

**ASIAN DEVELOPMENT BANK**

**TAR:STU 35329**

**TECHNICAL ASSISTANCE**  
(Financed by the Japan Special Fund)

**FOR**

**STRENGTHENING REGIONAL NETWORKING FOR  
SMALL AND MEDIUM-SIZED ENTERPRISES  
IN BRUNEI-INDONESIA-MALAYSIA-PHILIPPINES  
EAST ASEAN GROWTH AREA**

**December 2003**

## **ABBREVIATIONS**

ADB	–	Asian Development Bank
ASEAN	–	Association of Southeast Asian Nations
BDS	–	business development service
BIMP-EAGA	–	Brunei-Indonesia-Malaysia-Philippines East ASEAN Growth Area
CIDA	–	Canadian International Development Agency
IFC	–	International Finance Corporation
PENSA	–	Program for Eastern Indonesia SME Assistance
SME	–	small and medium-sized enterprise
TA	–	technical assistance
TEP	–	trade and export program

## **NOTE**

In this report, "\$" refers to US dollars.

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## I. INTRODUCTION

1. Subregional economic cooperation schemes or growth areas have emerged as an increasingly important strategy to accelerate economic growth and social development, by exploiting economic complementarities between participating regions. The 2003 Strategy for Small and Medium-Sized Enterprise (SME) Development in the Brunei-Indonesia-Malaysia-Philippines East ASEAN Growth Area (BIMP-EAGA) confirmed the role of a stronger private sector to promote SME development with the objective of stimulating long-term economic growth, creating jobs, and sustaining poverty reduction. All participating governments have adopted the strategy as their own, and asked the Asian Development Bank (ADB) to help operationalize it. The business development services (BDSs) is a key component in this strategy, and donors such as the International Finance Corporation (IFC) have followed international best practices in the provision of BDSs through its SME facilities, including its current facility in Indonesia. The present technical assistance (TA), included in ADB's 2002 subregional program for BIMP-EAGA, responds to the request of governments in the BIMP-EAGA to operationalize the BDS component of the strategy, by extending best practices in BDS provision to parts of the BIMP-EAGA not served by IFC.<sup>1</sup>

## II. ISSUES

2. BIMP-EAGA was formally launched in 1994 to develop the subregion by re-establishing and strengthening historical cultural and trade links between the member countries. BIMP-EAGA, with the exception of Brunei, share common characteristics such as considerable distance from their capitals, and resource-based regional economies that are less developed than the capital regions. BIMP-EAGA was a key strategy of the four participating governments to correct regional economic imbalance by (i) facilitating freer movement of people, goods, and services; (ii) developing vital infrastructure; and (iii) coordinating the management of ecosystems and common resources to ensure sustainable development.

3. The strategic objective of BIMP-EAGA is to ensure that growth is driven by private sector initiatives built on economic complementarities and the use of shared natural resources, technology, and information. Empowering the private sector is thus essential to realize BIMP-EAGA's economic and social development goals. As early as 1996 an ADB-funded study<sup>2</sup> identified a wide range of opportunities among member countries, and concluded that, with increased regional economic cooperation, the subregion would become a major investment destination in ASEAN for agro-industry, natural resource-based manufacturing, and tourism. The study also recognized the role of SMEs in attaining social stability and balanced growth for BIMP-EAGA, and, hence, identified SME promotion as a crucial component of the strategy.

4. Since 1999, ADB has funded assessments of the SME environment within BIMP-EAGA that produced a subregional strategy for SME development. The assessments were initially limited to the most needy subregions of Indonesia (Kalimantan and Sulawesi) and the Philippines (Mindanao and Palawan),<sup>3</sup> and later expanded to include Brunei and the Malaysian states of Sarawak and Sabah.<sup>4</sup> Most of territories of eastern Indonesia and all those in southern

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<sup>1</sup> The TA first appeared in the *ADB Business Opportunities* in July 2001.

<sup>2</sup> ADB. 1995. *Technical Assistance for the Study of the Brunei Darussalam-Indonesia-Malaysia-Philippines East ASEAN Growth Area (BIMP-EAGA)*. Manila (RETA No. 5625 for \$1,800,000).

<sup>3</sup> ADB. 1999. *Technical Assistance for the Small and Medium Scale Enterprise in the EAGA Region*. Manila (RETA 5880 for \$300,000).

<sup>4</sup> ADB. 2001. *Technical Assistance for Expanding the Strategy for SME Development in the EAGA*. Manila (RETA 6018 for \$240,000).

Philippines lag behind the rest of the country in social and economic development. One of the major constraints faced by SMEs in these territories includes the lack of an efficient and sustainable network of BDS providers to help SMEs meet challenges in generating viable trade and investment opportunities.

5. Effective networking with improved BDSs aims at removing SMEs' inherent constraint of small-scale production for better trade and investment opportunities. By definition, SMEs are constrained by their small operations, which preclude individual enterprises from benefiting from economies of scale, that is, from effectively establishing or expanding export linkages and tying into the supply chains of large firms. SME development elsewhere shows that information sharing is more effective within specific industries because of commonality of interests, concerns, and capabilities. Although chambers of commerce and other similar organizations provide opportunities for networking, the multiplicity of interests slows down the process of putting cooperative activities in place. Few alliances exist among industry associations in the subregions, resulting in the lack of opportunities for networking and defining requirements to vertically and horizontally integrate industries in-country and within BIMP-EAGA. In the absence of a focused group with common or related commercial interests, it is difficult to recognize and take advantage of expanded trade and investment opportunities.

