

INITIAL POVERTY AND SOCIAL ANALYSIS

Country:	<input type="text" value="Sri Lanka"/>	Project Title:	<input type="text" value="Small and Medium-Sized Enterprises Line of Credit Project"/>
Lending/Financing Modality:	<input type="text" value="Financial Intermediation Loan"/>	Department/ Division:	<input type="text" value="SARD/SAPF"/>

I. POVERTY IMPACT AND SOCIAL DIMENSIONS

A. Links to the National Poverty Reduction Strategy and Country Partnership Strategy

Small and medium-sized enterprises (SMEs) are important drivers of economic growth and poverty reduction through their impact on individual incomes and employment creation. The SME sector is often described as the backbone of the Sri Lankan economy, contributing about 30% of GDP and employing 35% of the total workforce. This proposal aims to develop the financial sector with a particular focus on SMEs via financial institutions to cater to the large and growing demand for SME financing.

The proposed investment is consistent with the goals of the *2013-2015 Country Operations Business Plan (COBP)* to catalyze private investment and promote inclusive growth. The project is also aligned with the government's *Development Policy Framework for 2010–2016 (DPF)* which aims to inter alia accelerate economic growth, improve access to finance and address low private sector investment. The *2012-2016 Country Partnership Strategy (CPS)* is built on the DPF and Strategy 2020 and specifies a focus of ADB assistance on private sector development, including projects that accelerate the pace of private sector participation and promote financial sector development.

The project will address issues of sustained regional disparities in income and gender inequality in employment by encouraging financial institutions to lend to the underserved.

B. Poverty Targeting

General Intervention Individual or Household (TI-H) Geographic (TI-G) Non-Income MDGs (TI-M1, M2, etc.)

This project is expected to fund SMEs in Sri Lanka, with a special focus on (i) new SME borrowers, (ii) borrowers without collateral, (iii) lower income areas outside of Colombo, including South and in the post-conflict areas in the Northern and Eastern provinces, and (iv) women led SMEs. The Project will promote SME lending in these focused areas by including regional and gender factors into eligibility criteria for onlending to SME subprojects, tentatively at least 50% of the funds should be disbursed to new clients, borrowers without collateral, borrowers outside of Colombo, and SMEs mainly owned or managed by women.

C. Poverty and Social Analysis

1. Key issues and potential beneficiaries.

Although Sri Lanka was able to reduce the share of the population below the official poverty line (\$1.48/day) to 6.7%, regional development disparities have subsisted. While Western Province that includes Colombo, with highest per capita income, records the lowest poverty incidence of less than 3% in 2013, North District records 12.8% and East District records 14.8%.

The primary beneficiaries of the project are SMEs, especially new borrowers, borrowers without collateral, borrowers outside of Colombo, and SMEs led by women. They will gain more access to finance to fund working capital and expand their business. Furthermore, PFIs will expand their customer base and gain experience in lending to unconventional SME clients.

2. Impact channels and expected systemic changes.

The project will (i) increase access to finance for SMEs in Sri Lanka; (ii) contribute to diversifying the economy through an increased SME share in GDP and (iii) result in employment creation especially for new SME borrowers, SMEs without collateral, SMEs outside of the Colombo, and SMEs mainly owned or managed by women.

3. Focus of (and resources allocated in) due diligence.

- Designing an auction mechanism that will incentivize banks to provide affordable credit to targeted SMEs but that will at the same time create a profit opportunity for them to undertake this new lending.
- Assessing the enabling environment for SME lending, including capacity of credit bureaus, collateral registries, and SME borrower support services.
- Identifying eligibility criteria for participating financial institutions and SME subprojects.

- Designing an attached technical assistance to support 1-2 emerging clusters.

4. Specific analysis for policy-based lending. N/A

II. GENDER AND DEVELOPMENT

1. What are the key gender issues in the sector/subsector that are likely to be relevant to this project or program?

Employment is a significant area in which women face inequality and gender discrimination. Women's unemployment rate has been double that of men for more than 3 decades. The quality of employment for women has deteriorated, as the demand is chiefly in casual and low-paying and low-skill jobs in the formal and informal sectors. In 2014Q4, labor force participation rates were 74.3% for men and 34.5% for women, while unemployment rates were 2.9% for men and 7.2% for women. Most enterprises that are owned or managed by women are micro- and small-sized and face limited access to finance because they cannot offer collateral and have limited access to technology and business development capabilities.

