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Micro, Small and Medium-sized Enterprises and the Global Economic Crisis

Impacts and Policy Responses

Sustainable Enterprise Programme



International Labour Organization

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Impacts and Policy Responses

Paul Vandenberg

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Foreword

The depth and severity of the global economic slowdown that began in 2008 has caught employers, workers and governments by surprise. What was first a problem stemming from lax mortgage lending in the U.S. has mushroomed into a global financial, economic and employment crisis. Governments around the world have responded by loosening monetary policy and then increasingly using fiscal policy to revive or prevent a fall in consumption and investment. The full effects of these measures are not yet known. It is hoped that they will help to ensure that the slowdown in demand is limited and that consumers will increase their spending, financial institutions will resume their lending and businesses will begin investing and hiring again.

While businesses of all sizes have been affected by the crisis, this booklet focuses attention on micro, small and medium enterprises (MSMEs). They contribute substantially to output and employment in both developed and developing countries. The ability of countries to limit the layoffs and closures of these enterprises will contribute greatly to the revival of the global economy and of individual national economies.

This booklet serves three main purposes. Firstly, it presents an analysis of the key issues that MSMEs face as a result of the crisis. Secondly, it provides real examples of measures that governments have taken to support these enterprises. And thirdly, it outlines the ILO's Five Point Crisis Response for MSMEs.

The booklet is part of a series on the crisis being produced by the Sustainable Enterprise Programme. Other booklets focus on the Resilience of the Cooperative Business Model, the Promotion of Responsible Enterprise-level Practices, and possibly other topics.

Executive summary

- While losses and layoffs at large firms are making headlines, many micro, small and medium-sized enterprises (MSMEs) are also severely affected by the global economic slump of 2008-09. Weak demand and tight credit are the chief pressures faced by these enterprises. Demand stimulus measures will assist all enterprises, whereas access to finance needs more specific targeting for small firms. Cooperatives (i.e. cooperative enterprises) appear to be the least affected by the crisis.
- The employment pillar of the Decent Work Agenda, which promotes the creation and maintenance of productive employment opportunities, is certainly under threat during the current downturn. One or more of the other three pillars (rights at work, social protection and social dialogue) may also be affected, although in less obvious ways.
- Many stimulus packages include specific measures for small and medium-sized enterprises. These measures include assistance with taxation, trade, credit and procurement. In addition, measures that apply to firms of all sizes support smaller enterprises operating in the formal sector. It is important that business owners are aware of these programs and can access them easily and without undue bureaucratic delays or paperwork.
- There is limited direct help for informal and micro-enterprises, which dominate the enterprise landscape in most developing countries. Micro-business startups are likely to increase as laid-off workers and returning migrant workers seek to make a living. Success for these new businesses and indeed many existing ones will be difficult to achieve, given weak demand and limited credit access. Entrepreneurs will need to be entrepreneurial in seeking out and exploiting new business opportunities.

- While government interest rates have fallen, credit is scarce because banks are risk averse and have difficulty screening even good clients in a downturn. Governments are attempting to reduce the shortfall by expanding loan programs. Many governments have created or are expanding loan guarantee programs for the MSME sector. These include developed countries such as the UK and developing ones such as India.
- Where possible, permanent layoffs are being averted through various measures including work-time reductions, temporary shutdowns, training schemes and employee retention subsidies. Unemployment insurance, where it exists, is being extended and used to fund training in some cases.
- Employers' organizations and trade unions have added their voices to the debate about appropriate crisis management measures. Some countries have reached tripartite agreements to promote economic activity and reduce social tensions during the crisis.
- The ILO's Five Point Crisis response for MSMEs offers support to policymakers and enterprises through: i) rapid assessments to pinpoint the constraints felt by MSMEs; ii) advice through examples on managing credit; iii) advice to policymakers on public procurement; iv) advice and training on business development services, notably entrepreneurship and enterprise management training; and, v) advice and training on supporting small business associations to take an active advocacy and support role during the crisis.



1. The evolving crisis

The global economy is experiencing its greatest slowdown since the Second World War. Due to the increased integration of goods, services and financial markets, the crisis has spread from housing and credit sectors in the U.S. to other markets and countries around the world. There are few, if any, economies that been left untouched by the crisis. The collapse of Wall Street investment banks and American mortgage lenders has had serious knock-on effects for commercial banks and non-financial companies around the world.

Credit everywhere is tight as lenders seek to shore up their financial positions and increase their precautionary reserves. Borrowers have become suspect as creditworthiness is difficult to assess. Businesses in the real economy have found it hard to survive, resulting in increased layoffs and closures. Retrenchment translates directly into a decline in the opportunities for women and men to engage in decent work. Thus, the credit crisis has developed, via weak demand, into a full-blown economic crisis. Many developed countries slipped into recession in the last quarter of 2008 and many developing countries have seen their growth rates plummet.

The crisis is affecting firms of all sizes. While large firms grab headlines when disclosing layoffs and dramatic declines in sales and earnings, many micro, small and medium sized enterprises (MSMEs) are also trying to cope with weak demand, tight credit and reduced orders from larger companies. Small businesses across a range of sectors and organizational types have been affected, although preliminary evidence suggests that the cooperative form of enterprise is managing particularly well and many are adding new members.¹

¹ According to the International Cooperatives Alliance and the ILO's Cooperatives programme



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MSMEs, which account for over 90% of enterprises in all countries, are an important source of output and employment.

They employ 33% of formal sector workers in low-income countries and 62% of such workers in high-income countries.² Because poor

countries have large informal economies, dominated by micro-businesses, the MSME portion of total employment is much higher. In India, for example, 86% of the labour force is employed in the informal sector, including farming. The crisis has not only hit Wall Street and Main Street, but it has affected the side streets, the dirt streets and the markets where many small retailers and producers thrive.