6. An initial mapping of existing SME-related BDSs in BIMP-EAGA prepared as part of the SME strategy shows that BDS initiatives are ongoing or planned in each area as provided by government agencies, multilateral and bilateral funding agencies, nongovernment organizations (NGOs), and the private sector. The mapping exercise showed, however, that in-country BDSs are more inward than outward looking and primarily aimed at increasing local, rather than regional or international, SME competitiveness. Considering trade and investments move beyond national boundaries in BIMP-EAGA, new opportunities for BDS providers must be opened to test the efficacy of the strategies used under greatly liberalized and highly competitive export market conditions. Worldwide, international agencies such as IFC and its partners have demonstrated the demand and effectiveness of high-quality BDSs. Through a series of specialized SME facilities, IFC, bilateral and multilateral donors provide local SMEs with avenues to meet the existing demand for services needed to build commercially viable businesses, and take other broader initiatives to develop sustainable and dynamic SME sectors. These facilities play a useful role, both in helping SMEs directly and in creating local capacity to give them technical and financial support. They also help SMEs attract necessary financing for their ventures, prioritizing projects with potential to develop self-sustaining enterprises, generate employment, increase skills, and stimulate export earnings. The staff and consultants in the project development offices also provide other essential services such as training and research, and work with donors to frame and promote policy reforms aimed to improve the local business climate. In Asia, examples of these IFC-managed facilities include the Mekong Project Development Facility, South Pacific Project Facility, and South Asia Development Facility, all funded by ADB.

7. BIMP-EAGA's common geography and waters (Celebes and Sulu seas) supply most of the world's exports of coconut, seaweed and live fish, and, hence, offers a sizeable and scaleable demand for BDSs among subregional SMEs whose activities are based on these indigenous and abundant resources in the subregion. BIMP-EAGA, mainly Indonesia and the Philippines, accounts for almost 80% of the world's coconut trade.<sup>5</sup> Coconut is largely produced in small landholdings and is consumed fresh, with the remainder of the crop dried to copra, and

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<sup>5</sup> The Philippines and Indonesia dominate coconut production. In 2002, according to the Food and Agriculture Organization (FAO), both countries produced more than half of the world's production of coconut (49.6 million metric tons).

pressed into coconut oil. The emergence of massive industrial production of palm oil has diminished the traditional importance of coconut oil for cooking, and, hence, rendered smallholder coconut production less commercially viable.<sup>6</sup> New product development for coconut aims at improving commercial prospects of the crop. Technology for charcoal based on coconut waste, oil for cosmetics, yogurt, and furniture are among some of the new commercial uses of coconut, for which research and development has already been undertaken, but not fully commercialized. Producers in BIMP-EAGA would benefit from BDSs to develop new trade and investment opportunities for the crop.

8. Seaweed is also a main BIMP-EAGA resource that is available to island communities and would potentially benefit from BDSs to improve commercial product development, protect the environment, and support sustainable income generation in small island communities. The Philippines is the largest world's supplier of seaweed, which has multiple uses such as stabilizers in food, cosmetics, and pharmaceuticals. In Indonesia, much of the seaweed produced is exported raw for further processing overseas, in some cases to the Philippines. Hence, there is potential for a cross-country exchange of technology, trade and investment opportunities between SMEs in southern Philippines and northern Sulawesi.

9. BIMP-EAGA countries, mainly Indonesia and the Philippines, also account for 85% of the world's aquarium fish supply—a growing but very specialized market—and thus intervention in these countries has an immediate global effect. The trade provides sustainable job creation for rural fishing communities, with increased retention of income at the community level and market-induced conservation of coral reefs.<sup>7</sup> To develop this niche trade, BDSs will be useful for SMEs to make live-fish trade sustainable through improved certification, potential financing, and reef conservation.

### III. THE TECHNICAL ASSISTANCE

#### A. Purpose and Output

10. The TA aims at promoting business networking among SMEs in the least developed areas of BIMP-EAGA where cooperation, especially between Indonesia and Philippines, will facilitate knowledge transfer or where trade and investment opportunities exist to establish direct trading relations while keeping in mind the economic, social, and environmental impact on BIMP-EAGA communities. The subregional approach of the TA with emphasis on private sector complements ADB assistance being prepared and considered under the Indonesia and the Philippines country programs.<sup>8</sup> The TA framework is in Appendix 1.

<sup>6</sup> ADB supports the Government of Indonesia to improve productivity of coconut smallholders in Indonesia. See ADB. 2003. *Technical Assistance for Productivity Enhancement for Tree Crops*. Manila (TA 4224 for \$1.4 million).

<sup>7</sup> In Indonesia and the Philippines, cyanide and dynamite fishing is rapidly destroying coral reefs. Of all 556 locations with coral in Indonesia, only one third is covered mostly with living coral. See ADB. 2003. *Country Environmental Analysis Report*, Table 2.4. Manila. Also, ADB has supported the Government's coral reef conservation in Indonesia, including a new participatory process under its latest loan. See ADB. 2002. *Coral Reef Rehabilitation and Management Project Phase II*. Manila. (Loan 1962 for \$41 million).

<sup>8</sup> ADB. 2002. *Report and Recommendation of the President to the Board of Directors on a Proposed Loan to the Republic of Indonesia for the SME Export Development Project*. Manila (Loan 1978 for \$85 million), and ADB. 2002. *Technical Assistance to the Republic of Indonesia for SME Export Development Project*. Manila (TA 4041 for \$0.5 million). ADB will sign a memorandum of understanding with the International Finance Corporation (IFC) to support small exporters, including those in eastern Indonesia, with combined BDS and investment credit. Also, future ADB lending and nonlending operations for SMEs are envisaged to benefit SMEs in southern Philippines.

## B. Methodology and Key Activities

11. The aim of the TA is to promote BDSs through networking within BIMP-EAGA, drawing from the vast experience of IFC in Asia,<sup>9</sup> to (i) facilitate knowledge transfer on product development among SMEs (through product and market studies, individual and group SME business plans, business strategy workshops); and (ii) identify common industry constraints in the subregion (through dissemination workshops and policy advocacy). TA activities will be designed to have economic, social, and environmental impact on coastal communities. The TA will target industries where new environmentally sustainable technologies and value-added processes can be developed to (i) increase the economic participation of SMEs through margin expansion and sales growth, (ii) underpin social development and poverty reduction through sustainable job creation, and (iii) develop financial incentives for environmental sustainability.

