Portfolio of Innovative Ideas on SME Growth and Entrepreneurship

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About the Private Sector Development Policy Innovation Lab

Currently, the World Bank and governments around the world have a very limited range of policy instruments that are typically used for trying to foster small and medium enterprise growth and entrepreneurship. The *Private Sector Development Policy Innovation Lab*, a collaboration between the World Bank's Development Research Group and the Innovation, Technology, and Entrepreneurship Practice, held a competition in which researchers from within and outside of the World Bank were asked to propose new ideas for policies in this area, motivated by economic theory and existing research findings. More than 70 initial submissions were received from around the world. The fifteen ideas profiled here were selected as finalists, and have developed full concept note templates of 8-9 pages around these ideas which can serve as a basis for discussions with policymakers, or for the initial preparation of a World Bank project that uses this idea. A pitch event will be held on May 28, 2015 to allow the originators of these ideas to succinctly explain them to World Bank operational staff working on SME projects. World Bank staff working on SME projects can also directly contact David to learn more about any of the ideas contained here and obtain the full templates.

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The Portfolio

The ideas proposed by the finalists cover a range of different types of innovations: from untested ideas motivated by theory and research in other branches of economics, through to design changes or tweaks to existing types of programs. They also attempt to alleviate a number of different constraints facing SMEs, help target programs directed towards SMEs better, and ultimately increase firm productivity, innovation, and exporting. Executive summaries of the ideas are listed approximately by theme below, although many proposals cover a range of themes.

	Increasing Exports	Markets and Value Chains	Capital and Innovative Financing	Targeting of Programs	Improving Business Skills	Improving the Investment Climate
Online Platforms, Market Access and SME Growth	X	X				
An ExPrize: Using prizes to encourage exports and learn about exporters	X		X			
Fashion Forward – The Fashion Global Value Chain	X	X			X	
P4S: Adding Paying for Success to Subsidy Instruments	X		X			
SokoText: Leveraging mobile phones for small enterprise empowerment		X				
A Networking Marketplace for SME development		X				
Challenge-driven open innovation platform to promote University-SME interaction		X			X	
Matching Equity Financing			X			
Using business libraries to promote growth in small manufacturers			X			
Targeting High Ability Entrepreneurs Using Social Network Information			X	X		
Identifying High-Impact Entrepreneurs through a Screening Platform				X		
Finding Permanent Impacts for SME growth: The Role of Sequencing				X	X	
Improving Management Remotely Through Benchmarking and Tablets					X	
Service Performance Guarantees to Improve the Business Climate						X
Expanding Legal Services for SME Growth						X

Online Platforms, Market Access and SME Growth

What is the best way to foster growth of SMEs in emerging markets? In recent years, policy innovations targeting supply-side constraints—for example, improving access to capital and providing management training—have yielded mixed results.

Our proposal examines constraints that SMEs face from a different perspective: *lack of demand*. We propose an intervention that increases demand by linking SMEs to larger markets (and, in particular, export markets). This type of intervention can generate growth directly, and can incentivize firms to make investments that raise productivity and increase scale. It also has the potential to raise the returns to supply side interventions (such as extending credit to SMEs) that may be ineffective without access to larger markets.

Our proposal leverages the penetration of IT across the developing world to improve market access for SMEs. We intend to assist firms in matching with buyers through online platforms (e.g., Alibaba). These internet-based marketing channels can be a cost-effective way for SMEs to grow given the high fixed costs of establishing their own distribution networks. Although these services are available in the developing world, many SMEs are not on these platforms as they are either not aware of them or mis-estimate the potential returns. Those that do transact on the platforms may not be using them effectively because of lack of information (e.g., not making use of search engine optimization (SEO) techniques that improve pagerank). We expect that providing these services will foster firm growth, and by exploring differences across the various types of interventions we hope to better understand which constraints are particularly severe.

Team: David Atkin, Amit Khandelwal, Adam Osman

An ExPrize: Using prizes to encourage exports and learn about exporters

Prizes and competitions are back in fashion as ways to encourage innovation and solve difficult problems. Grand Innovation Prizes (GIPs), such as the XPRIZE, provide substantial cash prizes and publicity to the first team to reach a predefined goal, for example private space-flight. Smaller scale competitions, such as those posted at Kaggle.com, are also used by firms to solve difficult problems. Prizes and incentivized competitions of this nature are scarcer in development research though.