This booklet analyses the constraints faced by MSMEs during the current crisis and reviews the actions taken by policymakers. Section 2 focuses on the various aspects of Finance while Section 3 is dedicated to Demand and Employment and includes such issues as public procurement, changes in taxation policies and self-employment. Country examples are used frequently so that this booklet can act as a means of sharing experiences and providing ideas to countries that have, as yet, focused only limited attention on the needs of small business. Section 4 outlines the ILO's Five Point Crisis Response for MSMEs so as to provide constituents with ideas of how they can best collaborate with the ILO in this area. Section 5 addresses more specifically the actions that the social partners can take to ensure that there is a shared approach to managing through the crisis, notably as it pertains to maintaining decent work. Cooperatives (i.e. cooperative enterprises) are not included in the analysis both because they appear to be weathering the current crisis better than other small businesses and because they are the subject of a companion ILO publication.

² *World Employment Report 2004-05* (Geneva: ILO), p. 228

Many, if not most, of the stimulus packages announced by governments in late 2008 and early 2009 include measures for the MSME sector. This is true of both developed and developing countries. For example, an announcement by Indian Prime Minister Manmohan Singh on the country's first stimulus package, stressed that "The Government attaches the highest priority to supporting the medium, small and micro enterprises (MSMEs) sector which is critical for employment generation".³ Similarly, Peter Mandelson, the UK's Business Secretary, when outlining measures to increase credit to small and medium enterprises, stated that "UK companies are the lifeblood of the economy and it is crucial that Government acts now to provide real help to support them through the downturn."

The MSME sector is highly varied, both within a country and between richer and poorer countries. Formal sector firms, working within the framework of formal credit institutions, tax regulations and social security programs can benefit from changes to the policy environment that are designed to assist enterprises during the downturn.⁴



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³ Government announces measures for stimulating the economy', Press release, Prime Minister's Office, India, 7.12.08.

⁴ Real help for business,' Press release, U.K. Department for Business, Enterprises and Regulatory Reform, 14.01.09

Job cuts at small industrial firms in Pune, India

The Indian economy lost half a million jobs in the last quarter of 2008, according to a conservative estimate. Many of the affected firms are small ones which have grown up over the last decade as large Indian firms have taken eagerly to outsourcing as a competitive strategy.

- In Pune, in central India, small industrial firms have cut jobs as work from their buyers has fallen. "As of now, over 40,000 workers have lost their jobs and we fear that number may increase," says Nitin Bankar, President of the local Small Scale Industries Association.
- One of the companies that may be shutting down currently supplies Tata Motors, the homegrown car and bus manufacturer. Prakash Dhawale, who worked at the company until recently, is concerned he will not be re-employed. "Our children are studying, our daughters are yet to marry," he says. "We are thrown out on the streets like this. The government must help."
- Workers have come to Pune from the small villages and towns in the rural areas over the years. They are finding it hard to survive and many are moving back. "We used to have a lot of work here earlier," says Gagan, a carpenter. "But now there is no work, so we are returning."

'Big trouble for small industries in Pune'
www.ndtv.com, 04.02.09

Micro enterprises, notably those operating in the informal sector, constitute the vast majority of businesses in most developing countries. They include what are often called own-account workers, the self-employed and small family operations. They are unlikely to benefit directly from changes to the formal policy environment and from efforts to expand credit through banks and other formal lenders. They will only benefit from procurement and infrastructure programs if they are consciously included. In addition, small and medium firms engaged in export-related industries, producing either final products or components in a value chain, are being affected as recession hits importing countries.

Governments in many countries have responded with a range of policies, often combined together in fiscal stimulus packages. These policies are designed to stabilize the financial sector but also support companies and workers in the real economy. Many enterprise-related policies provide assistance to companies of all sizes, while others specifically target the MSME sector. Policy support is also designed for specific (notably exporting) sectors where smaller firms are known to be a significant part of the enterprise landscape.

Voices of shopkeepers in Delhi

"It has been slow for the last several weeks, since Christmas," says the young man taking orders for freshly dressed chickens at INA Market.

In upscale Khan Market, one grocer has seen a dramatic decline. "We are about 25 per cent down," he says. The decline has been evident for the past six months. People are buying necessities (fruits and vegetables) but cutting backed on the higher-priced packaged goods.

"We are about 10 to 15 per cent down," says the owner of a durable goods supplier in Khananna Market. "The Sunday afternoon crowd is down," he says. Large flat screen TVs are not selling well with the public or business clients. He supplied a building with 10 flat screens last year. The same client completed a similar building this year but wanted only one screen.

"Business is good," says the man handling the cash register at the popular Evergreen Sweets in Green Park. His 12-person sales crew is working at a brisk pace. Asked if the shop is affected by the economic slowdown, he replies, "Yes, we are down a little, but not much."

Interviews, 02.09, P. Vandenberg

2. Finance

Access to finance and low demand are the chief factors affecting small businesses in the current downturn. Governments have responded by loosening monetary policy, strengthening banks, encouraging lending and providing demand stimulus through fiscal policies. It is too early to tell which policies will be effective in supporting recovery. This section sets out the various financial constraints faced by small businesses and the measures being taken by policymakers. Examples are provided from both developed and developing countries.

Credit has tightened in most countries and not only where banks held mortgage-backed securities (MBS) and collateralized debt obligations (CDO) linked to the U.S. housing market. Most governments have cut interest rates, lowered reserve ratios and urged lenders to pass on lower rates to their customers. As few countries set the rates that are charged by commercial banks, lower rates in the inter-bank markets are not automatically passed on to commercial customers. In addition - and in most cases more importantly - lenders are offering fewer loans.

Credit has tightened for small enterprises in many countries although the actual impact is not well known. A survey of banking executives in 19 Latin American and Caribbean countries in late 2008 found that 58% expected that less credit would be available to SMEs during the coming year. Just under half of the executives thought that the interest rates on loans to the sector would increase.⁵ Many governments have anticipated this slowdown in lending and have sought to preempt it through measures in their stimulus packages.

⁵ 'IDB, IIC, Felaban pool shows continued SME credit interest despite crisis,' Business News Americas, 13.02.09.

Banks and non-bank financial institutions are consolidating their own financial positions by ensuring adequate reserves as a precaution against delinquency and default. These prudential measures have reduced the flow of new lending and the extension of existing lines of credit in many countries. Lenders are finding it difficult to assess creditworthiness in the downturn. A stable company last year may be risky this year, notably if demand has slumped for its products or services. Even enterprises with a good credit history are finding it difficult to obtain loans.