12. The TA represents ADB's efforts to adopt international best practices in BDSs for SMEs in BIMP-EAGA through one of the newest IFC facilities in Asia—the Indonesia Enterprise Development Facility, renamed Program for Eastern Indonesia SME Assistance or PENSA. Under the facility, there are four program areas with proven potential to create a significant number of jobs and spur local economic growth, and will be supported by a business-enabling environment program based in Jakarta. Development of agribusiness in south Sulawesi is one of such programs. For a full description of the PENSA's setup, program and budget for 2003-2008, see Appendix 2.

13. Under the TA, the agribusiness program will be expanded to include BIMP-EAGA centers such as Manado (north Sulawesi), and Davao (southern Philippines) and BIMP-EAGA specific agro-industries (coconut and marine products). The expanded program represents part of a logical building block in subregional SME development, and builds on the existing TA experience of ADB,<sup>10</sup> Swisscontact and the Canadian International Development Agency (CIDA),<sup>11</sup> in both Indonesia and the Philippines, two of the member countries in BIMP-EAGA. The TA will help establish a regional network for SMEs to develop indigenous natural resources such as coconut and marine products. These agribusinesses have been chosen because they are based on similar geography and topography and have scaleable opportunities for trade and investment in new technologies. The TA activities will focus on promoting these indigenous agribusinesses to stimulate exports under a dual approach. One will focus on SMEs themselves, and support BDS provision to promote product development and marketing to commercialize existing or new technologies. The other will focus on local governments and support fast-track plans to promote product delivery, investment, and environmental protection. Under the expanded program, PENSA will provide short-term BDS assignments, including advice on the enabling environment. For a full description of the program and terms of reference for consultants, see Appendix 3.

## C. Cost and Financing

14. The total estimated cost of the TA is \$700,000, to be financed on a grant basis by the Japan Special Fund (JSF), funded by the Government of Japan, for a total of 60 person-months

<sup>9</sup> BDSs are the focus of these facilities. The IFC SME Department recently established a knowledge management team working specifically on BDSs. A recent survey by this team identified that the facilities have over 100 different BDS-related activities under implementation around the world.

<sup>10</sup> ADB works with local governments in Pare-Pare and Bulukumba in southern Sulawesi to improve BDS and regulations affecting small businesses. See ADB. 2002. *Technical Assistance for Strengthening BDS for SMEs*. Manila (TA 3829 for \$1.5 million).

<sup>11</sup> CIDA works in southern and northern Sulawesi through the Private Enterprise Project (PEP), and several initiatives in Mindanao, southern Philippines.

of international (20 person-months) and domestic (40 person-months) full-time and part-time consultancies. Cost estimates are in Appendix 4. IFC's parallel cofinancing of the entire facility amounts to \$5 million for 2003–2008 while other multilateral and bilateral funding agencies<sup>12</sup> parallel cofinancing amounts to the balance (\$17 million). To ensure sustainability of the project, the TA will institute cost recovery measures for the BDS component.<sup>13</sup>

#### **D. Implementation Arrangements**

15. ADB's Southeast Asian Department, in coordination with the Private Sector Department, will be the Executing Agency for the TA. The consultants will be IFC, through PENSA, hired as a direct award. The operating procedures for the direct award under the TA are also in Appendix 4. The current arrangement is based on previous cooperation between ADB and IFC with RETAs to finance other similar SME facilities in the South Pacific, Mekong, and, more recently, South Asia.<sup>14</sup>

16. The program will mainly focus on developing linkages between Indonesian and Philippine SMEs in BIMP-EAGA, which includes north and south Sulawesi in Indonesia, Mindanao and Palawan in southern Philippines, and Sabah and Sarawak in east Malaysia. Initially, the program will be developed, managed, and supported by PENSA offices in the Denpasar headquarters and Makassar office (south Sulawesi). Two Manado and Davao office representatives will be selected and they will draw on the work of PENSA, particularly in marketing, access to capital, and business association development. The program will establish links between Indonesia and the Philippines, whether through direct trade or through knowledge and skills sharing. Initially, the program will be structured as a series of pilot programs, mainly in north Sulawesi (Indonesia) and Mindanao (Philippines). During the pilot phase, these projects will be overseen from the Makassar office in south Sulawesi. Based on the initial results, the projects might be scaled up.

17. In close coordination with ADB, IFC will manage the program and coordinate the TA activities for up to 36 months, through international and domestic consultants, starting in February 2004. The individual experts financed by the TA will support implementation by providing individual SMEs and local associations of SMEs with specific advice and skills in such technical fields as the trade in seaweed, live fish, and coconut.

### **IV. THE PRESIDENT'S DECISION**

18. The President, acting under the authority delegated by the Board, has approved the provision of technical assistance not exceeding the equivalent of \$700,000 on a grant basis for Strengthening Regional Networking for Small and Medium-Sized Enterprises in Brunei-Indonesia-Malaysia-Philippines East ASEAN Growth Area, and hereby reports this action to the Board.

<sup>12</sup> Australia, Canada, Japan, the Netherlands, and Switzerland. See Appendix 2, Table 2A.2.

<sup>13</sup> Any funds recovered will be utilized by PENSA for further research and product development in the BIMP-EAGA.

<sup>14</sup> ADB. 2000. *Technical Assistance for the South Pacific Project Facility II: Private Sector Development Support*. Manila (RETA 5891 for \$300,000); ADB. 2000. *Technical Assistance for SME Growth and Development in the Mekong Region*. Manila (RETA 5951 for \$750,000); ADB. 2002. *Technical Assistance for SME Growth and Development in the South Asia Region*. Manila (RETA 6087 for \$750,000).