There are many reasons for SMEs to export, not least that exporting is associated with improved productivity, learning and higher quality products. However, many SMEs do not participate in the export market and there are relatively few evaluations of specific policies to encourage SME exports. This idea has two aims: the first is to investigate whether competitions with substantial cash-prizes for the most improved exporter can increase exports; the second, is to identify the types of characteristics and strategies associated with those enterprises who become successful exporters as a result of the change in export incentives. A broader aim is to investigate whether prizes can be used by policy makers to promote development objectives.

This idea is likely to be particularly relevant in two contexts – governments looking to encourage exporting among a very specific group of enterprises, for example smaller agricultural producers; or to encourage exporting across a broad group, for example manufacturing in general. However, it is unlikely to work for very small firms which are not large enough to be able to sustain export participation.

Team: Neil Rankin

Fashion Forward – The Fashion Global Value Chain

Textile, apparel, accessories and designed goods and services for home-ware and interior design, are growing industries. Design, authenticity, and ethical considerations (environmentally and socially friendly produced inputs under fair labor conditions) are now drivers in the international apparel, fabric, accessories and home-ware global trade. Yet, many governments in developing countries do not have a policy for the fashion sector which would assist them to tap into this market beyond industrial policy around low-value added apparel firms. The policy gap is often characterized by the lack of curricula for design skills, for supply chain processes (sourcing, quality production, standards, and merchandizing) and for branding of the fashion sector - significant for any global industry.

Developing countries could benefit more from this sector through a three tier value addition process – for designers, SMEs, and workers. Our proposal suggests developing for each tier skills and know-how in terms of trade, design, supply chain management and operations, as well as for MSMEs trade facilitation and branding know-how. This will include international brand recognition of 2-4 selected fashion designers; set up of a sustainable know-how and skills transfer system to micro and SMEs; developing relevant curricula and securing equipment and teachers in fashion and design departments in technical schools and universities; and the establishment of a cluster under a Public Private Partnership approach.

Team: Michaela Weber

P4S: Adding Paying for Success to Subsidy Instruments to Incentivise and Support SMEs

It is generally a good use of scarce public resources to support the development of a robust, competitive, and dynamic small and medium enterprise (SME) sector. Existing subsidy instruments do this by subsidizing inputs (like lowering the costs of credit through cheaper loans) or subsidizing risk (for example, a credit guarantee). These instruments imperfectly align the interests of the public and private sector. We propose an alternative way to distribute subsidies that links payouts to performance. These pay for success (P4S) clauses can be easily added to many kinds of subsidy instruments. They pay out subsidies from the public sector to private firms only if those firms achieve valuable, visible milestones, which might be greater exporting, more job creation, or higher quality production. We set out how this would work, how it should be integrated into existing government systems, and why P4S clauses might be a more efficient and more effective way to deliver socially-beneficial outcomes through the private sector at the same expected cost to the public sector as alternative subsidy programs.

Team: Theodore Talbot, Owen Barder

SokoText: Leveraging mobile phones for economic empowerment of small enterprises and food security at the Base of the Pyramid

Small food retail businesses are the last link in a long and fragmented supply chain, resulting in little market power and highly inefficient practices. SokoText is a technology-based solution that strengthens the position of these businesses through the creation of virtual buyer groups, enabling access to wholesale suppliers and lower prices, and better links these SMEs to existing supply chains. It is designed to empower small-scale food vendors in urban slums and marginalised neighbourhoods in developing countries. By virtually intermediating directly between suppliers and retail businesses, it creates a more efficient supply chain and increases the productivity of food retailers. How? SokoText uses mobile phones to collect and aggregate the demand of small vendors, and purchases it in bulk as early as possible in the supply chain at significantly lower prices, allowing to pass-on a large share of these savings to the retailers while retaining a margin to cover operating costs of the service.

SokoText currently focuses on the fresh produce supply chain, motivated by (a) the inability of retailers to store large quantities of fruits and vegetables even when capital is available, and (b) the secondary effects of lowering input costs for fresh produce – namely, the potential to improve access to fresh and healthy food for everyone at the Base of the Pyramid. While SokoText builds a social enterprise targeting food vendors in Bogotá, Colombia, the model can be applied to a variety of geographical and industry contexts with varying governance structures across public and private organizations.