In the UK, where the number of small business closures rose dramatically to 85 per day in early 2009, the Federation of Small Businesses summarized the problems succinctly: "Costs are up, orders are down and banks are not being helpful."⁶ Smaller enterprises that can access credit in good times now face difficulties. Micro-enterprises and some small business which are unable to access credit under normal conditions will continue to be shut out during the crisis.



⁶ Small business closures hit 280 a week', *The Guardian* (UK), 23.10.08 and 'Banks have run out of excuses as Government announces £1 billion fund for small business', press release, Federation of Small Businesses, 14.01.09. The number of UK closures rose from 280 per week in October 2008 to 85 per day in early January, according to FSB.

Lobster fisherman needs working capital, Canada

Many small firms are in need of working capital during the downturn. Even though they may have a good credit repayment history, their bank may be short of funds to lend. This is the case of a Canadian lobster fisherman.

The fisherman from Prince Edward Island, on the east coast, supplies high-end restaurants in the region. With the downturn, many of his regular customers were becoming delinquent in their payments. The fisherman asked his bank to increase his working capital line of credit. Despite a good credit history and being current in his payments, the bank denied the increase, citing pressure on its own funds.

The fisherman was able to secure extra financing from a public sector financial institution that has received funds through the federal government's new Business Credit Availability Program. The program is providing C\$5 billion for on-lending to businesses during the global slump.

'Canada's Economic Action Plan'

Budget 2009, 27.01.09 (p. 82)

The following sub-sections discuss specific types of finance and the measures being taken by governments.

2.1 Investment lending

Few small businesses are initiating new investment projects in sectors and countries where demand is weak. Existing projects, notably those that are more than three-quarters finished, are likely to be completed because of the sunk costs and thus the need to begin generating a return.⁷ In countries and sectors that are less affected by the crisis, the desire for investment loans will be stronger. Banks are scrutinizing investment proposals more closely.

⁷ The idea that projects ¾ completed would continue was provided by an industry expert in India. The figure is a rough estimate and relates to all sizes of business.

Many countries are ensuring that specialized lenders have sufficient resources to extend loans to small borrowers. For example, the central bank has provided \$1.45 billion to the Small Industries Development Bank of India to deal with the downturn. The Chinese government has eliminated credit ceilings imposed on commercial banks to channel more loans to various areas including small enterprises and to encourage investment in technical innovation. The European Investment Bank, which regularly provides about €5 billion annually to banks for on-lending to small and medium enterprises, has increased the amount to €7.5 annually for 2008-11. The increased allocation is designed partly to support SME sector during the global downturn and partly has a long-term effort to increase support to these enterprises.⁸

Credit policy options

- Continue with loose monetary policy to encourage low interest rates
- Ensure adequate MSME lending through state-owned development and commercial banks
- Ensure adequate credit for working capital requirements
- Increase lending through enterprise support programs
- Expand micro-credit to micro-businesses, including those newly created by laid-off workers
- Improve access to finance for exporters
- Encourage prompt payment and enforce rules on late payment in the private sector
- Ensure local, provincial and federal governments pay promptly their bills to MSMEs
- Expand the coverage and decrease the enterprise cost of credit/loan guarantee schemes
- Ensure access to equity finance
- Assist enterprises in preparing high quality loan proposals

⁸ 'EIB rolls out SME funding scheme', www.euractiv.com 13.02.09

2.2 Working capital

A chief concern of enterprises is to ensure sufficient working capital, especially when payments for goods sold or services provided are delayed. This involves, in part, astute cash flow management, tight tracking of accounts receivable, maximizing the use of supplier credit and managing overdraft facilities. Several countries have instituted programs to support working capital, notably through loan guarantee schemes (see below).

2.3 Credit guarantees

Banks may have the funds but are restricting lending to enterprises due to the negative economic environment. As a result, governments have created or expanded guarantee schemes or reduced the costs paid by borrowers. For example, the size of loans covered under the Credit Guarantee Scheme in India has doubled to approximately \$200,000. The guarantee covers half of the loan amount, but 85% for micro loans up to \$10,000.

In the U.K, two major programs have been launched for small and medium firms.⁹ The Working Capital Scheme provides a government guarantee for 50% of the value of short-term loans provided by commercial banks. Total lending of £20 billion will be guaranteed and the scheme applies to firms with turnover of under £500 million. The Enterprise Finance Scheme is for smaller firms, with turnover up to £25 million and will provide guarantees for a total of £1.3 billion in bank lending for working capital or for investment loans of up to £1 million. It can also be used to covert existing overdrafts into loans to free up the overdraft.

⁹ 'Real help for business', Press release, U.K. Department for Business, Enterprises and Regulatory Reform, 14.01.09.

2.4 Equity

Finance provided by venture capital funds and business angels has declined in several countries, although good data is generally not available.¹⁰ In most developing countries, this type of finance is not well developed, especially for small firms. Governments have, however, taken equity positions in struggling banks and, in a few cases, in non-financial enterprises. These latter schemes allow a business to convert debt into equity to improve its financial position. In Mauritius, for example, the government is offering to take an equity stake in manufacturing firms, notably small and medium textiles firms, which need to restructure due to weak international demand.¹¹ In the United Kingdom, the Capital for Enterprise Fund will finance the conversion of business debt into equity. The government will provide £75 million and the main commercial banks an additional £25 million. The scheme is open to large and small companies.¹²



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- ¹⁰ 'Issues Paper', Turin Roundtable on the Impact of the Global Crisis on SME and Entrepreneurship Financing and Policy Responses, OECD, Turin (Italy) 26.03.09, pp. 16-17
- ¹¹ 'Additional Stimulus Package: Shoring up economic performance', Government of Mauritius, December 2008
- ¹² 'Real help for business,' Press release, U.K. Department for Business, Enterprises and Regulatory Reform, 14.01.09.

