Small and medium-sized enterprise (SME) development is critical for broad-based and sustained economic growth as Latin America and the Caribbean (LAC) grapple with ongoing global shocks following two years of pandemic-related fiscal challenges. SMEs are a primary source of job creation, comprising 99.5 percent of firms in the region, and accounting for 60 percent of employment. Yet, these same firms represent only 20 percent of gross domestic product (GDP), due to constraints spanning financial to productivity issues.

Helping SMEs both overcome growth constraints and provide higher-quality jobs is important in the context of today’s disparate and fragile economic recovery. SMEs are particularly vulnerable to inflation and labor-market weaknesses from scarcity to informality. With risks of lasting consequences still present, returning to pre-pandemic levels of output is insufficient for the economy in general, and for SMEs.

Many LAC governments provided extraordinary support for SMEs throughout the COVID-19 pandemic. Now is the time to look beyond the pandemic and consider actions to enhance SME access to financing, technical assistance, and digital literacy—three drivers for unlocking the potential of LAC SMEs.

The following pages help to unpack three questions for these three drivers: How can LAC create a financial system more in line with the needs of SMEs to achieve greater development and growth? What capacity-building and technical assistance do SMEs need to increase productivity? What new opportunities does digitalization present for SMEs? A sneak peek: the answers highlight the importance of a multisectoral, holistic approach to empowering SMEs.

This spotlight built upon findings from private, nonpartisan strategy sessions as part of the Adrienne Arsht Latin America Center’s #ProactiveLAC Series, which aims to provide insight and foresight to LAC countries on how to advance economic reactivation and long-term prosperity.

1: HOW CAN LAC CREATE A FINANCIAL SYSTEM MORE IN LINE WITH THE NEEDS OF SMES TO ACHIEVE GREATER DEVELOPMENT AND GROWTH?

LAC public policies for SMEs have been designed with three main objectives: creating jobs, mitigating market shocks, and increasing competitiveness. Since the pandemic, governments have relied heavily on policy tools enabling SMEs’ access to finance. Four such policy tools include:

- **Providing financing and lines of credit**, either through national financial institutions or other agencies that direct resources to the financial system. For example, Argentine banks provide financing and lines of credit to SMEs that are women led; fall under certain sectors like grape har-
vesting for winemaking; intend to export; and desire to buy necessary tools and equipment.4

- Developing financial products appropriate to the size and needs of SMEs. Mexico has developed differentiated strategies to determine credit options for SMEs. Medium-sized enterprises may access financing directed for exporting goods, while small-sized enterprises may access preferential microcredits.5

- Facilitating access to accurate information to evaluate credit risks. Banks in LAC face financial, accounting, and operation limitations that constrain their ability to conduct credit and risk analyses in the SME lending market.6 For example, Brazil’s Central Bank aims to adopt “open banking” practices to enhance information sharing and efficiency in credit and payment markets for a more inclusive and competitive business environment.7

- Implementing government guarantee mechanisms to facilitate access to traditional banking for those without collateral. Chile’s Guarantee Fund for Small Entrepreneurs (FOGAPE) created guarantees for up to 85 percent of loans for SMEs.8

Many countries in LAC have regulatory and institutional framework and financing opportunities potentially conducive to the financial inclusion of SMEs. In response to the pandemic, Argentina introduced four lines of credit under the Reactivation and Financial Inclusion Plan for SMEs to promote productive investment in medium- and long-term projects for the industrial, agro-industrial, and service sectors.9 Similarly, in the last three years, Colombia has codified its commitment to SMEs by introducing regulatory frameworks aimed at accelerating entrepreneurship, financial education and inclusion, and business formalization.10 Hurdles remain, however, for lending institutions to invest in SMEs (conditioned by the high costs and risks of processing) and for SMEs to undertake the financing process (due to the collateral requirement, credit history and formality, high interest rates, and lack of financial and regulatory knowledge).

That is why it is necessary to design public policies that prioritize financial education for SMEs—for example, by including SMEs in the countries’ national financial-education strategies. Development banks and commercial banks (including second-tier banks) can also play a helpful role in bringing financial-education content to SMEs in a more systematized way that also allows results-based measurement and follow-up.