***Team*:** Carolina Medina Gutiérrez, Verena Liedgens, Rebecca Willett

A Networking Marketplace for SME Development

The limited development and low survival rates of SMEs are serious obstacles to sustainable economic growth throughout the developing world. Although there are many reasons behind these issues, poor business-to-business "networking capital" is believed to play an important role. Networking capital can be understood as the ability for a firm to draw on social and professional networks to gain access to information and business opportunities that can improve its productivity. With limited networking capital, SMEs often struggle to become known to a broader customer base and to earn the trust of new buyers. Leveraging a network of more established and experienced customer firms is critical, but access to business opportunities is a common struggle for SMEs worldwide. This problem limits market competition and reinforces informational asymmetries across different types of entrepreneurs, potentially introducing significant distortions in the overall development of the private sector.

Technology provides an excellent opportunity to enhance the networking capital of SMEs at low marginal cost. With the objective of expanding SMEs networking capabilities, we propose creating an online networking marketplace where buyers and suppliers can openly exchange information and initiate business deals. The aim of this marketplace is twofold: to reduce the cost for buyers to search for SMEs; and to provide a platform for suppliers to market themselves and build a reputation, which can help buyers screen them for quality and reliability.

We expect the expansion of the networking capital of SMEs to translate into an expansion of their customer base and into an improvement in the terms of their contracts. Combined, we expect these benefits to result in an increase in SMEs' survival rates, as well as in improvements in sales performance and innovation. Large firms will also benefit from an expansion and diversification of their pool of suppliers, with potential increases in the efficiency of their supply chains.

Team: Thomas Bossuroy, Francisco Campos, Aidan Coville, Markus Goldstein, Gareth Roberts.

Challenge-driven open innovation platform to promote interactions with SMEs

The idea is to put forth a platform to promote interactions between large firms, SMEs and universities, focused on solving technical challenges these firm run into by firms allowing them to find solution providers more effectively. The platform is a common space designed to reduce information asymmetry and help counterparties (supplying and demanding knowhow) to start interactions that will eventually result in innovative products, services and processes. Countries worldwide are impelled to increase their productive knowledge and it becomes critical to unleash the potential knowhow existing in a territory that is commonly locked up in universities and firms. An open innovation platform will help SMEs and large firms to learn and to create more value, in the form of new products and new businesses while upgrading the innovation system conditions.

Team: Fabio Hideki Ono

Matching Equity Financing – extending risk capital financing in emerging markets to promote entrepreneurship, innovation and job growth

Google, Uber and Facebook are well known global examples of companies that received risk capital financing. Less well known is that risk capital financing can also provide the funding for a company to establish new hospital facilities in India, or that it is currently used to finance a company developing innovative off-grid lighting solutions in Sub-Saharan Africa. Firms such as these have the potential to have a substantial and positive impact on jobs, productivity and the opening up of new sectors. The matching equity finance program aims to support and encourage development of these firms by increasing the supply of risk capital finance. The core of the program is a "risk capital facility" that provides funds that match the investments made by risk capital providers. This increases the resources risk capital providers have to invest and increases their incentive to make these investments. The risk capital facility is designed so that it can be implemented in under-developed risk capital markets by public agencies with limited experience providing risk capital finance. This proposal would complement initiatives that agencies may already be implementing such as providing matching grants and guarantees.

***Team*:** Justin Hill, Andrew Myburgh, Derick Bowen

Using business libraries to promote growth in small manufacturers

Developing economies often have high numbers of low-capital enterprises that manufacture similar products and are located in close proximity to one another. While industrial clusters of very small firms provide some economic benefits, such as reducing input costs, firms operating in these clusters often operate inefficiently, use limited capital, do not consolidate and fail to grow significantly or differentiate. Though various factors constrain the growth of small firms, several prominent impediments to growth are a lack of access to physical and human capital and access to markets.

Our proposal is to create a tool lending library that would address the constraints faced by particularly low-income business owners. This library would encourage access to physical capital by lending tools, provide training to address human capital gaps and create opportunities for producers to organize to collectively market their products. Libraries like the one proposed could enable clustered, small-scale firms to grow, produce more specialized goods, and increase their economic efficiency.

Aside from initial startup costs, we believe these libraries will be economically self-sustaining. Equipment rental and marketing fees will provide the funds for ongoing management of the center. The libraries would operate similar to many existing cooperatives and community organizations in developing economies, a number of which have been highly successful in increasing efficiency and accessing new markets for their members.