Credit support - Country examples

- Mauritius: MRs 100 million directly to small and medium enterprises that need assistance with liquidity or to restructure
- India: US\$1.4 billion to the Small Industries Development Bank of India for direct or indirect on-lending to MSMEs
- China: Government financial support and insurance to small textile and garment firms, hit by the sharp decline in export demand.
- UK: Loan guarantees for £20 billion in working capital to enterprises with turnover of over less than £500 million; and guarantees for £1.3 billion of other bank lending to enterprises with turnover of less than £25 million ¹³
- Canada: raised the maximum loan amount to C\$350,000 and to C\$500,000 for real property under the existing the Canada Small Business Financing Program, which should increase lending by C\$300 million; the loans are guaranteed up to 85%.



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¹³ 'Real help for business,' Press release, U.K. Department for Business, Enterprises and Regulatory Reform, 14.01.09



Facilitating loan applications in Singapore

The Financial Facilitator Program was established in Singapore to provide free advice to small enterprises on finance and loans during the slump. Assistance will be given to: diagnose the health of their enterprise; understand financing options; and, put together a high-quality loan application.

Mr. Png Cheong Boon, chief executive of SPRING the government's business support agency, says, "One common feedback from the banks is that many SMEs are unable to present their case to the banks." The new service will be provided at the island's six business membership organizations, including the Association of Small and Medium Enterprises.

SPRING also lowered rates on loan programs for small enterprises. Interest rates were cut by 1.25%, with the rate for loans of 4 years or less falling to 5%. The changes will affect 13,540 existing loans and new ones. The government's portion of loan insurance is being raised from 50% to 90%. Thus an enterprise will pay only 0.15% of the loan amount for the insurance, which, in total, costs 1.5% of the loan amount.

SPRING website

2.5 Export finance

Recession in developed economies has reduced global trade and cut exports from developing countries. Exporters have sought relief in the form of reduced export financing costs. Labour-intensive goods from developing countries have been particularly affected by the slump, notably in sectors with a heavy small enterprise presence. The textile sector has been particularly affected in India, China and other countries. To provide general relief to exporters, the government in India is providing an interest rate subsidy of two per cent on pre- and post-shipment export credit for labour-intensive exports and those produced by small and medium enterprises.

2.6 Receivables and supplier credit

The credit squeeze may be affecting inter-firm finances, although it is hard to know the full extent of this problem. Small enterprises generally have difficulty receiving timely payment from larger firms, given the power imbalance. During a credit squeeze, accounts receivable may mount and reduce further the funds available for working capital. (As part of its crisis response, the Indian government has instructed all public sector departments and companies to ensure prompt payment to micro, small and medium firms.) In addition, small firms rely regularly on credit from suppliers to meet working capital needs for inputs and sales inventories. In a crisis, such credit may be more difficult to secure or the terms may be more demanding. Small firms may need to try to compensate in other ways, either through the use of their overdraft (if they have such access), by securing new government lending or by better management of finance in other areas.

2.7 Micro-finance

Household-based micro businesses and some small businesses rely on micro-credit for working capital and for needed investments in tools and machinery. The crisis is putting pressure on these lending operations but much depends on the nature of the micro-finance institution (MFI) and its clientele. Deposit-based institutions are weathering the crisis better than non-deposit institutions, which instead rely for funds on outside sources including government development banks and foreign capital sources, including donors.

Financing has become scarcer and more expensive during the crisis and foreign finance is prone to the added risks of exchange rate movements. One Indian micro-finance institution said the cost of borrowing (for on-lending to its clients) had recently risen by 2-3%, while another institution noted that "banks are taking more time to lend to MFIs".

Some experts in the micro-finance industry feel that the crisis may encourage a focus on sound micro-banking practices and an increased emphasis on local funds generation through deposit-taking. The risk is that governments may meddle needlessly. Claudio Gonzalez-Vega, an expert at Ohio State University, sees the following risks: "interest rate ceilings, mass loan forgiveness, the encouragement of delinquent borrower associations [and] the development of credit programs in government agencies that lack financial experience." Some of these practices are already in evidence.¹⁴



¹⁴ The section is derived from a written summary of 'CGAP Virtual Conference: Microfinance and the financial crisis,' 18-20.11.08

3. Demand and employment

The financial crisis has evolved rapidly into a crisis of demand and employment. Reduced access to credit for businesses, homeowners and consumers, along with uncertainty, has stalled demand in the U.S. and increasingly in other parts of the world. The American economy is set to shrink by 2.8 per cent and the Euro-zone by 4.2 percent in 2009. Together these two markets account for more than a third of global demand. Overall, the world economy is likely to see output fall by 1.3 per cent.¹⁵ The slump is having a profound affect on trade for both developed and developing countries. Trade flows grew by only 2% in 2008 and are expected to fall by 9% in 2009. Early in the crisis many commentators suggested that the developing world has become increasingly 'decoupled' from developed economies and would not be vulnerable. As the WTO has noted recently, however, this "has not turned out to be the case."¹⁶

Export-oriented sectors felt the impact early, along with construction. The impact has been uneven, however. For example, manufacturing exports from China's coastal are down considerably but low-end ready-made garments from Bangladesh which supply discount retailers such as Wal-Mart appear to be doing reasonably well.¹⁷ Footwear and handicrafts exports have seen a decline. The commodities picture is more complex because prices for many goods, notably food, petroleum and steel, rose dramatically in the first half of 2008 be-

¹⁵ *World Economic Outlook, April 2009* (Washington: IMF 2009). For share of global expenditure: *World Development Indicators*, World Bank, figures for 2007 PPP.

¹⁶ 'WTO sees 9% global trade decline in 2009 as recession strikes', WTO press release, 24.04.09Ibid.

¹⁷ This is according to experts that the author met in Dhaka in May 2009.

fore falling significantly as a result of the crisis.¹⁸ Higher food prices tend to be good for rural producers but impact negatively on consumers; be they rural or urban.



