5%

Introduction

- MSME & The Economy
 - MSMEs are significant drivers of growth in Jamaica
 - 97.6% of classified taxpaying businesses are MSMEs
 - Employment - Over 50 % of Jobs created
 - Taxes – 20% of taxes
 - Foreign exchange saving/earnings – import substitution and supply chains

Introduction

- Estimated that there are about 200,000 formal SMEs and between 200,000 and 400,000 micro-entrepreneurs
- According to the Ministry of Industry, Commerce and Agriculture and Fisheries (MICAF), MSME contribution in terms of jobs reaches levels of 90%.

Introduction

- Social Inclusion
 - Wider income distribution – over 400,000 own account workers
 - Women in business – over 49% of MSMEs are owned and operated by Women
 - Youth - significant employment opportunities for youth employment
 - Social enterprises – social value creation

The Jamaican MSME sector

■ Definition

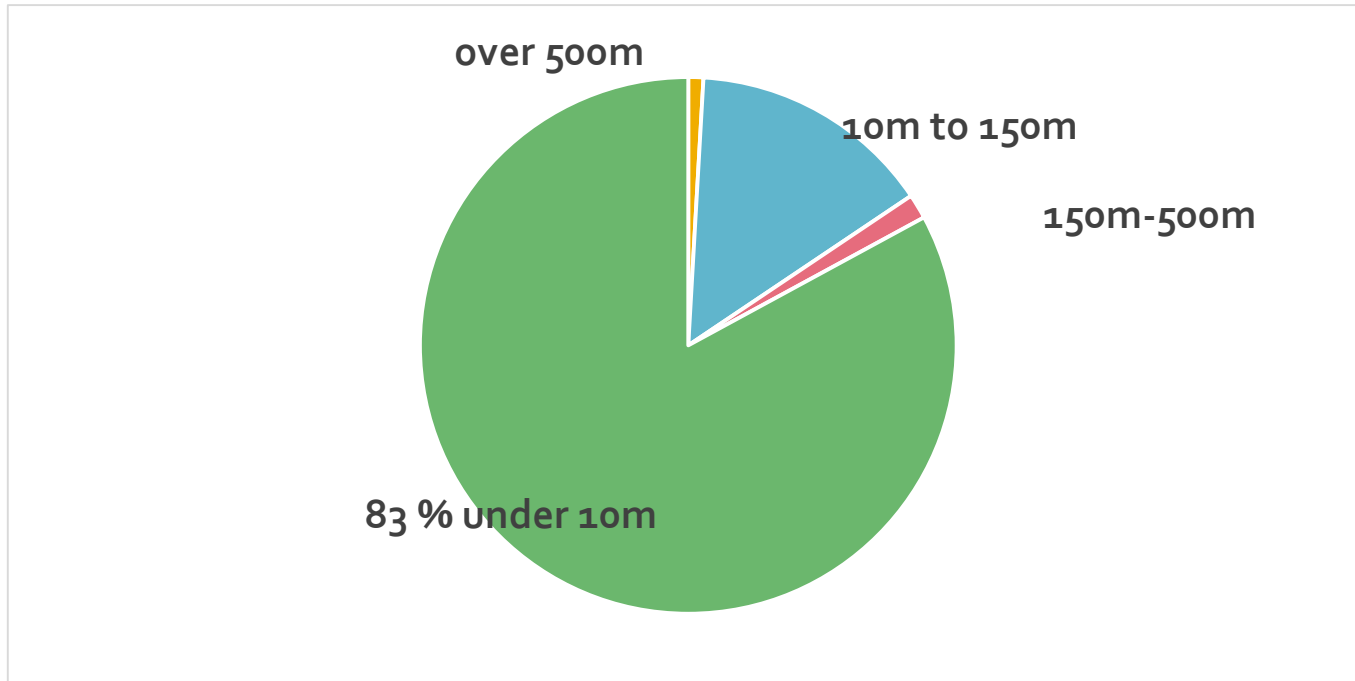
Jamaica's Revised MSME Definition

	PRIMARY INDICATOR	SECONDARY INDICATOR (For Guidance Purposes Only)
Firm Category	Total Annual Sales/Turnover	No. Employees
Micro	≤J\$15 million	≤ 5
Small	> \$15 million ≤ J\$75 million	6 – 20
Medium	> J\$75 million ≤J\$425 million	21 – 50