***Team*:** Jeremy Shapiro, Jack Hoskins

The Cream of the Crop: Targeting High Ability Entrepreneurs Using Social Network Information

Discerning between high and low potential entrepreneurs is of first order importance, both to lenders and the businesses they support. It is especially challenging in environments characterized by a high degree of asymmetric information and a scarcity of collateral. If a lender can reliably predict which entrepreneurs are most likely to succeed, it can channel a larger percentage of its resources to these individuals, thereby increasing returns for both the lending institution and the community.

The aim of this project is to develop and evaluate a tool to better distinguish between high and low ability entrepreneurs as well as to better identify reliable borrowers. We do so by wielding information that microlenders to the poor already use--the wisdom and knowledge contained in social networks—but in a more direct and systematic manner. The tool is an incentive-based reporting mechanism that uses a scoring rule as a method for screening borrowers: at the time of determining which applicants are eligible for a loan or loan size increase, other community members are asked to rank potential borrowers in terms of their repayment reliability and entrepreneurial ability. We propose to test a series of scoring rules that elicit information from borrowers about characteristics of their peers, and reward them for accurate reports. In evaluating these tools, we will also determine the degree of strategic behavior exhibited by borrowers who know their reports have real lending consequences, and we will determine to what extent this strategic behavior is due to social pressures and obligations that can be ameliorated through careful attention to privacy.

Team: Reshmaan Hussam, Natalia Rigol, Benjamin Roth

Identifying High-Impact Entrepreneurs through a Screening Platform

The priority for most MSME development programs is to target the 'right' entrepreneurs, i.e. to allocate resource-constrained project funds in a way that maximizes the impacts of interventions. However, government led MSME development programs have currently limited ways of identifying these high-impact entrepreneurs, often relying on either subjective measures or simple rules of thumbs not necessarily associated with impacts. These existing methods to select project beneficiaries are not cost-effective and limit the impacts of projects.

In order to give implementers the means to make informed decisions on targeting, we propose to develop a screening platform that will collect information on personality traits, preferences and strategic behavior of potential project participants. We will then model the expected impacts for each individual, in essence getting a ranking of expected impact by entrepreneur. As the model can be calibrated for different types of interventions (e.g. credit, grants and entrepreneurship training) and for different outcomes, such as profit growth and employment creation, this platform offers policy makers an easy-to-use and flexible platform to identify high-impact entrepreneurs and optimize program targeting strategies.

***Team*:** Johanne Buba, Niklas Buehren, Francisco Campos

Finding Permanent Impacts for SME growth: The Role of Sequencing

Human capital and credit constraints are among the most widely cited barriers to developing country SME growth. However, interventions designed to address these problems separately have yielded modest improvements in business outcomes at best. As a result, there is increased recognition that SME growth may depend on relieving both credit and human capital constraints together. The literature has therefore moved to providing both treatments within the same program, but even here the results have been mixed. In this research proposal, we posit that the sequencing of multiple development interventions may be fundamental to the success of these enterprise interventions and propose testing variations on the timing of credit and training interventions. One theory suggests that human capital takes time to get fully absorbed into practice, and providing credit access too early may lead to inefficient investments. However, an alternative theory suggests that human capital interventions may suffer from very low demand and lack of attention among participants without the necessary financial backing already in place to serve as an incentive. Ultimately, testing these theories is an important empirical question. Our study aims to address this question using rigorous empirical methodology in the field. Specifically, we propose to conduct a trial where we vary the sequencing of business training and financial assistance (either through microcredit or grants). The results from this study have the potential to significantly inform World Bank policy advice offered on SME growth by identifying the sequence of interventions that yield the largest and most permanent impacts.

Team: Bilal Zia

Improving Management Remotely Through Benchmarking and Tablet Feedback

The proposed project idea is to implement a pilot of "technology extension" that relies on use of tablets to collect and store information on key indicators, benchmark the company against similar companies, and provide feedbacks remotely through the tablets. The pilot would involve a first phase, the diagnostic, that would involve visit in person of consultants that would serve to train the company managers in the use of the tablets and collecting information. Additionally, some follow up visits may be required but most of the communication and messages would be exchange remotely based on the analysis of the data and benchmarking. The share of "in person" vs "remote" advisory support needs to be fine-tuned and would have to be tested in practice. Also to be tested is the possibility of including, in addition to communication via tablet/computer, also advisory and communication via phone.

***Team*:** Leonardo Iacovone**,** Shawn Cole

Service Performance Guarantees to Improve the Business Climate

Many developing countries have made progress in political openness and economic management but lag in terms of attracting private sector investments, at least outside of narrow resource-based enclaves. These countries may have recognized potential but have not yet established the reputation needed to sustain investment through the inevitable political and policy shocks that take place in most countries. The concerns that deter investors are many but can be broadly classified into high costs that that prevent global competitiveness and high actual or perceived risks.