The decrease in demand has put serious pressure on enterprises of all sizes to reduce staff. Indeed, the ILO estimates that global unemployment increased by 11 million people in 2008 and may increase by an additional 40 million in 2009.¹⁹ In China, the steep decline in exports has resulted in the layoff of 20 million workers. The

US economy lost 4.4 million jobs since the crisis there began in late 2007²⁰ and the Indian economy lost half a million jobs in the last three months of 2008.²¹ Unemployment rates are rising to levels not experienced for decades. The jobless rate in Spain reached 14.9% in January 2009, for example. Layoffs in developing countries are pushing large numbers into poverty. As Michelle Bachelet, President of Chile, said recently about the crisis, "We need to focus on what is necessary - and today that is to guarantee employment."²²

The crisis is also impacting on the demand for migrant workers and reducing the remittances they send back home. It is currently unclear whether, glob-

¹⁸ For example, the world export price of rice rose by May 2008 to over 130% of the previous year's average and then fell by 28% by early 2009.

¹⁹ 'The financial and economic crisis: A decent work response,' ILO Governing Body, ESP Committee, 04.09

²⁰ 'When jobs disappear', *The Economist*, 14.03.09

²¹ 'Report on effect of economic slowdown on employment in India', Ministry of Labour and Employment, 01.09

²² 'Chile's Bachelet sets date to combat unemployment,' *La Nación* (Santiago) .4.03.09

ally, the net flow of migrants is positive or negative,²³ but certain countries, including Nepal and Bangladesh, do expect a large reflow of migrants.²⁴ The pull factors that entice people to seek work abroad (vacancies, better pay) have certainly weakened. At the same time, however, the push factors have strengthened (few opportunities, low remuneration at home). Even where workers decide to remain in a foreign country, they face increasing difficulty in finding decent paying jobs and thus maintaining the flow of money home. In 2009, global remittances are expected to fall by 5-8%, the first annual decrease in almost 25 years.²⁵ While some existing migrants are returning home after losing their jobs, others are shifting to different sectors. In the U.S. for example, there has been a move from manufacturing and construction work into hotels and restaurants, and wholesale and retail trade.²⁶

Governments have responded to the slump with fiscal stimulus packages to boost demand and support employment. Such measures have taken the form of infrastructure and procurement measures, employment programs and changes to tax policies. These programs provided opportunities for MSMEs as well as large enterprises.

3.1 Infrastructure and procurement

Many of the fiscal stimulus packages now being implemented include infrastructure development, such as the building of roads, ports, houses and schools. In some cases, they are designed to engage needed development (rural infrastructure), the dredging of rivers (Korea) or the creation of green jobs. Such stimuli are designed to create employment either directly on the projects or indirectly through machinery and inputs that companies will supply to those projects. The speed at which governments can implement those projects will determine how quickly they can contribute to reversing the downturn.

²³ According to the World Bank.

²⁴ Opinions of researchers in Kathmandu and Dhaka as told to the author in May 2009.

²⁵ 'Revised outlook for remittance flows 2009-2011', D. Ratha and S. Mohapatra, Migration and Development Brief 9, World Bank, 23.03.09. Global remittances doubled over a five-year period beginning in 2003, reaching \$305 billion in 2008, or 1.9 per cent of those countries' GDP.

²⁶ Ibid.

For many of the larger projects, governments may seek to engage large firms, although high capital intensity will limit the employment creating benefits of such stimulus measures. Governments that use labour-intensive practices will see a greater employment impact. This approach may include the contracting of work to MSMEs.

Governments can also support procurement in other ways. For example, the Mexican stimulus package requires that at least 20 per cent of government purchases be made from small and medium companies.²⁷ Small tenders and the decentralization of procurement decisions can also increase opportunities for small firms.



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²⁷ 'Stimulus plan to curb impact of crisis', IPS News Agency 18.03.09

In the UK, the government launched a campaign in the midst of the crisis urging small businesses to register with its on-line procurement portal. In February 2009, there were over 100,000 supply opportunities, with many of the contracts valued at less than £100,000. About 3,000 new contracts are advertised every month and 123,000 firms are registered on the portal. According to Ian Austin, a Regional Minister, "Every year the government spends billions of pounds with SMEs on public sector contracts... Many of them are lower-value contracts that until this website were difficult to find out about".²⁸



Infrastructure and procurement options

- Ensure there is no enterprise size minimum for bidding on projects, where feasible
- Source MSMEs for small projects and components of large projects
- Reserve a specific percentage of government contracts for MSMEs
- Favor bids with high employment intensity

²⁸ 'West Midlands SMEs urged to sign up for Government contracts', Press release, U.K. Department for Business, Enterprises and Regulatory Reform (West Midlands), 04.02.09.

3.2 Taxation

A reduction in tax can ease working capital constraints for businesses and stimulate demand among consumers. As taxes are levied at several levels - income, production, value added, sales and imports - there is considerable room for governments to make cuts. Many of these measures are applicable to enterprises of all sizes but governments are aware that in many cases they will benefit MSMEs.²⁹

Anggito Abimanyu, Chief of Policy Affairs, Ministry of Finance in Indonesia, explained his country's approach to tax changes during the slowdown: "[Businesses] can save costs from not paying their taxes which will increase their profits."³⁰

Such cuts result in the loss of public revenues but a number of governments around the world are not particularly concerned about the size of deficits at the present conjunction. The benefits of keeping business operating and workers employed currently outweigh concerns about the effects of future public debt servicing. Egyptian Trade Minister Rachid Mohamed Rachid was echoing a common sentiment when he said, "Everyone is willing to sacrifice an increase in the budget deficit to stimulate growth."³¹

Tax cuts today will require additional taxation in the future, which, however, will be resisted by taxpayers and businesses. Policymakers need to decide judiciously how much cutting is feasible and to what extent debt accumulation will inhibit future growth prospects and future social spending.

Changes in taxation will affect formal sector businesses but are likely to have only limited direct effects on the fortunes of informal enterprises. The latter tend to fall outside of the tax net and their owners' income may also not be taxed. Informal operators may benefit indirectly, however, if purchasing supplies from formal firms which normally do pay tax.

In late 2008 and early 2009, governments in many countries cut taxes in a variety of ways. Some countries chose to cut corporate income tax that affected all sizes of incorporated firms. For example, Singapore cut the corporate tax

²⁹ Many countries already provide lower tax rates for small businesses or for those with a low level of profit.

