

## Small and Medium Enterprises Development in Bangladesh: Problems and Prospects

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### Abstract

*Small and medium sized enterprises (SMEs) are playing increasingly important role as engines of economic growth in many countries including ours. SMEs provide low cost employment opportunities and render flexibility to the economy. Many of the SMEs are engaged in export activities suggesting that they are internationally competitive. Considering the importance of SME sector in the economy of Bangladesh and understanding the constraints under which such enterprises operate, it is evident that policies to support the development and growth of SMEs are necessary. In the policy strategies, smooth and sustainable development of SMEs all over the country will be considered as one of the vehicles for poverty alleviation, and generation of more employment. An attempt has been made in this paper to identify major financing constraints faced by SMEs in Bangladesh and suggest some policy measures to overcome those constraints.*

**Key words:** SME, development, income, employment generation, poverty reduction, financing constraints, prospects for SMEs.

### Introduction

Small and Medium sized Enterprises (SMEs) have drawn a lot of interest among policy makers, academics, businessmen and people in general. There is a broad consensus that a vibrant SME sector is one of the principal driving forces in the development of the economy of Bangladesh. SMEs stimulate private ownership and entrepreneurial skills and can adapt quickly to changing market situation, generate employment, help diversify economic activities, and make a significant contribution to exports and trade. Therefore, policies and initiatives to develop SMEs and to increase their competitiveness are a priority for Bangladesh. Liberalization of the economy along with rapid globalization has posed severe challenges to SMEs not only in international market but also in the domestic economy. Since SMEs are based on relatively small investment, their survival depends on readily available market with easy access. In this context, access to finance, market development and expansion as well as removal of other bottlenecks are a challenging task, which requires coordinated efforts by individual business enterprises and the government.

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### **Objectives of the study**

The present study focuses on the current scenario of SMEs and problems faced by them in Bangladesh as well as suggest some policy recommendations. The specific objectives of the study are to:

- i) Examine the role of SMEs in the economy of Bangladesh;
- ii) Analyze the current status of SMEs in Bangladesh;
- iii) Review the situation regarding their access to finance by SMEs;
- iv) Identify the major financing constraints to SMEs development in Bangladesh; and
- v) Put forward some specific recommendations for future growth of SMEs in Bangladesh.

### **Methodology of the Study**

The study is mainly based on secondary data. Data have been collected from different published materials like the publications of Bangladesh Bank, Bangladesh Bureau of Statistics, Ministry of Finance, World Bank and relevant writings of some scholars. The collected data have been processed manually and paper in the present form has been prepared in order to make the study more informative, analytical and useful for the users. Tabular and graphic representations are made in MS Word and MS Excel.

### **Role of SMEs in the Economy of Bangladesh**

In Bangladesh, SMEs including micro enterprises comprise over 99 per cent of all industrial units, contributing over 85 per cent of industrial employment. Focusing on the 10+ units, small units constitute 87.4 per cent, followed by medium and large units comprising 5.7 and 6.9 per cent respectively. In other words, 81 thousand SMEs all together constitute more than 93 per cent of the total 10+ units. Again, focusing on the 10+ units, small units contribute to 35 per cent of the employment, followed by medium and large units comprising 8.8 and 56.0 per cent respectively. In other words, SMEs employ 1.3 million people, constituting 44 percent of employment generated by 10+ units.

The recent available estimates obtained from two major micro surveys, International Consulting Group (ICG) study and South Asia Enterprise Development Facility (SEDF) survey suggest the SME contribution to manufacturing value added to be in the range of 20 to 25 percent (Ahmed 2008; Bahar and Uddin 2007). The micro, small and medium enterprises (MSMEs) together employ a total of 31 million people, equivalent to about 40 per cent of the population of Bangladesh, aged 15 years and above. More than three quarters of the household income in both urban and rural areas are provided by the MSMEs (Rahman 2007).

### **Current Status of SMEs in Bangladesh**

The National Report of BBS based on the nationwide census of all non-farm economic activities in 2001 and 2003 presents data by employment size and category.

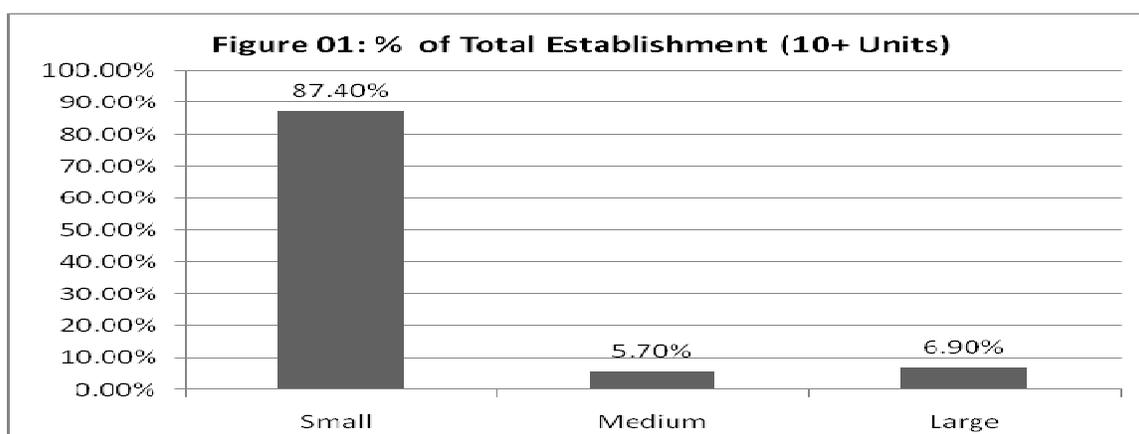
**Table 01: Sectoral and rural/urban distribution of establishment of micro, SME and large enterprises in Bangladesh-2001-2003**