Issues Of the sector

- Issues faced
 - 1) Need for Business environment reform – formality, taxation, registration
 - 2) Adequate Business development support
 - 3) MSME Financing
 - 4) Innovation and Standards – Jamaica is 'efficiency driven' economy and not 'innovation' driven
 - 5) **high level of business discontinuances**
 - 6) **early-stage entrepreneurial activity** - either actively trying to get a business started (nascent entrepreneurs) or owning a young business that is less than 42 months

Composition



MSME Policy Landscape

- Establishment of the MSME Policy Office
- MSME & Entrepreneurship Policy
- MSME Policy Elements
 - Business development support, financing, social value creation, entrepreneurship, business environment, cross cutting themes
- Regional Collaboration on MSMEs
- Public Procurement Regulations
- Small Business Development centre Model

MSME Financing

- **Finance is one of the major** challenge facing MSMEs in Jamaica in terms of their limited ability to access adequate and/or serviceable financing sources.
- MSME Financing Taskforce Report (2015) – demand side & Supply side issues
- Access to finance Project/Working Group
- Growth Council, World Bank
- Financial Inclusion Strategy -

MSME Financing

- Policy strategies place emphasis on innovative mechanisms to increase the supply of financing to the sector that are appropriate, affordable and accessible throughout the MSME business lifecycle
- In terms of access, greater emphasis will need to be placed on using the Secured Transactions Regime to improve the acceptance of non-traditional collateral such as accounts receivable, equipment and intellectual property.

Financing Challenges

- Unavailability of adequate financing;
- High financing costs (high interest rates);
- Lack of appropriate financing – a preponderance of loan funding and inadequacy of non-loan financing (equity) that would better accord to firms' business and product life-cycles;
- Inadequacy of MSMEs to access financing even when funding is available; and
- Underservice by the private financial system (financial exclusion).

Financial System Participation

- The *Jamaica: National Financial Inclusions Strategy (NFIS), 2016* indicates that 27% of all formal small and medium enterprises (SMEs) have a bank loan, or access to credit, which is below the average of 48% in Latin America and the Caribbean (LAC).
- Over 40% of firms in Jamaica consider access to finance to be a major constraint but it is more acute for the small firm where 47% indicated it was a major constraint (compared with an average of 32% in the LAC region).
- The 2008 PSDP survey revealed that 57.9% of MSMEs used their own savings to start their business, 27.5% used funds from family members, 8.4% from credit unions while approximately 17% were able to source funds from banks.
- More than half (53.2%) of the MSMEs surveyed continued to use their own savings to finance business activities, 16% relied on family members, 12.4% accessed funds from banks and 5.6 % from credit unions.

Financial System Participation

- The lack of access to capital remains an impediment to the growth and development of the MSME sector and calls for a comprehensive approach and strategy to address the needs of the sector over the entire business and investment life-cycle. However, this is only one side of the coin, as the capacity of MSMEs to effectively access and manage financing remains a key issue.

Supply Side Issues

- Promote and/or facilitate the establishment of systems that encourages suppliers of credit to target MSMEs
 - Lifecycle financing
 - Equity
 - Debt instruments
- Expand special Lines of Credit at [concessionary] rates that will support the productive sector.
- Incentivize financial institutions, especially commercial banks, to make more loans available to businesses in the rural areas.

The Junior Stock Exchange

- The Jamaica Stock Exchange Junior Market offers an alternative equity financing option to small and medium businesses.
- It is designed to attract new capital from equity investors, encourage new start-ups and provide financing to existing businesses, thereby enabling small businesses to participate more effectively in the country's economic development process.
- Investors and small and medium businesses have displayed confidence in the Junior Market since 2009 with 33 listings up to December 2016 and over J\$5billion in capital being raised.
- However, these 33 companies still represent only a small percentage of formal small and medium enterprises.