³⁰ 'Government to maintain income tax cuts as economic stimulus,' Antara news agency, 7.02.09, Embassy of Indonesia, Oslo

³¹ 'Rachid details trade ministry's stimulus package,' *Daily News Egypt*, 11.12.08

rate by one percent for all firms. Korea went much further, cutting the rate for small firms by three percent over two years and by five per cent for larger firms over the same period in 2009 and 2010.

Value-added taxes are an important target of cuts. In India, the central value-added tax was reduced a full 4% on all products, except for oil. Similarly in China, the value-added tax for small businesses was cut to a uniform 3% from the existing 4-6%. The government there is speeding up the process of moving away from the use of excise taxes (on production) to value-added taxes. Recent changes are estimated to reduce total taxes paid by companies by US\$17.6 billion annually.

Many countries have found ways to promote exports by cutting the tax related to export production or by rebating duties on imports used in exports (duty drawbacks). Specific sectors that have been hit hard by the crisis, such as textiles and garments, have received specific attention from governments. For example, China increased the tax rebate for textile and garment exporters four times between August 2008 and February 2009. The most recent increase, of one percent, raised the rebate to 15%.



Taxation policy options

- Reduce the corporate tax rate
- Reduce the tax rate for sole proprietorships and partnerships
- Link tax rate reduction to employee retention
- Reduce excise tax
- Reduce value-added taxes
- Allow multi-year income/loss smoothing
- Increase duty drawback rates (rebate on duty for imports used in exports)
- Bring forward property assessments (newer assessments will be lower, thus lowering property tax payable)

Some countries have tax schemes that allow profit and loss to be smoothed over several years and are extending such provisions to reduce tax payments in 2009. Singapore has a unique scheme in which it is moving forward on property assessments because with lower property prices, assessments will be lower and will result in a lower tax burden on households and businesses.

Countries which recently made tax cuts (i.e. before the crisis) have found it difficult to do so again due to its impact on revenues. South Africa made changes in 2008 such that in early 2009 the government resisted calls for further cuts. Indonesia moved from progressive taxes to a flatter regime in 2008. While the changes decrease revenues, the government resisted calls to halt the cuts in 2009. It sees the cuts as part of its stimulus efforts.

Micro and small businesses that do pay taxes need to be aware of the changes and may need assistance to understand how they apply. In this regard, business associations, including sectoral ones, can play a role in explaining tax changes to their members. Enterprise promotion agencies may provide similar assistance. Business associations have also a critical role to play in advising governments on the hardships of their members and on where tax cuts can be most effective in stimulating output, exports and employment.

Tax relief during the crisis - examples

- Korea: Tax rate from smaller businesses reduced by 2% to 11% in 2009 and a further 1% the following year; the rate for larger businesses reduced 3% to 22% and then further to 20%.
- Egypt: As part of its stimulus package, government proposed tax rebates for loss-making small businesses.
- Indonesia: Due to the crisis, government resists calls that it not proceed with historical corporate tax cuts program (to a flat 28%) for 2009 that were announced a year earlier.
- China: The value-added tax for small businesses and the self-employed reduced to a universal 3% from either 4% for commercial enterprises or 6% for industrial ones.
- Mauritius: To protect domestic business, the government froze for two years its plan to lower import duties.
- India: Central government value-added tax was reduced by 4% on all goods except oil or where the tax is already below 4%; the cut affects enterprises of all sizes.
- Singapore: Corporate tax rate reduced by one per cent to 17%; this measure, combined with existing Partial Tax Exemption Scheme in which a company pays no tax on 75% of its first S\$10,000 and no tax on 50% of its next S\$290,000, provides a low tax regime for MSMEs.
- Brazil: To boost demand, taxes on cars, personal income and industrial earnings lowered; cars with an engine size of less than 1 litre now have no tax.
- France: Complete corporate tax exemption on investments made between now and early 2010.
- Canada: The amount of small business income eligible for the lower 11% tax rate has been increased to C\$500,000 from C\$400,000. It is expected to reduce the total tax bill for small business by C\$45 million.

3.3 Employment

While layoffs reduce businesses costs, they put further downward pressure on consumption, thereby prolonging the downturn. Thus, efforts to maintain employment are of benefit both to the welfare of workers and to the prospects for economic recovery. Worker retention may also aid businesses if it allows them to avoid losing valuable human capital, although businesses are unlikely to retrench their best workers.

Firms are taking their measures to reduce labour costs. Many are implementing wage freezes or low wage rises. In the U.K., for example, a quarter of wage settlements in January 2009 resulted in a year-long wage freeze and more than half had lower settlement (often lower rises) compared with a year earlier.³² These measures also tend to dampen demand but if instituted in lieu of layoffs, they may provide a more acceptable alternative. This is especially true in countries where unemployment insurance and related welfare measures are weak or non-existent.



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³² 'More firms freeze annual pay rises', Virgin Media, website, 20.02.09. The article is based on figures of the Industrial Relations Services.

Employment options

Business strategies

- Shift workers to required training
- Move workers to units, plants or offices where demand is stronger
- Negotiate a reduction in length of the work week (to avoid layoffs)
- Temporary work stoppage
- Negotiate wage freeze or low wage rise

Government support

- Use unemployment insurance benefits to cover work-time reductions
- Subsidize new hiring or retention
- Extend unemployment insurance benefits period
- Subsidize training
- Subsidize non-wage labour costs (payroll deductions)

To avoid permanent retrenchment, many firms have instituted work-time reductions, either in the form of a shorter work week or a temporary plant shut-down. Such measures ease pressure on the payroll while still allowing workers to bring home a paycheck. Temporary shutdowns have been common in the past at North American automobile companies and other manufacturers when inventories build up. Bipartite and tripartite dialogue can play an important role in shaping socially acceptable employment solutions during the downturn.

Workers affected by time reductions or temporary layoffs can often avail of unemployment insurance in countries where such schemes exist. Governments have been innovative in adapting their schemes. In Canada, for example, an employee whose workweek has been cut to four days can receive unemployment insurance benefits for the fifth day.