### TECHNICAL ASSISTANCE FRAMEWORK

Design Summary	Targets/Measurable Indicators	Project Monitoring	Risks/Assumptions
<p><b>Goal</b></p> <ul style="list-style-type: none"> <li>• Stimulate productive private sector investment and business development in the Brunei-Indonesia-Malaysia-Philippines East ASEAN Growth Area (BIMP-EAGA) developing member countries (DMCs)</li> <li>• Improve the competitiveness of subregional small and medium-sized enterprises (SMEs)</li> <li>• Facilitate cross-border knowledge sharing and technology transfer between SMEs in BIMP-EAGA</li> <li>• Improve the regulatory framework to create an enabling environment for SME development</li> </ul>	<ul style="list-style-type: none"> <li>• Increased SME private sector investments in absolute amounts and as a share of gross domestic product (GDP)</li> <li>• Increased foreign direct investments</li> <li>• Increased business formation and provision of business development services (BDSs)</li> <li>• Increased intraregional trade in goods and services</li> </ul>	<ul style="list-style-type: none"> <li>• Statistical data on private sector investment and business activities, including data on private sector investments, business formation, job creation, training, foreign investment, and demonstrated development impact and regulatory measures in place to improve the enabling environment for SME development</li> </ul>	<ul style="list-style-type: none"> <li>• Continuing reform in BIMP-EAGA DMCs to create a conducive environment for private sector development, an effective banking system and open investment regimes</li> <li>• Conducive macro environment</li> </ul>
<p><b>Objective and Purpose</b></p> <ul style="list-style-type: none"> <li>• Enhance provision of business and technical assistance to SME markets through capacity building and new product development</li> </ul>	<ul style="list-style-type: none"> <li>• Improved availability and diversity of business and technical advice to SMEs to achieve positive development impact in BIMP-EAGA</li> </ul>	<ul style="list-style-type: none"> <li>• Feedback from SME clients, local financial institutions, investors, nongovernment organizations, business associations, service providers, government agencies, and aid organizations in BIMP-EAGA</li> </ul>	<ul style="list-style-type: none"> <li>• Favorable private sector investment environment and effective and efficient banking systems</li> </ul>

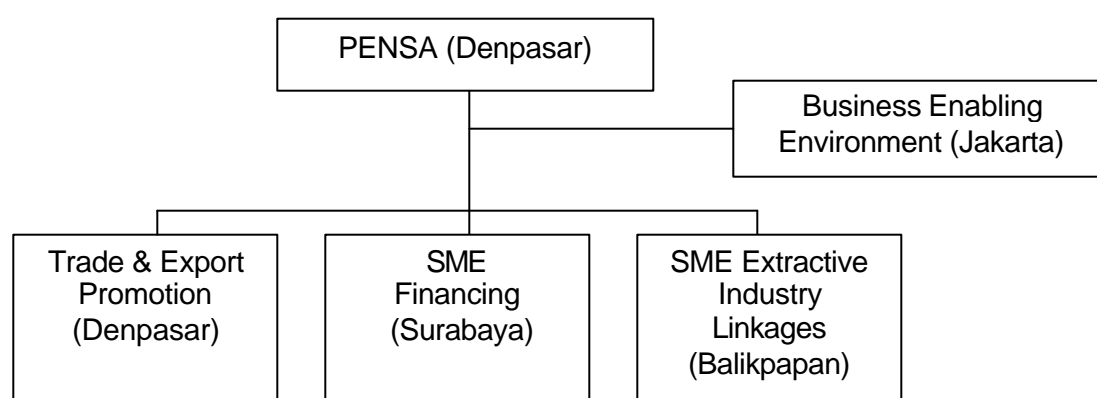


Design Summary	Targets/Measurable Indicators	Project Monitoring	Risks/Assumptions
<p><b>Outputs</b></p> <ul style="list-style-type: none"> <li>• Feasibility and market studies conducted</li> <li>• Training for business development service providers prepared and new business services extended</li> <li>• Managerial and training requirements identified and addressed (marketing skills, accounting system, management information system, planning, etc.)</li> </ul> <p>Targeted new product development facilitated</p>	<ul style="list-style-type: none"> <li>• Measurable forecasts of the following captured indicators: number of projects screened; number of feasibility studies conducted; number of training courses conducted for local SME staff; number of BDS providers trained, revenue earned by BDS providers, amount of new investment generated in chosen sectors within the subregion, incremental employment, increase in women employed</li> </ul>	<ul style="list-style-type: none"> <li>• Annual and semiannual monitoring and evaluation reports, consultant project completion reports, and multilateral and bilateral funding agency review meetings (annual and semiannual)</li> </ul>	<ul style="list-style-type: none"> <li>• Active local business community</li> <li>• Increase in investment opportunities, including foreign investment interest</li> </ul>
<p><b>Activities</b></p> <ul style="list-style-type: none"> <li>• Program for Eastern Indonesia SME Assistance (PENSA) programs and consulting services (60 person-months) provided</li> <li>• Coordination and cooperation with the Asian Development Bank (ADB) and other aid agencies in the reform program process</li> </ul>	<ul style="list-style-type: none"> <li>• Quality of PENSA programs and consulting services provided and quantity of services sought</li> <li>• PENSA programs and projects addressing needed policy reforms as identified by ADB, World Bank, Canadian International Development Agency (CIDA), and other aid agencies</li> </ul>	<ul style="list-style-type: none"> <li>• Consultant reports and PENSA reports</li> <li>• Multilateral and bilateral funding agencies' advisory board meetings, program report sharing, ADB resident missions' meeting with PENSA staff on programs and enabling environment reform efforts</li> </ul>	<ul style="list-style-type: none"> <li>• Interest on the part of SMEs in PENSA services</li> <li>• Weak aid agency, multilateral cooperation and coordination</li> </ul>

## PROGRAM FOR EASTERN INDONESIA SMALL AND MEDIUM-SIZED ENTERPRISE ASSISTANCE (PENSA)

1. PENSA will initially work in four program areas: (i) trade and export promotion, (ii) SME financing, (iii) extractive industry linkages to small and medium-sized enterprises (SMEs), and (iv) agribusiness linkages to SMEs. The latter is the focus of this technical assistance (TA), and its geographical coverage will be extended to include activities in northern Sulawesi, southern Philippines, and, if possible, eastern Malaysia. PENSA has selected these four program areas for their potential to create a significant number of jobs and spur local economic growth, and will be supported by a business-enabling environment program based in Jakarta.

