



Enhancing access to financial services for MSMEs in the green building construction sector in Zambia

“ There is undoubted agreement, as a result of numerous global, regional and country-specific studies, that micro, small and medium sized enterprises (MSMEs) play a major role in economic and social development, especially in developing countries. As important as MSMEs are in contributing to both employment and gross domestic product (GDP), access to finance (A2F) remains a key constraint to their development. A2F allows enterprises to invest in expansions, the latest technology and in improving their competitiveness. ”

– Dr Michael Gondwe, Central Bank Governor, Zambia

In Zambia, the inability to access finance is a significant barrier to the growth and development of MSMEs in the building construction sector and to the home ownership market. The reasons behind this relate to the high lending risks associated with the sector which, paired with market constraints, not only limits the channelling of funds to housing finance, but keeps borrowing costs high (FinMark Trust, June 2013).

The limited access to finance for MSMEs can be ascribed to a mismatch between the needs of MSMEs and the supply of financial services relating to both the demand and supply sides of the financial services market.

Demand-side problems

Demand-side issues relate to the MSMEs themselves. These include lack of understanding of loan application requirements; lack of financial records and bankable business plans; no credible, traceable credit history and collateral; inadequacies in corporate governance; and shortcomings in business management practices and attitudes.

Supply-side problems

On the supply side, financial service providers (FSPs) do not understand the unique financial needs and business models of MSMEs. They subject these businesses to the same assessment criteria as large corporates. Other issues include lingering deficiencies in the legal and regulatory framework and poor financial infrastructure of financial institutions, ranging from branch networks, accounting and auditing standards, to credit reporting systems, collateral and insolvency regimes which are not pro-MSME. There is also the crowding out effect of government – borrowing being a much more attractive option than delving into riskier MSME lending.

Only 20% of African MSMEs had access to credit and only 9% of the investments MSMEs make are funded by a bank.

(African Development Bank, 2012)

55% of MSMEs ranked access to finance as the main obstacle to their operations.

(Zambia Business Survey, FinScope)

Formal MSMEs contribute up to 45% of employment and up to 33% of GDP in developing countries. These numbers are significantly higher when enterprises in the informal sector are included, according to an IFC study conducted in October 2010.

World Bank Enterprise Surveys conducted between 2006 and 2009 revealed that 41% of MSMEs in developing countries report access to finance as a major constraint to their growth and development, compared to 30% in middle income countries and 15% in high income countries. MSMEs in high income countries ranked barriers such as tax rates, regulations and electricity higher than their counterparts in low income countries, who cited corruption, electricity and finance as their biggest hindrances to growth (World Bank).

According to the Zambia Business Survey, 2010, large enterprises account for only 7% of employment in the country's almost 5 million-strong workforce, while the majority of the workforce works in the informal sector and 16% is unemployed.

Bridging the gap

Under the Zambia Green Jobs Programme, the International Trade Centre (ITC), a joint technical co-operation agency between the World Trade Organization, United Nations Conference on Trade and Development and local partners, aims to tackle the lack of access to financial services faced by MSMEs in the green building construction sector in general and green housing in particular. The expected outcome is to enhance the competitiveness of targeted MSMEs, which will lead to increased profit, income and consequently employment levels. The assistance provided will involve empowering both the demand and supply side of MSME financing.



Demand-side response

The intrinsic shortcomings of MSMEs in accessing financial services are tackled through the engagement of business development service (BDS) providers working with targeted MSME associations. The ITC trains these BDS providers in financial management in order for them to become certified financial management counsellors (FMCs). The role of these FMCs is to train, coach, mentor and advise targeted MSMEs in the areas of financial record management, business plan development, corporate governance, adherence to statutory obligations, risk identification and mitigation, interpretation of financial records, cash flow management, contract management, etc. The guidance provided will allow entrepreneurs to develop their own business plans, get financing and successfully grow their businesses.

This approach enhances the chances of accessing finance from FSPs, as the FMCs pre-screen the loan applications and business plans. In addition, the continued mentoring, coaching and advisory services provided to MSMEs assures FSPs of higher success rates and complements their monitoring and performance evaluation duties (something FSPs often find overwhelming when dealing with MSMEs). In a way, the role of an FMC can best be seen as that of a non-financial 'guarantor' to FSPs, leading to enhanced lending through reduced perceived risk.

Supply-side response

The ITC, in collaboration with various experts from local and international institutions, will undertake the following on the supply side:

- a. **Create green finance awareness:** Create awareness of the green economy, green finance and the role of the financial sector in fostering sustainable development. It will also promote the business opportunities in green finance, development of green financial products and services, establishment of green banking processes and procedures as well as assessing loans from a 'green' perspective.
- b. **Provide access to green finance:** FSPs can tap into lines of credit from development financial institutions (DFIs) such as the African Development Bank's Climate Fund or the IFC. They can also benefit from credit guarantee funds from DFIs as they are aimed at increasing the portfolio lent to targeted MSMEs. FSPs can equally benefit from leveraging their funds, directly or indirectly, with government-financed green funds, which are often augmented by DFIs.

Green funds can also be used to assist in the deepening of the financial marketplace through the introduction and encouragement of funds such as green private equity funds, mobilisation of green bonds, green joint venture funds, green mortgages and other such products.

- c. **Provide access to business linkage fuelled finance:** MSMEs can access financial services indirectly by being linked to big companies in the building construction sector. These companies, by nature, have a better chance of obtaining credit. By creating awareness in the financial sector about the potential of green or sustainable housing, institutions such as pension houses and other FSPs can make funding available to big property developers who can in turn subcontract the targeted MSMEs to build their houses.
- d. **Build capacity:** Technical assistance to FSPs can be facilitated to improve access to finance for MSMEs. Training can, for instance, be conducted to enable FSPs to better understand MSMEs and come up with appropriate and innovative products for this sector. Technical assistance can also be provided in terms training FSPs to handle new product lines, such as asset and fund management, project finance assessments, and public-private partnership ventures or any other such special purpose financing arrangement.

The Zambia Green Jobs Programme is a partnership between the Government of Zambia, the United Nations System in Zambia, and public and private stakeholders. The Programme aims to support the creation of green jobs among micro, small and medium enterprises (MSMEs) in the Zambian building construction industry, while at the same time generating systemic change and contributing to the broader discussion on inclusive green growth and job creation in Zambia. The Zambia Green Jobs Programme is supported by the Government of Finland.

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