Political and credit risk guarantees are often used to encourage investors but they cover only a narrow range of risks and are often issued on a deal-by-deal basis. This proposal explores the possibility of expanding the range of guarantee instruments to encompass a wide range of risks and to integrate guarantees more centrally into the reform and investment programs supported by donors. The proposed approach is to offer firms Service Performance Guarantees (SPGs) -- the opportunity to purchase insurance against a wide range of risks and through this to strengthen the accountability of both governments and development partners to their clients – in this case the firms. While it may not be practical to fully cover business losses, firms would receive highly visible payouts if service delivery standards fall short of those expected from the program.

Team: Vijaya Ramachandran and Alan Gelb

Expanding Legal Services for SME Growth

SMEs in developing countries lack access to affordable legal services for writing and enforcing contracts necessary to establish new business relationships and maintain cooperation when unexpected contingencies arise. As a result, informal (or "relational") contracts are common, wherein counterparties use the expected future value of a business relationship to guard against underperformance or breach. Such relational contracts are less complete than formal contracts, and less able to reduce uncertainty over price or performance standards, or to signal SME potential to new business partners or outside lenders. Furthermore, given the high transactions costs associated with formal legal institutions in these settings, parties in dispute have few avenues of external redress, causing disputes to be resolved on terms favoring the party with greater market power. These features limit SMEs' ability to enter into new business relationships, increase operating costs, and curtail growth and productivity.

Providing affordable "transactional" legal services that enable firms to (i) write formal contracts and (ii) access alternative dispute resolution may help relax these constraints and increase SME growth and productivity by improving existing business relationships, establishing new partnerships to expand sales and services, and accessing external capital. We propose trialing of transactional legal services for SMEs that measures the separate and joint impacts of (i) ex ante contracting and (ii) ex post dispute resolution services. Our ideal context is an export-oriented priority growth sector with a high concentration of upstream SMEs; and a setting where legal services are widely available (via private law firms or legal aid clinics). While this model is applicable in a wide range of contexts, including manufacturing and services sectors in both middle- and low-income countries, we illustrate our proposal using examples of the tourist industry in Tanzania and the software industry in India.

Team: Abhay Aneja, Tarek Ghani, Justin Sandefur, Bilal Siddiqi

The Finalists (in the topical order above)

- David Atkin, *UCLA*, Amit Khandelwal, *Columbia Business School*, Adam Osman, *University of Illinois*
- Neil Rankin, *Stellenbosch University, South Africa*
- Michaela Weber, *GTCDR*, *World Bank*
- Theodore Talbot, *Center for Global Development*, Owen Barder, *Center for Global Development*
- Carolina Medina Gutiérrez, *SokoText*, *Colombia*, Verena Liedgens, *SokoText, Colombia*, Rebecca Willett, *SokoText*, *Colombia*
- Thomas Bossuroy, *GSPDR*, *World Bank* Francisco Campos, *GTCDR*, *World Bank* Aidan Coville, *DECIE*, *World Bank* Markus Goldstein, *AFRCE*, *World Bank* Gareth Roberts, *GTCDR*, *World Bank*
- Fabio Hideki Ono, *Sebrae-Paraná*, *Brazil*
- Justin Hill, *GTCDR*, *World Bank*, Andrew Myburgh, *GTCDR*, *World Bank*, Derick Bowen, *DECAR*, *World Bank*
- Jeremy Shapiro, *Princeton*, Jack Hoskins, *Princeton*
- Reshmaan Hussam, *MIT*, Natalia Rigol, *MIT*, Benjamin Roth, *MIT*
- Johanne Buba, *GTCDR*, *World Bank*, Niklas Buehren, *GPVDR*, *World Bank*, Francisco Campos, *GTCDR*, *World Bank*
- Bilal Zia, *DECFP*, *World Bank*
- Leonardo Iacovone, *GTCDR*, *World Bank*, Shawn Cole, *Harvard Business School*
- Vijaya Ramachandran, *Center for Global Development*, Alan Gelb, *Center for Global Development*
- Abhay Aneja,*Stanford and UC Berkeley* Tarek Ghani, *UC Berkeley* Justin Sandefur, *Center for Global Development*, Bilal Siddiqi, *DECIE*, *World Bank*