The Junior Stock Exchange

- Capital Raised on the Jamaica Junior Stock Exchange for the period April 2009-

	2009	2010	2011	2012	2013	2014	2015	As at June 2016	TOTAL
Listings	1	7	4	4	7	3	1	6	33
Capital Raised	100	895	953	399	936	718	250	927	5,179

Secured Transaction Regime

- The OAS (Department of International Law Secretariat for Legal Affairs) has noted that:
 - *"Wealth in Latin America has remained almost exclusively land-based. Consequently, when assets are physically located in Latin America or the Caribbean, lenders are constrained by outdated laws that are largely based on real property regimes. Developing modern legal frameworks will foster the necessary transition to enable financing secured by personal property in order to help businesses, especially MSMEs, gain access to affordable credit."*
- MSMEs do not have the typically acceptable assets to serve as collateral.

Secured Transaction Regime

- In January 2014 the Government of Jamaica introduced the Secured Transactions Regime with the passage of the Security Interests in Personal Property Act (SIPPA) and the establishment of a National Collateral Registry
- With the Passage of the SIPPA Jamaica moved to 7th in the Doing Business Report in terms of access to credit

Secured Transaction Regime

- Diversify the classes of assets that can be used as collateral
- Files secured interest in personal property
- Secondary market for tradeable assets

Demand Sides issues

- **More funding to the sector** – Increase the quantity of funds available for MSME Financing
- **Interest Rates:** A challenge to MSMEs borrowing is that frequently they are required to pay higher interest rates than are typically faced by other borrowers. To establish systems that encourage financing institutions to offer lower interest rates to MSMEs
- **Capacity building support** – Instruments that are aligned to support and capacity measures
- **Diversified Products** - Include special loan programmes and financing windows that target qualified Women-Owned Businesses, youth-owned businesses and persons with disabilities operating businesses.

Financing Framework

- Wholesaler – Development Bank or Government Institution
- Retailer – Commercial Banks and Credit Unions
- Micro financing institutions - DBJ has lent over \$4.6 billion to Micro Finance Institutions (MFI) since the Micro Finance Window was established in 2009.

Dormant Funds Proposals

- Dormant Funds Proposals - to use unclaimed (dormant) funds in the banking and life insurance sectors to provide a pool of sustainable loan funds (Dormant Funds Scheme) to support MSMEs

Loan Guarantees

- Explore the development and utilization of guarantee systems to support SME financing.
- **Access to Finance Project - World Bank supported (Us\$20 M)**
 - a) Improving the enabling environment for access to finance for MSMEs, including by encouraging the development of financial instruments, such as leasing and factoring;
 - b) encouraging the development of private equity and venture capital (PEVC), through investing into an SME fund and reforming the related legal, regulatory, and tax regime
 - c) capacity building for MSMEs to improve their bankability.

Credit Enhancement Fund (CEF)

- The Credit Enhancement Fund (CEF) focuses on addressing problems related to the limited collateral capacity of firms in Jamaica
- The CEF provides partial loan guarantees to approved AFIs for loans given to MSMEs which are unable to meet AFIs collateral requirements.
- The CEF also acts as an incentive for lenders to increase their MSME loans portfolio by providing additional security coverage on loans to MSMEs for projects geared towards growth and development.

Credit Enhancement Fund (CEF)

- 50% of DBJ-funded SME loans up to J\$15M
- 80% of Energy Loans up to a maximum of J\$15M
- 80% of *SMALL LOANS up to J\$6.25M up to a maximum of J\$5M

Credit Enhancement Fund (CEF)

- During its history, the CEF has provided over 300 guarantees, mobilizing close to US\$9 million to cover US\$18 million in loans (47% coverage on average).
- On an individual basis, the CEF can cover up to 50% of a loan amount (80% for climate friendly projects), with a limit of up to approximately US\$115 thousand.