**Figure A2.1: PENSA's Overall Program Structure**



SME = small and medium -sized enterprise; PENSA = Program for Eastern Indonesia SME Assistance.

### **A. Trade and Export Promotion (Denpasar)**

2. PENSA's Trade and Export Program (TEP) will be based in Denpasar and initially work with furniture and handicraft producers. The furniture and handicraft sector was selected as skilled local craftsmanship and local designers can contribute significant local value added. Production in this sector is also centered around local villages, so the benefits of identifying new sustainable export market opportunities will flow almost directly to large numbers of local villagers, improving the prospects of many local communities.

3. The initiative will first develop and deliver a program of training to local wood and furniture producers in Bali and east Java. A major production problem in this region is that wood is frequently not properly treated or dried, causing it to crack once it leaves the humidity of Indonesia, which discourages repeat export orders.

4. The training program will set in place sustainable structures and systems of training delivery covering quality improvement, as well as basic business skills in marketing, design, and basic finance. The training will be developed by PENSA staff, and delivered by local providers such as local tertiary institutions or local business service providers on a cost-recovery basis.

5. The training program will also include an international marketing component. Market building is important as numbers of international buyers coming to Indonesia have dropped dramatically following the Bali bombing and, more recently, the severe acute respiratory

syndrome (SARS) epidemic. Local producers stand to benefit greatly from being able to market their products overseas without waiting for the buyers to come to them. TEP's marketing component will commission trade data research to identify which international markets potentially offer the best price point or the greatest demand for selected products. This initial analysis will then be followed up with a more detailed market survey of those higher-priced or greater-demand markets to see what sort of products are most likely to be successful. The survey results will be made available on a fee-for-service basis to Indonesian producers and exporters. The program will look to hand over the market research processes it develops to local partners for ongoing delivery.

6. In cooperation with the Kearny Alliance Foundation, TEP will provide practical hands-on assistance to selected local producers who apply what they have learned from the program's training and marketing components to day-to-day attempts to meet export orders. For a fee, a stand-alone center will provide this deal-facilitation service. One such center will be established as a pilot. The Kearny Alliance Foundation has a long history of working with SMEs in Indonesia and can provide TEP with valuable insight into the practical problems that befall SMEs securing export orders.

## **B. Small and Medium-Sized Enterprise Finance (Surabaya)**

7. The PENSA SME financing program will be based in Surabaya and focus on helping local SMEs gain access to new and more suitable sources of financing.<sup>1</sup> This work will involve delivering training and seminars to build understanding between banks and SMEs. For local banks this training will cover how to better design and market their products and services to meet the needs of SMEs, as well as education in the practical constraints that face small business. For SMEs this training will cover the financing process and its obligations.

8. Another major problem that many SMEs cite is the banks' requirement that loans be secured by collateral worth 100–150% of the value of the debt, with most of this collateral in real estate. Historically, banks had sound reasons to limit their lending focus. Nonetheless, local banks could safely expand their criteria, supporting the growth of SMEs while maintaining strong credit quality and risk-management procedures. However, several changes may be needed: (i) banks need to understand the potential applicability of other financing products, (ii) customers need to provide banks with more uniform and higher-quality financial statements, and (iii) bankers must become more sale and solution oriented.

9. As a result PENSA will implement the following initiatives: (i) create a targeted sales and marketing training program for banks; (ii) develop a training program for banks to help them establish SME industry analysis; (iii) prepare and sponsor an SME banking best-practices forum; (iv) support the creation of industry standards for financial information provided by SMEs; (v) build a turnkey financial product with select bank partners; and (vi) directly train SMEs to better prepare them to access sources of finance. Indonesian banks have already established a foundation to serve the SME market. Even so, PENSA has significant scope to work with local banks and broaden their SME-financing activities without eroding the bank portfolios' credit quality.

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<sup>1</sup> Under ADB. 2002. *Report and Recommendation of the President to the Board of Directors on a Proposed Loan to the Republic of Indonesia for the Small and Medium Enterprise Export Development Project*. Manila; and ADB. 2002. *Technical Assistance to the Republic of Indonesia for Small and Medium Enterprise Export Development Project*. Manila. ADB will sign a memorandum of understanding with the International Finance Corporation (IFC) to support small exporters with investment credit, especially in Bali and east Java.

### **C. Extractive Industry Linkages (Balikpapan)**

10. The extractive industry sector in eastern Indonesia generates hundreds of millions of dollars of revenue, of which only a small share is captured by local communities and SMEs. Balikpapan is a center for many of the oil, gas, and mining companies operating in east Kalimantan. This part of the program will help local SMEs and communities capture a greater share of the economic benefits generated by large-scale extractive industries based in eastern Indonesia. PENSA will establish an extractive industry linkage program based in Balikpapan.

11. Crucial to the success of the program is determining where opportunities lie for SMEs in east Kalimantan. A study will determine the nature of the market's demands, in particular the sourcing requirements of multinational corporations and their relationship with their incumbent suppliers. On the supply side, the study will determine the capabilities of local SMEs and their potential to meet the demands of multinational corporations.

12. The results of the diagnostic study will be used to establish a number of pilot programs working with selected producers and their key customers. The linkage work will operate on two levels: first, as a continuation of the current oil, gas, and mining community development work; and second, by supporting the development of local SMEs to meet the demand for locally sourced higher value-added products. As this linkage work can be replicated in other industry sectors, the program will ultimately develop a model for supply chain linkage and community development, drawing on the experiences of the Balikpapan pilot projects.