In other countries, unemployment insurance funds are not only being used to provide passive assistance. In China, for example, funds are being used to train unemployed and migrant workers. As explained by Mr. Zheng, Vice-Minister of Human Resources and Social Security, "The unemployment insurance fund has topped 100 billion yuan [\$14.5 billion], and it's high time it is used."³³

Subsidies to retain workers or hire new ones are provided in some countries including Singapore, Japan and the UK (see 'Employment schemes'). The Singaporean government is providing a cash grant equal to 12% of the first S\$2,500 in wages for each regular worker retained during the slowdown.



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³³ 'Economic crisis and policy responses in China', ILO-Beijing, undated

Employment schemes

- Slovakia: Subsidies for new jobs and reduction of employment taxes for employers that might otherwise retrench workers.
- Brazil: Duration of unemployment insurance benefits has been extended by two months.
- China: Vocational training program for unemployed and migrant workers funded from unemployment insurance and related funds.
- Japan: \$16 billion package to: expand training for unemployed; provide benefits to laid-off workers not covered by unemployment insurance; subsidize companies to retain workers; and, expand job creation schemes.³⁴
- Singapore: Under a new Jobs Credit scheme, employers of all sizes receive a cash grant for each regular employee.
- Korea: \$3.5 billion to create half a million temporary jobs, expand training schemes and fund unemployment insurance.
- UK: Companies will receive £2,500 for hiring workers who have been unemployed for more than six months.

3.4 Self-employment

Some countries have realized the important role that business start-ups can play in easing the impact of the slowdown. New businesses can be started by locally retrenched workers, by migrants moving from urban to rural areas and by migrants returning from abroad. New businesses have a high potential to fail, however, and therefore require planning and supportive measures to increase their chances of success. Ideas for new businesses should be grounded in the realities of market demands that either exist or can be developed in the rural or urban environments where they are established. Local economic development (LED) approaches, in which local communities come together to assess and determine

³⁴ 'Japan and S. Korea seek to ease jobs pain,' FT.com, 19.03.09. The package was being proposed at the time of writing.

local market potential, can be facilitative in this regard. Pinpointing the market potential can then be supplemented with training on how to start and manage a business, with skills training and with access to credit. The ILO has a number of programs on local economic development, skills training (CBT-TREE)³⁵ and enterprise management (Start and Improve Your Business) that can be helpful in this area.

In the Philippines, the government has established Help Desks in provinces to guide returning migrants to new jobs and also advise them on self-employment. A total of 250 million pesos from the Overseas Workers' Welfare Fund has been allocated for livelihood support for returning migrants.³⁶ In China, governments are supporting the return of retrenched workers from cities and industrial zones to rural areas and helping them to start businesses with credit and other supports. In Canada, the government's stimulus package provides C\$10 million to the Canadian Youth Business Foundation which mentors new entrepreneurs.



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³⁵ 'The effect of the global economic crisis on Asian migrant workers and governments' responses', Technical Note (M. Abella and G. Ducanes), ILO, Manila, February 2009

³⁶ 'The effect of the global economic crisis on Asian migrant workers and governments' responses', Technical Note (M. Abella and G. Ducanes), ILO, Manila, February 2009



4. ILO's Five Point Crisis Response for MSMEs

The ILO has developed a Five Point Crisis Response to help existing MSMEs weather the crisis and to support unemployed workers, including migrants, in creating self-employment. The five points, detailed below, focuses on assessing environments and on providing advice, examples and training to policymakers, businesses and business associations. The ILO stands ready to offer this assistance through its network of Enterprise Specialists at ILO offices around the world and through the network it has developed of SME experts who deliver its well-known package of enterprise training, the Start and Improve Your Business (SIYB) suite of programs.

P1: Rapid assessments of the enterprise environment

The impact and severity of the crisis have caught employers, workers and policymakers by surprise. As such, a rapid assessment of the impacts and how they are making enterprises vulnerable is an important first step in designing appropriate responses. The crisis has had a general impact on all economies around the world, but there are sectoral and geographical (region, country, within-country) differences. The crisis has also hit economies and enterprises at different times and some will exit from the crisis more rapidly and in better condition than others. A rapid assessment will pinpoint problem areas.

P2: Advice through examples for policymakers on access to finance

Access to finance is a key constraint for MSMEs during the crisis. The ILO has produced this guide, which in Section 2 focuses considerable attention on the credit issue and provides a range of examples drawn from countries in various parts of the world. These examples offer ideas for policymakers and social partners in other countries on how to take a proactive approach to unblocking the financing constraint. Each country will need to work out its own approach based on its own set of banking institutions (including development banks and small enterprise banks) and credit programs, and on its resources, expertise and regulatory environment.

ILO's Five-Point Crisis Response for MSMEs

1. Rapid assessment of factors that make enterprises vulnerable
2. Advice through examples for policymakers on enterprise financing strategies
3. Advice on public procurement programs
4. Advice and training on business development services
5. Advice and training on strengthening small business associations

P3: Advice to policymakers on public procurement

The ILO promotes an approach to public procurement that seeks to both remove the constraints faced by MSMEs in gaining access to government contracts and by actively promoting these enterprises because of their high labour intensity. Many governments have responded to the crisis with demand stimulus measures that involve spending on public works. With adequate access, MSMEs in relevant sectors, notably road and building construction, can compensate for the decline in demand from private clients with increased servicing of public sector customers. Other micro or small businesses, which are not or have not been able to secure public contracts, may benefit by supplying or sub-contracting with other enterprises that have. The ILO has a training program on public procurement by MSMEs that can be used to provide advice and ideas to policymakers.

P4: Advice and training on business development services

Small enterprises need to cope with reduced demand in their traditional markets and develop products and services for new markets and new opportunities arising during the crisis. For this they need help to 'think outside of the box' and take initiatives to ensure that instead of being 'entrepreneurs in crisis', they are 'entrepreneurial in the midst of the crisis'.



Entrepreneurship is a complex issue involving personal attributes, a supporting culture and an enabling policy environment. It can be assisted through training on how to start and manage a business. For many years the ILO has promoted entrepreneurs through its Start and Improve Your

Business (SIYB) suite of course, which also includes Generate Your Business Idea and Expand Your Business. These programs have been used for emergency situations, notably in Indonesia and Sri Lanka for tsunami survivors and in China, where the Emergency-SYB program was successful in assisting those whose lives were disrupted by the Sichuan earthquake of 2008.