2. Does the proposed project or program have the potential to make a contribution to the promotion of gender equity and/or empowerment of women by providing women's access to and use of opportunities, services, resources, assets, and participation in decision making?

Yes No

Some gender benefits are expected as loans contribute to SMEs owned or managed by women. Please refer to the above **B. Poverty Targeting**.

3. Could the proposed project have an adverse impact on women and/or girls or widen gender inequality?

Yes No

4. Indicate the intended gender mainstreaming category:

GEN (gender equity) EGM (effective gender mainstreaming)

SGE (some gender elements) NGE (no gender elements)

III. PARTICIPATION AND EMPOWERMENT

1. Who are the main stakeholders of the project, including beneficiaries and negatively affected people? Identify how they will participate in the project design.

Main beneficiaries are new SME borrowers, SMEs without collateral, SMEs outside of Colombo, and SMEs mainly owned or managed by women. There are no negatively affected people. ADB will consult with stakeholders during fact finding to facilitate project feasibility.

2. How can the project contribute (in a systemic way) to engaging and empowering stakeholders and beneficiaries, particularly, the poor, vulnerable and excluded groups? What issues in the project design require participation of the poor and excluded?

The project design does not require direct participation of the poor and excluded. However, the project design will have to consider what limitations financial institutions face in lending to un- or under-banked SME.

3. What are the key, active, and relevant civil society organizations in the project area? What is the level of civil society organization participation in the project design?

Information generation and sharing (L) Consultation (L) Collaboration (N) Partnership (N)

4. Are there issues during project design for which participation of the poor and excluded is important? What are they and how shall they be addressed? Yes No

IV. SOCIAL SAFEGUARDS

A. Involuntary Resettlement Category A B C FI

1. Does the project have the potential to involve involuntary land acquisition resulting in physical and economic displacement? Yes No

The project will increase access to finance for SMEs. No involuntary resettlement involved.

2. What action plan is required to address involuntary resettlement as part of the PPTA or due diligence process?

N/A

Resettlement plan

Resettlement framework

Social impact matrix

Environmental and social management system arrangement

None

B. Indigenous Peoples Category A B C FI

1. Does the proposed project have the potential to directly or indirectly affect the dignity, human rights, livelihood systems, or culture of indigenous peoples? Yes No

2. Does it affect the territories or natural and cultural resources indigenous peoples own, use, occupy, or claim, as their ancestral domain? Yes No

3. Will the project require broad community support of affected indigenous communities? Yes No
There will not be any affected indigenous communities.

4. What action plan is required to address risks to indigenous peoples as part of the PPTA or due diligence process?
 Indigenous peoples plan Indigenous peoples planning framework Social Impact matrix
 Environmental and social management system arrangement None

V. OTHER SOCIAL ISSUES AND RISKS

1. What other social issues and risks should be considered in the project design?

- Creating decent jobs and employment (L) Adhering to core labor standards (L) Labor retrenchment
 Spread of communicable diseases, including HIV/AIDS Increase in human trafficking Affordability
 Increase in unplanned migration Increase in vulnerability to natural disasters Creating political instability
 Creating internal social conflicts Others, please specify _____

The incentives for the line of credit must be carefully calibrated so that the banks extend credit for the targeted SMEs and not for SMEs that already have secure access to finance.

2. How are these additional social issues and risks going to be addressed in the project design?

The line of credit will include an auction mechanism to allow banks to recover the higher operational and credit costs of extending credit to the targeted SMEs.

VI. PPTA OR DUE DILIGENCE RESOURCE REQUIREMENT

1. Do the terms of reference for the PPTA (or other due diligence) contain key information needed to be gathered during PPTA or due diligence process to better analyze (i) poverty and social impact; (ii) gender impact, (iii) participation dimensions; (iv) social safeguards; and (v) other social risks. Are the relevant specialists identified?
 Yes No

Due diligence will be undertaken by staff since the project entails limited poverty and social issues.

2. What resources (e.g., consultants, survey budget, and workshop) are allocated for conducting poverty, social and/or gender analysis, and participation plan during the PPTA or due diligence?

- Yes No

Due diligence will be undertaken by staff since the project entails limited poverty and social issues.