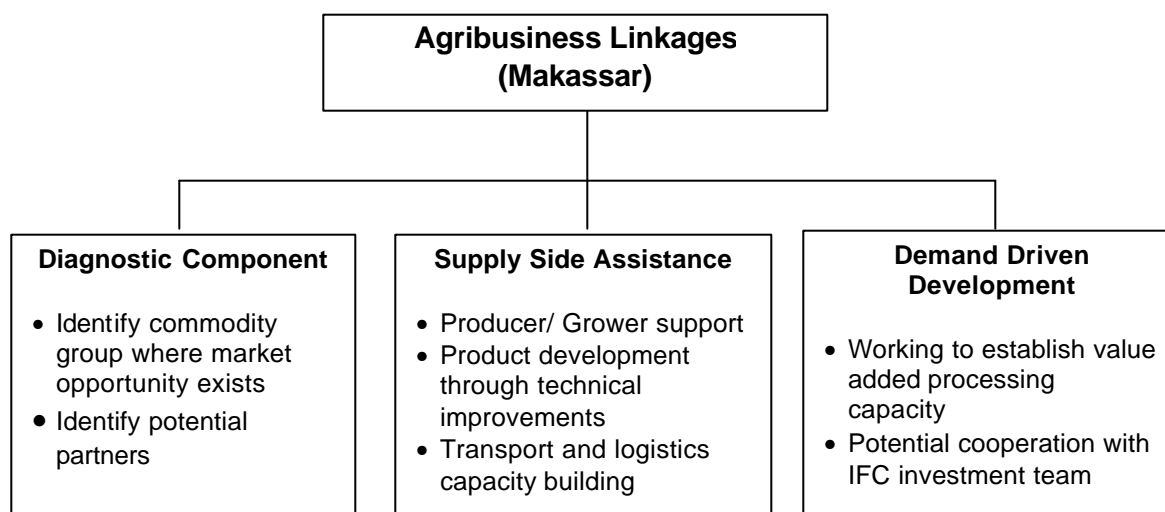
### **D. Agribusiness Linkages (Makassar)**

13. The Makassar program will focus on developing the infrastructure and opportunity for SMEs within the agribusiness sector in south Sulawesi. Agribusiness is the single largest employer, particularly at the lower income level. PENSA will undertake a demand-driven analysis of the potential opportunities present in south Sulawesi for local growers and suppliers of agricultural produce.

14. The program will develop the business environment by strengthening the market for business development services, improving access to capital and forging relationships with universities to improve the technical capacity of local SMEs. The program will also seek to improve transportation and logistics to enhance delivery between south Sulawesi and the end export markets.

15. PENSA will build a linkage to a large local or international processor that will purchase, process, and then market this produce. The program will seek to promote fair trade where labeling can open new markets, and business opportunity will be a powerful incentive to the program's implementation.

Figure A2.2: PENSA's Program on Agribusiness



IFC = International Finance Corporation.

**Table A2.1. Donor Contributions to Program for Eastern Indonesia  
SME Assistance (PENSA), 2003-2008**  
(\$)

Item	Current	FY 2004	FY 2005	FY 2006	FY 2007	FY 2008	Total
IFC		1,000,000	1,000,000	1,000,000	1,000,000	1,000,000	5,000,000
Australia/AusAID		325,000	650,000	650,000	975,000		2,600,000
Japan/MOF		500,000	500,000	500,000	500,000	500,000	2,500,000
Switzerland/SECO	2,531,828	1,085,069					3,616,897
The Netherlands	869,262	870,000	870,000	870,000	870,000		4,349,262
Canada/CIDA		670,000	670,000	670,000	670,000	670,000	3,350,000
<b>Total</b>	<b>3,401,090</b>	<b>4,450,069</b>	<b>3,690,000</b>	<b>3,690,000</b>	<b>4,015,000</b>	<b>2,170,000</b>	<b>21,416,160</b>

AusAID = Australian Agency for International Development; CIDA = Canadian International Development Agency; FY = fiscal year; IFC = International Finance Corporation; MOF = Ministry of Finance; SECO = State Secretariat for Economic Affairs.

Source: Program for Eastern Indonesia SME Assistance (PENSA) estimates, as of August 2003.

**Table A2.2. Program for Eastern Indonesia SME Assistance (PENSA)**  
**Proposed Budget Breakdown, 2003-2008**  
 (\$)

Item	FY 2003	FY 2004	FY 2005	FY 2006	FY 2007	FY 2008	Total
<b>Staff Costs</b>							
Expat Salaries & Benefits	61,875	889,875	934,369	981,087	1,030,142	1,081,649	4,978,996
Other Staff Costs	31,434	687,904	1,006,842	1,274,239	1,337,951	1,404,848	5,743,218
Temporaries							
Consultants	139,800	489,930	490,592	491,286	492,015	492,781	2,596,404
Field Benefits (housing)	13,800	165,600	165,600	165,600	165,600	165,600	841,800
<b>Other Nonoverhead Costs</b>							
Travel	41,550	490,200	629,700	769,200	769,200	769,200	3,469,050
Representation & Hospitality	1,950	15,000	16,500	18,000	18,000	18,000	87,450
Contractual Services	80,000	0	0	0	0	0	80,000
<b>Overhead Costs</b>							
Equipment & Building	161,025	457,828	209,202	200,655	190,450	193,625	1,412,785
Communications	14,200	152,100	152,100	152,100	152,100	152,100	774,700
Other Costs	3,050	78,830	81,690	82,790	82,790	82,790	411,940
<b>Total Direct Costs</b>	<b>548,684</b>	<b>3,427,268</b>	<b>3,686,594</b>	<b>4,134,957</b>	<b>4,238,248</b>	<b>4,360,592</b>	<b>20,396,343</b>
5% Contingency	27,434	171,363	184,330	206,748	211,912	218,030	1,019,817
3.5% IFC Administration Fee <sup>1</sup>	119,038	155,752	129,150	129,150	140,525	75,950	749,566
<b>Grand Total of Costs</b>	<b>576,118</b>	<b>3,598,631</b>	<b>3,870,923</b>	<b>4,341,705</b>	<b>4,450,160</b>	<b>4,578,622</b>	<b>21,416,160</b>
<b>Agribusiness Linkages (Makassar)</b>	<b>16,326</b>	<b>595,334</b>	<b>644,390</b>	<b>731,240</b>	<b>750,757</b>	<b>775,594</b>	<b>3,513,641</b>
<b>% of Grand Total Costs</b>							<b>16%</b>

IFC = International Finance Corporation; FY = fiscal year.