	Micro < 10	Small 10 – 49	Medium 50 – 99	SME 10-99	Large 100+	Total 10 +	All
No. of Establishment (000)	3620	76	5	81	6	87	3708
% of total units	97.6	2.0	0.13	2.18	0.16	2.35	100.0
% of 10+ units	-	87.4	5.7	93.1	6.9	100.0	-
<b>Sectoral composition (% of total)</b>							
Manufacturing	12.6	34.8	45.1	35.5	66.4	37.5	13.2
Trades and Service	87.4	65.2	54.9	64.5	33.6	62.5	86.8
All	100	100	100	100	100	100	100
<b>Rural-urban distribution (% of total)</b>							
Urban	35.5	60.1	73.6	60.9	83.1	62.4	36.1
Rural	64.5	39.9	26.4	39.1	16.9	37.6	63.9
All	100	100	100	100	100	100	100

Source: Compiled from Economic Census 2001 & 2003, National Report, BBS, July 2005.

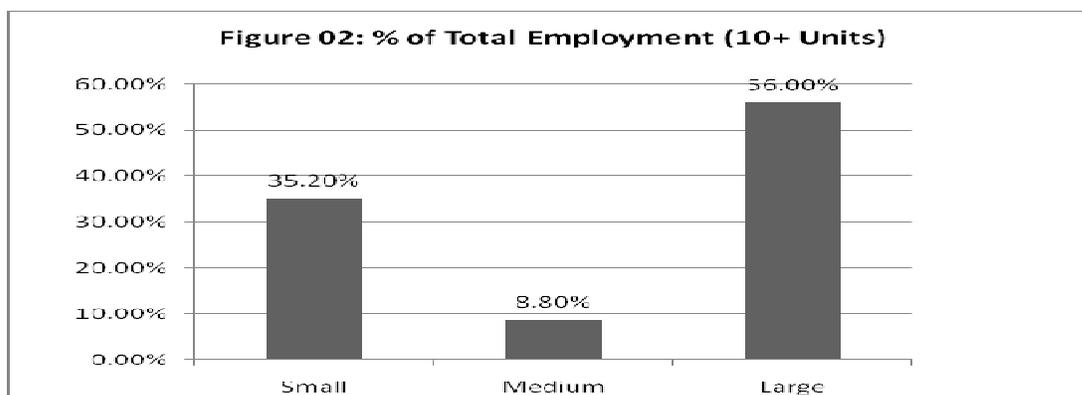
### Number of establishments by category

An overwhelming majority—98 per cent of establishments—are micro units having less than 10 workers. Only 13 per cent are in manufacturing and the remaining 87 per cent are involved in trade and services (Table 1).



### Employment

Nearly 11.3 million jobs are generated by non-farm establishments in Bangladesh, of which 73 per cent are created by micro enterprises. Focusing on the 10+ units, small units constitute 35.2 per cent of the employment, followed by medium and large units comprising 8.8 and 56.0 per cent respectively. In other words, SMEs employ 1.3 million people, constituting 44 per cent of the total 10+ units employment.



### *Size and structure of manufacturing SMEs (10-99 workers)*

As regards manufacturing SMEs (10-99 workers), the Economic Census 2001 & 2003 indicate that there are nearly 28 thousand small and medium manufacturing establishments employing some 644 thousand persons. In the 10+ size group, manufacturing SMEs account for nearly 88% of the manufacturing establishments while this is about 29% of manufacturing employment.

### *Rural-urban distribution*

Small manufacturing enterprises are almost evenly distributed between rural and urban areas both in terms of number of establishments (52% and 48% respectively), and employment (51% and 49% respectively). In the case of medium manufacturing enterprises, there is a higher incidence of both urban establishments and urban employment (57% for both counts). Rural location for medium units constitutes 43 per cent in terms of both establishments and employment.