The ILO has developed a network of 7,000 trainers and 277 licensed master trainers for the SIYB suite in over 500 partner organizations worldwide. Through ten sub-regional workshops, the ILO is mobilizing and reinvigorating this network for ready deployment during the crisis. It can provide training for entrepreneurs and would-be entrepreneurs on coping with reduced demand and seizing new opportunities.³⁷

³⁷ Few governments have included business development services in their stimulus packages. There are exceptions, however. In Mauritius, the government will help SMEs develop plans to qualify for financing. It is also accelerating the implementation of its Manufacturing Adjustment and SME Development Fund (MRs500 million) which supports standards upgrading, productivity improvement, marketing, export promotion and other aspects to expand markets. In Canada, the government's stimulus package provides C\$30 million to the Can-

P5: Advice and training to strengthen enterprise associations

Enterprise associations can be a valuable support mechanism for businesses during the downturn. They allow members to share ideas and knowledge, provide information on new policies and programs and advocate on behalf of their members vis-à-vis governments. The effectiveness of such organizations varies considerably, depending on the ability to attract members, the level of funding and the leadership and management. The Federation of Small Businesses in the U.K. and the Canadian Federation of Independent Business are two of the many effective organizations around the world. Unfortunately, there are also many small business associations which are less effective and thus the voice of small entrepreneurs it often inaudible. The ILO is ready to strengthen these associations through its training program for small business associations so that these associations can play a more active role during the downturn.



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ada Business Network, which provides a single window for accessing information and tools for business, mostly smaller ones.

5. Role of the social partners

The economic crisis has prompted the ILO's social partners to put forward suggestions on how their country can manage the crisis. In many cases, this involves advice to governments. There is some consensus of a need to moderate wage demands and to find ways to retain workers and to support those who are retrenched.

In a number of countries, the crisis has created social tensions that have boiled over into street protests. The government in Iceland resigned in January 2009 after months of protests, while in Ireland over 100,000 people protested the imposition of a pension levy on public sector workers during the recession. Protests have also occurred in France, Greece, Bulgaria, Lithuania, Latvia and elsewhere.

The tripartite parties have come together in several countries to seek agreement on how to manage through the crisis. For example, in Slovakia the government and the umbrella trade union, along with employers, agreed to limit salary increases to productivity increases.³⁸ In Mexico, employers' and workers' organizations have publicly supported the country's stimulus package. In addition, the Confederación de Trabajadores de México, which represents workers, has pledged not to engage in strikes or protests related to the current economic crisis.³⁹

Employers' organizations in many countries have added their voices to the debate about appropriate economic policies to help businesses weather the downturn. Small business associations and small business cells within larger organizations have an important role to play in keeping the concerns of MSMEs at the forefront of policymaking during the crisis.

³⁸ 'Slovak government, unions agree to cap wage hike demands,' Reuters 06.02.09

³⁹ 'Stimulus plan to curb impact of crisis', IPS News Agency, 18.03.09

Social dialogue initiatives

By employers' organizations

- engage in high-level dialogue with workers' organizations
- suggest crisis management strategies that are in tune with the interests of workers
- set long term goals that extend beyond the short-term stresses of the current crisis

By workers' organizations

- understand how the crisis is affecting business owners and managers
- defend decent work
- work with management to find ways to increase productivity in the current crisis



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Advocating for Indian garment exporters

Indian garment exports for 2008-09 are expected to be 9% lower than a year earlier. India is the world's fifth largest exporter of readymade garments. The sector comprises small and large producers and provides employment to 33 million workers directly and 55 million indirectly. The industry estimates that 700,000 workers lost their jobs in five months in late 2008.

The Apparel Export Promotion Council has asked for an increase in the duty drawback, which was lowered in September to between 8.8% and 10.5%. AEPC has asked for it to be raised to 14.65%.

AEPC also asked for a 5-year income tax holiday, interest-free loans on machinery investments, zero duty on machine imports and a lower fringe benefit tax. In its stimulus package of late 2008, the government provided a 2% interest subsidy on loans for exporters and a US\$290 million allocation to the sector's technology upgrading fund.

Press release, AEPC, 07.12.08



6. Conclusion: Securing recovery and beyond

Many analysts expect the first signs of economic recovery to appear in 2009 with a more robust upturn in the following year. Certain countries and sectors may recover more quickly than others. In the interim, many jobs and enterprises will be at risk. As the examples in this booklet have shown, governments have demonstrated a commitment to supporting small enterprises and the employment they provide.

We should not, however, view the current situation as merely a crisis to be survived. It also presents opportunities, on three fronts. One, the recent efforts to support MSMEs may provide an opportunity for policy experiments. Reduced regulation for start-ups, better access to finance and improved methods for monitoring and sustaining decent work can be developed during the crisis and continued when growth revives. We may recall that important aspects of Western social security systems were initiated during the last great crisis: the depression of the 1930s.

Two, even in a downturn, true entrepreneurs will arise, finding profitable opportunities to fulfill consumer wants either by innovating new products and services or by devising ways to produce existing products or deliver existing services more cheaply. And three, demand stimulus packages present important opportunities for small businesses to build infrastructure and supply goods and services to governments.

Carpe diem [seize the day] - even when it's gloomy!

Sustainable Enterprise Programme

What began as a crisis in finance markets has rapidly become a global jobs crisis. Unemployment is rising. The number of working poor is increasing. Businesses are going under. Concern is growing over the balance, fairness and sustainability of the sort of globalization we have had in the run up to the financial crash. The International Labour Organization, representing actors of the real economy, that is governments, working together with representatives of employers and workers organizations, is playing its role within the UN and multilateral system to support its constituents as they seek to weather the crisis, prepare for recovery and shape a new fair globalization. The Decent Work Agenda provides the policy framework to confront the crisis. In this series of brief publications, the ILO's Sustainable Enterprise Programme reflects on impacts of the global economic crisis on enterprises and cooperatives, provides examples of policy and enterprise-level responses, and indicates how constituents can be supported by the ILO.