<sup>1</sup> IFC Administration Fee to be waived under ADB's technical assistance.

Source: Program for Eastern Indonesia SME Assistance (PENSA) estimates, as of August 2003.

**EXTENSION TO BRUNEI-INDONESIA-MALAYSIA-PHILIPPINES  
EAST ASEAN GROWTH AREA (BIMP-EAGA):  
THE INDONESIA-PHILIPPINES AGRIBUSINESS LINKAGE (IPAL)  
¾ WORK PLAN AND TERMS OF REFERENCE FOR CONSULTANTS**

1. Facilitation of regional business development services (BDSs) will build on findings and recommendations from the International Finance Corporation (IFC) and Asian Development Bank (ADB). The focus will be on Manado (north Sulawesi, Indonesia) and Davao (Mindanao, Philippines). The BDS consultants, experts, and small and medium-sized enterprise (SME) policy advisors will be part time and full time. The team will operate from out of the Denpasar and Makassar offices, and support both components of the technical assistance (TA) (BDSs for product development and enabling business environment), with emphasis on agribusinesses in BIMP-EAGA.
2. PENSA will undertake special studies for native product development in BIMP-EAGA, including the provision of direct advice to SMEs and their associations on profitable, bankable, and environmentally sound initiatives. PENSA will undertake special studies to identify regulatory constraints in particular industries and to improve environmental protection along with SME development.
3. Details of all assignments involving the TA will be provided to ADB along with a proposed work plan, terms of reference, and deliverables as they are developed by PENSA, and presented to all stakeholders before the start of the TA in early 2004. Below are the estimated work plan for 2004 and sample terms of reference for consulting services to be required under the plan.

**I. Work Plan for 2004**

4. The program will focus on three sectors and will run a number of pilot programs in each sector during the year. The objective will be to determine which projects have the potential for replication and for upsizing in BIMP-EAGA. Pilot projects will be initially carried out in both the Philippines and Indonesia. These will be stand alone projects, however efforts will be made to ensure that the lessons learned on one project be applied to another. In particular, cross-BIMP-EAGA knowledge transfer will be actively stimulated. The initial projects are detailed below and while this list is neither exhaustive nor exclusive.

**A. Seaweed Program**

5. The program will build on PENSA's existing work and would increase its regional impact by raising the level of market information, allowing better risk adjusted investment decisions to be made. Through demonstration projects, the program will illustrate how regional comparative advantage can be turned into international competitive advantage.

**1. Information for Seaweed Industry Strengthening (ISIS)**

- Develop a business plan for the establishment of ISIS as a private-sector orientated information service provider;
- Commence the development of ISIS, record baseline information, attract private sector partners, create a network of production industry market intelligence providers, establish links with collaborative information service providers, develop an ISIS bulletin for test

marketing to potential clients and a website portal with technical specifications, standards and post-harvest content;

- Develop ISIS into a stand-alone fee for service commercial BDS operation.

## **2. Demonstration Programs to Increase Local Value Addition**

- Promote improved production techniques, such as deeper water production, quality seed stock and post-harvest handling, with demonstrations in both marine and coastal and brackish water pond environments;
- Increase value added processing at a local level such as semi-refined carrageenan processing and agar sheet production at village level;
- Strengthen business associations;
- Facilitate access to credit; and
- Investigate larger scale processing opportunities.

## **B. Coconut Program**

6. The coconut program will help to develop high value-added coconut products. Working on a pilot project basis, the program will identify potential new products and promote their commercialization in partnership with private partners.

### **1. Virgin Coconut Oil**

- Work with CIDA under its Private Enterprise Project (PEP) to help commercialize a new technology for the production of virgin coconut oil;<sup>1</sup>
- Develop further the plans for a medium-sized virgin coconut oil factory which will collect the semi-finished oil production from the household units;
- Complete the production process to reduce moisture levels and filtering; quality control; packaging and distribution; and
- Provide additional TA alongside PEP to support this evolutionary process such as market assessment, analysis of distribution channels, supply chain linkages, production and general management training, and business plan preparation.

### **2. Other Coconut Products**

- Identify other potential pilot projects (including activated charcoal and coconut yogurt) in eastern Indonesia and/or southern Philippines; and
- Ascertain their financial viability as well as their development impact.

## **C. Sustainable Fisheries Program**

7. The program will initially work to help strengthen the supply chain for sustainably-caught aquarium fish. Through business training and association strengthening PENSA will work to support the development of a business case for the sale of sustainably-caught fish by supporting and contributing to the work of the Marine Aquarium Council (MAC) and the Marine

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<sup>1</sup> CIDA has developed a machine that produces high-grade virgin coconut oil through a separation process, and is currently undergoing field tests.



Aquarium Market Transformation Initiative (MAMTI).<sup>2</sup> MAC has pilot programs in the Philippines and Indonesia, and through MAMTI, is now preparing to scale up its operations in the Philippines and extend the scope of work into Indonesia, in partnership with PENSA and other specialized nongovernment organizations (NGOs).

### **1. Developing Fish Trade in the Philippines and Indonesia**

- Develop BDSs for prospective SMEs in fish trade (such as improvements in inventory handling and tracing);
- Facilitate transfer of knowledge from southern Philippine Pilot projects to Indonesia;
- Develop opportunities for southern Philippine BDS providers to expand operations into Eastern Indonesia; and
- Identify and develop Eastern Indonesian demonstration sites.

### **2. Linking SMEs to Supply Chain and Capital**

- Strengthen SMEs to better participate in the supply chain;
- Strengthen local BDS companies to deliver relevant market driven services, with focus on business management including information technology (IT) applications;
- Develop village-level organizations that will enable economies scale; and
- Improve access to capital through an investment vehicle to promote conversion to MAC-certified practices in partnership with CoreResources (a San Francisco venture capital fund), the Conservation and Community Investment Forum (CCIF) and PENSA.