Credit Enhancement Fund (CEF)

CEF Loan Approvals and Guarantees Since Inception 2010 (by year)			
	Loan	Guarantee	#
Mar-10	30,000,000	8,320,000	4
Mar-11	10,800,000	3,956,000	3
Mar-12	34,700,000	10,750,000	3
Mar-13	254,969,378	166,797,000	108
Mar-14	225,994,000	83,957,150	26
Mar-15	487,378,123	218,662,568	51
Mar-16	539,201,456	282,331,343	56
TOTAL	1,583,042,957	774,774,061	251

Foundations for Competitiveness & Growth Project

- Jamaica Foundations for Competitiveness and Growth Project
 - Small Business Development.
 - Supply-Chain Productivity Improvement

Funded with US\$4.5 million, is designed to drive economic development by increasing the impact of businesses on the economy.

Goal – to increase the productivity within businesses which cause an increase in exports and, or reduce imports through import substitution.

Grants are also offered to upgrade and support enterprises' competencies, knowledge and skills within successful supply chains/

Jamaica Venture Capital Programme

- Established by the Development Bank of Jamaica (DBJ), with technical assistance and financial support from the Inter-American Development Bank's, Multilateral Investment Fund (MIF).
- Due to a number of factors, among these being the absence of an environment conducive to long term private capital development.
- The projects is a new approach by the DBJ, to create sustainable development of the VC industry, by focusing on the establishment of an ecosystem conducive to venture capital development
 - partnerships with private sector interests in the development of projects which impact entrepreneurs, fund managers and investors.
 - A key aspect of the ecosystem development is the establishment of an appropriate legal and regulatory framework for venture capital and private equity in Jamaica.

Jamaica Venture Capital Programme

- a dynamic venture capital industry in Jamaica represents a viable option for creating greater access to long term 'patient' financing, particularly equity capital, to high potential SMEs, in Jamaica, allowing them to invest in the start-up, expansion and growth of their enterprises.
- The current venture capital ecosystem in Jamaica has a number of gaps that inhibit the development of the industry, and the DBJ interventions are aimed at the development and execution of programmes, over the medium term, to address these gaps. The model being pursued recognizes that an effective, sustainable, long term venture capital market will need to be private sector driven.
However public policy intervention is needed to create the necessary incentive to catalyse private capital formation and venture capital investment.

Jamaica Venture Capital Programme

- The model being pursued has been utilized, with the assistance of the MIF, in other programmes such as the Inovar Program in Brazil. The model involves the development of a programme of activities, aimed at providing the training, tools, mechanisms, knowledge and infrastructure needed by stakeholders to develop the VC market.
- JVCP include the training and capacity building of SMEs and entrepreneurs, to improve their readiness for investment, building the expertise of local fund managers and investors, as it relates to the venture capital asset class, and partnering with eligible fund managers in the development of local venture funds.

Other Alternative Financing

- Receivables Financing - World Bank loan to establish platform for Receivable financing
- Angel investor networks - Promote and facilitate the use of Angel Investing (convertible debt) to fund MSMEs.

Recommendations

- Alignment of financing with Capacity building
- Continue to promote the development of a regional stock exchange.
- Educate small enterprises on the merits of equity financing and the options available.
- Continue collaboration with the private sector toward the further development of a venture capital ecosystem and the use of angel financing that will provide opportunities for funding for MSMEs.

Recommendations

- Explore bilateral (eg. CBI) agreements where members of the Diaspora could direct portions of their Company's Profit Tax to support local fund for venture development
- Explore the establishing of DIASPORA angel and venture funding, offering requisite incentives
- Greater financial inclusion and financial literacy
- Innovative financing not tied to collateral

Conclusion

- Several initiatives have been implemented by the Government to support the growth and development of the sector. Despite the several initiatives implemented by Government, improving access to capital by MSMEs remains extremely critical to the growth and development of the MSME sector.

End of Presentation