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7 “The Banco Central do Brasil (BCB) and the National Monetary Council (CMN) define the Brazilian Open Banking environment as the sharing of data, products and services between regulated entities—financial institutions, payment institutions and other entities licensed by BCB—at the customers’ discretion, as far as their own data is concerned (individuals or legal entities).” “Open Banking,” Central Bank of Brazil, 2022, https://www.bcb.gov.br/en/financialstability/open-banking; “Comunicó 33,455 of April 24, 2019,” Central Bank of Brazil, April 2019, https://www.bcb.gov.br/content/config/Documents/BCB_Open_Banking_Communique-April-2019.pdf.


2: WHAT CAPACITY-BUILDING AND TECHNICAL ASSISTANCE DO SMES NEED TO INCREASE PRODUCTIVITY?

Low productivity has a decisive influence on SME performance in LAC, limiting contributions to the broader economy. It also aggravates socioeconomic inequality by reinforcing capacity gaps with larger firms in terms of resilience, skills, digital literacy, and negotiation power, among other things.

- **Skills**: In Mexico, for example, small businesses are a primary source of employment for low-skilled workers—and yet, they have few or no resources to train these workers. According to the 2019 Economic Census of the National Statistics Bureau (INEGI), 50.6% of the employees in small businesses have ninth grade as their highest level of education, compared to 35.4% of those in large companies. On the other hand, only 28.8% of SMEs provide training to their employees, which contrasts with 59.1% in the case of large companies. This number is even lower for microenterprises; only 2.4% provide training to their employees.11

- **Resilience**: SME informality is associated with a lower probability of survival when facing crises, as demonstrated by the health emergency caused by COVID-19. Between May 2019 and February 2021, the number of informal companies operating in Mexico decreased by 32.4%, while this reduction was 21.8% for formal establishments.

To keep up with a competitive and evolving job market and better prepare for the "jobs of tomorrow," SMEs need to up-skill their workforces.12 Many countries across the region offer a wide range of free (in-person and virtual) courses aimed at teaching entrepreneurs how to conduct business, develop strategies for innovation, and create mentorship networks. For example, Argentina’s Ministry of Productive Development and Software Industry Chamber (CESSI) offers Argentina Programa, a two-course program focused on teaching computer-programming basics and helping individuals obtain a programmer license from the National Industrial Technology Institute.13

In particular, governments must be intentional in their efforts to support SMEs belonging to women, minority groups, and underserved populations. The Regional Alliance for the Digitalization of Women in Latin America and the Caribbean is one such example.14 Coordinated by Chile’s Ministry of Women and Gender Equity—in partnership with Mexico, Uruguay, Costa Rica, Panama, the United Nations Economic Commission for Latin America and the Caribbean (ECLAC), United Nations (UN) Women, and Microsoft—the initiative promotes collective actions to close gender gaps in access to technology, skills development, and usage of digital technology. Fostering more opportunities for traditionally underserved entrepreneurs is central to enabling economic growth and development.

3: WHAT NEW OPPORTUNITIES DOES DIGITALIZATION PRESENT FOR SMES?

LAC remains a young region, eminently urban, and increasingly interested in technology. This bodes well for the potential of digitalization to address the pervasive challenges of low productivity and high inequality. Most countries have programs aimed at promoting digitalization, ranging from e-government services to register new businesses in Honduras to a multi-year coherent framework to further digitalize production, education, and training in Brazil.15

Digital transformation can be particularly advantageous for SMEs. According to the Organisation for Economic Co-operation and Development (OECD), digitalization allows for greater access to information, communications, and network collaboration, which benefits smaller businesses with greater

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Digitalization also makes it possible to improve SME access to strategic resources including:

- **Financing**: through the development of innovative financial services to meet the demand of traditionally excluded businesses;

- **Skills**: through digital platforms for recruitment and contracting services;

- **Global markets**: through reduced transportation costs and border operations; and

- **Public services**: through online business registration and development services, permit and license systems, and tax payments.

But the extent to which SMEs can exploit the advantages of digital transformation will depend partially on government efforts to support adequate market conditions for SMEs. These conditions include the provision of wide coverage for telecommunications infrastructure, adoption of digital tools through e-government services, and development of institutional frameworks and policies that stimulate competition with incumbents in the same industry and protect against cybersecurity risks. With a growing number of SMEs connected to formal systems and databases due to digitalization, policymakers can leverage this valuable information to design efficient policy instruments and better serve SMEs.