## **II. Sample Terms of Reference for Consultants**

### **A. Business Development Service Specialists**

8. The specialists will work under the supervision of PENSA. The specialists will have experience in BDS and industry requirements such as licenses, relevant to the dominant industry in the SME sector of the selected municipalities, especially agribusiness. The specific tasks are the following:

- (i) Assess local needs of SMEs for BDSs;
- (ii) Identify BDS providers and NGOs suitable for agribusinesses in these municipalities;
- (iii) Help develop and implement training programs for BDS providers in specific business technical services such as international marketing, basic accounting systems, trade finance, feasibility studies and business plans, information technology (IT) in business operations, among other relevant areas for SME development according to assessment;
- (iv) Help to commercialize BDS provision or NGO activity to support business development;
- (v) Build capacity to implement monitoring and performance evaluation concepts of BDS providers and SMEs served by these providers; and
- (vi) Work to strengthen the business associations or community level organizations to enable greater efficiencies.

<sup>2</sup> MAMTI aims to convert a substantial portion of the marine aquarium industry into a trade-based marine conservation for sustainable livelihoods. It is a tripartite agreement between the Marine Aquarium Council, the Conservation and Community Investment Forum (CCIF), and Reef Check.

**B. Agribusiness Technical Specialists**

9. Technical specialists will be required on both a short and long term basis to deliver technical support to the program. These individuals will be expert in particular sectors relevant to the program. The technical experts will likely be based in one location but their work will cover all of the areas covered by IPAL within BIMP-EAGA.

- (i) Develop and implement training programs to improve the quality and quantity of products produced;
- (ii) Examine the ecological, biological and economic opportunity for a particular crop;
- (iii) Provide technical advice to potential new market entrants;
- (iv) Introduce international best practice to and facilitate knowledge transfer within BIMP-EAGA; and
- (v) Prepare reports recommending how legal and regulatory changes could improve productivity for a particular crop.

## COST ESTIMATES AND OPERATING PROCEDURES FOR DIRECT AWARD UNDER TECHNICAL ASSISTANCE

### A. Cost Estimates

Item	Total Cost (\$)
<b>Asian Development Bank (ADB) Financing<sup>a</sup></b>	
1. International Consultants	180,000
2. Domestic Consultants	270,000
3. Training and Workshops	110,000
4. Equipment <sup>b</sup>	18,000
5. Reports and Studies	40,000
6. Printing and Publication	10,000
7. Communications (fax/phone)	14,000
8. Miscellaneous Administrative Expenses	8,000
9. Contingencies	50,000
<b>Total</b>	<b>700,000</b>

<sup>a</sup> Financed by the Japan Special Fund, funded by the Government of Japan.

<sup>b</sup> Computers, printers, and air conditioners for use during the technical assistance will be disposed of by Program for Eastern Indonesia SME Assistance (PENSA) among the participating producers' associations, NGOs, and chambers of commerce, according to ADB's disposal guidelines.

Source: ADB staff estimates.

### B. Operating Procedures

1. Technical assistance (TA) funds may be used to meet the costs of consultants recruited by the Program for Eastern Indonesia SME Assistance (PENSA) for specific project assignments as detailed here. The Asian Development Bank (ADB) and International Finance Corporation (IFC) will enter into an agreement incorporating the following eligibility criteria and operating procedures:

- (i) Consultants will work on assignments undertaken by PENSA to promote viable private sector SME projects, thereby contributing to self-sustaining economic growth in BIMP-EAGA.
- (ii) Viable and suitable projects developed using TA funds will be referred to ADB for potential financing by ADB and IFC.
- (iii) Each individual consultant will be selected and engaged in accordance with IFC consultant recruitment procedures that are consistent with ADB's *Guidelines on the Use of Consultants*. In particular, PENSA will ensure that qualified candidates from all ADB member countries are eligible for consideration for any TA-financed assignment.
- (iv) Eligible expenses under the TA are fees, airfares, and subsistence payments to consultants, and for workshops, training, and support services determined in accordance with IFC standard procedures and guidelines, consistent with ADB guidelines.

- (v) Except as ADB may otherwise agree, work undertaken by consultants will be carried out in, or related to, projects in eastern Indonesia (north Sulawesi) and southern Philippines (Mindanao) during this TA.
- (vi) Except as ADB may otherwise agree, TA funds will not be applied to any single consulting assignment with a total cost exceeding \$200,000 equivalent.
- (vii) Following an initial advance payment (\$100,000), PENSA will then submit semiannual claims to the director of the Governance, Trade and Finance, Southeast Asia Department, ADB, for reimbursement of eligible expenses under the TA under the statement of expenses, a simplified procedure for international organizations such as IFC and the World Bank. Such claims will provide details required by ADB, including the name and country of the project; name, address, and nationality of the consultant; and expenditure category (fees, travel expenses, subsistence expenses, workshop, training, support services, etc.). ADB will remit the reimbursement upon review and acceptance of the claim.
- (viii) PENSA will submit to ADB semiannual status reports covering all of its projects. PENSA officers and consultants will meet and communicate regularly with ADB to discuss TA-funded projects to update workplan, ensure close coordination and information sharing. As advisor to BIMP-EAGA, ADB headquarters (Governance, Finance, and Trade Division, Southeast Asia Department [SERD]) will attend the Donor Oversight Committee for PENSA, and advise BIMP-EAGA national secretariats about relevant activities under the TA. SEGF will also coordinate communications with the Private Sector Operations Department and resident missions (Indonesia Resident Mission and Philippines Country Office).
- (ix) TA-funded projects will have a demonstrative, positive development impact in BIMP-EAGA.
- (x) While PENSA does not normally process TA completion reports, ADB will receive status reports and all specific reports financed under the TA. A TA completion report will be prepared by ADB and shared with other PENSA multilateral and bilateral funding agencies, IFC, and the World Bank.