The private sector can be a critical ally for the public sector in accelerating SME digital transformation through capacity building and support programs. To adapt to the...
pandemic’s “new normal,” Mexico’s Ministry of Economy partnered with MX Internet Association in 2020 to launch the #LeAtiendoPorInternet campaign, which aims to integrate more than two million SMEs into the digital economy in its first two years by advancing home delivery services, provide online sales and services, and increase social media presence and digital promotion. Similarly, companies like Microsoft, Visa, and Millicom have committed to accelerate SME digitalization by providing subsidized access and support for software and cloud-based computing, accelerating contactless and mobile payments and e-commerce activities, and offering digital marketing and security packages, respectively. Collectively, these public-private initiatives have the potential to help level the playing field for SMEs operating in the region.

**4: HOW CAN THE PUBLIC, PRIVATE, AND MULTILATERAL SECTORS RAISE AWARENESS ABOUT SME RECOVERY AND ITS IMPORTANCE AS AN ENGINE OF SOCIOECONOMIC PROSPERITY?**

Since the COVID-19 outbreak, governments have implemented many programs aimed at addressing SME needs. Chile’s Digitaliza tu Pyme, a program to promote SME digitalization, captures how policymakers have adapted to pandemic-induced challenges. Other immediate-term responses, like issuing emergency lines of credit, have allowed business owners to access critical funds and support. Looking ahead, governments must carefully balance the tradeoffs between such crucial support and fiscal sustainability. Fiscal and structural reforms should be pursued in an orderly way, to avoid disruptive effects on SMEs. In the long term, policymakers must focus on enabling an SME support ecosystem around resilience through trainings and financing, and by creating a business-friendly environment.

Within the private sector, SME support can take place in more practical ways through business and productive linkages. SMEs are not only customers, but also suppliers to larger companies across the value chain. In Peru, for example, the Asociación PYME Peru (a national SME union association) has spearheaded Provee Pyme, where large companies may advise potential Peruvian SME suppliers on product offerings. Private-sector-led initiatives like Provee Pyme foster collaboration and strategic alliances between small and large businesses, providing a mutually beneficial space.

Beyond policymakers and the private sector, multilateral institutions have an important role to play in supporting SME development through financial and technical assistance and knowledge sharing. The Inter-American Development Bank, the UN ECLAC, the Corporacion Andina de Fomento (CAF)-Development Bank for Latin America, and the World Bank can:

- effectively leverage their unique expertise in developing, collecting, and informing quantitative analyses on the emerging challenges and opportunities facing SMEs, from environmental, social, and corporate governance (ESG) to digitalization;
- advise government and provide a renewed impetus for broader, SME-friendly reforms in related areas such as finance, innovation, taxation, regulation, employment, skills, trade, and environment; and
- make use of their extensive networks, including with stakeholders from the private sector and financial institutions, to improve SME access to financing.

**CONCLUSION**

Together, public, private, and multilateral stakeholders should continue to raise awareness about the importance of SMEs for their economies and society. SMEs provide jobs, incomes, goods, and services to millions of people in LAC. Mom-and-pop shops, restaurants, and workshops dot the landscape across the region. They have an essential role to play as the region addresses its long-standing challenge of increasing productivity while recovering from the socioeconomic effects of the pandemic—and, more recently, inflationary and other macroeconomic shocks. SMEs should be part of the solution, not the problem. Their important contribution to innovation and dynamism will be essential for the region to achieve more competitive economies and increasingly inclusive societies, and to emerge from the pandemic more prosperous.

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With a practical, forward-looking approach to advancing economic development and growth in LAC alongside public- and private-sector stakeholders, we were pleased to launch our Center’s #ProactiveLAC content series in February this year. This Spotlight is the first publication of said series, following six high-caliber #ProactiveLAC discussions and convenings. It focuses on the timely topic of small businesses, a critical yet underdeveloped segment of the regional economy. Through this publication, we hope to provide policymakers with concrete tools to dream and act big on economic recovery and prosperity by, first, starting “small.”

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