**Table 02: Location of industries by division, 2001 & 03**

Division	% Total						Total	
	Micro (1-9)		SMEs (10-99)		Large (100+)		Number	Empl.
	Number	Empl.	Number	Empl.	Number	Empl.		
Barisal	5.6	5.1	4.0	3.9	1.9	1.2	5.5	4.6
Chittagong	18.0	18.6	12.5	13.3	16.2	17.6	18.1	17.9
Dhaka	31.2	32.3	46.3	46.5	62.2	64.9	32.2	38.3
Khulna	15.1	12.9	8.3	8.7	7.7	6.9	14.7	11.7
Rajshahi	25.1	25.7	26.1	25.0	9.8	6.9	24.4	22.8
Sylhet	5.1	5.5	2.7	2.7	2.3	2.5	5.0	4.7
Bangladesh	100.0	100.00	100.00	100.00	100.0	100.0	100.0	100.0
Number	3620461	8272858	81573	1317088	6118	1680478	3708152	11270422

Source: Economic Census (2001 & 2003), BBS

### **Geographical location of non-farm enterprises**

The highest concentration of SMEs in terms of both number (46.3%) and employment (46.5%) can be observed for Dhaka Division, followed by Rajshahi: 25-26%, Chittagong: 12- 13%, Khulna: 8.3-8.7%, Barisal: 3.9-4.0% and Sylhet Division: 2.7-2.7%. Thus, Dhaka has the top position in terms of industrial location for all enterprise sizes. This is due to obvious reasons such as availability of infrastructural and other facilities. Instead of Chittagong, Rajshahi ranks next to Dhaka in terms of the choice of the SME location. This is, perhaps, not surprisingly, due to the existence of, among other factors, the Jamuna bridge, and different types of fiscal and financial incentives provided for the development of export oriented SMEs, especially in the Northern regions of Bangladesh (Ahmed 2008). In terms of the location of large enterprises, however, Chittagong seems to have been preferred to Rajshahi by the entrepreneurs.

### **Women Entrepreneurs in Bangladesh**

The concept of women entrepreneurship is still not well accepted in society, particularly in family circles. Business is considered a man's job. The Economic Census, 2001-2003 data reveals that women own only 2.83% of all enterprises. Rural women are involved in cattle and poultry rearing, rice husking, spice making, imitation ornament trading, pickle making and other micro businesses. Urban women are mostly involved in block printing and boutiques, bakery and fast food, doll making, tailoring, fabrics paint, interior decoration, etc. They are also owners of beauty parlors, computer training centers, leather goods, fish culture etc, which are non-traditional activities for women. Women entrepreneurs prefer to start their business in sectors where female employment is concentrated. The choice of the sector is limited by various factors such as resource constraint, female aversion to risk-taking, etc., which forces them to engage in activities with low entry barriers and low financial risks such as food processing and or clothing and textile sector. Hence female businesses have smaller employment and sales than male business. Majority are micro and small enterprises, employing less than 10 persons. Most of them are sole proprietors. Participation of women as entrepreneurs has also improved their quality of life and their households. They serve as a role model for young generation for self-employment opportunities.

Women enterprises are small in size. Short-term loans were more widely used than medium term loans, which had an average size of Tk 3 lakh. The average interest rate was 13%, ranging from 10% to 14 %. Loan giving process discriminates against women. The average time required for an SME to process loan was 57 days, while for women enterprises it took 145 days. Debt financing has yet to deeply penetrate women-led enterprises (Bangladesh Bureau of Statistics, 2007).

### **Access to Finance by SMEs: A Review**

It has been realized by and large that lack of access to finance is a key impediment to SME development in Bangladesh. This is more so in the case of women entrepreneurship development.

In this context it is appropriate to make a review of the available institutional support for SMEs and the problems faced by women entrepreneurs.

Studies on SMEs have revealed that while SME loans are largely meant for meeting the needs of working capital, such loans meet around a third of the demand. The rest is met from own source, and partly by bank loans under other heads, friends/relatives and NGO sources.

### Status of institutional financing for SMEs

The government is continuously taking policies to address the problem of SME finance through extending institutional financial support. There are several sources of institutional financing. From the formal sector, the flow of credit to SMEs comes from state-owned commercial banks (SOBs), specialized banks (SCBs), non-bank financial institutions (NBFIs), domestic private commercial banks (PCBs), foreign commercial banks (FCBs) and some government and non government organizations. A break-up of SME loan disbursed by these institutions is shown below:

**Table 03: Institutional financing of SMEs, 2003-2008**

Institutions	Details	Outstanding SME Loan (Crore Taka)	
		2003	2008
SOBs	Sonali Bank, Janata Bank, grani Bank, and Rupali Bank	127 (0.34)	15010 (29.91)
PCBs	Almost all private banks	193 (0.48)	23254 (18.11)
NBFIs	21 NBFIs; MIDAS has the highest SME credit disbursements	112	1340 (12.64)
FCBs	Standard Chartered Bank, HSBC Bank	0.0	764 (5.06)
SCBs	BASIC Bank, Karmasangsthan Bank, Banfghanistan Krishi Bank, Rajshahi Krishi Unnayan Bank, Ansar-VDP Development Bank	Not Available	3071 (20.94)
Government Organizations (GOs)	ASA, BRAC etc.	Not Available	Not Available
NGOs		Not Available	Not Available

*Note: Figures in parentheses represents percentage of SME loan to total loan; Source: Bangladesh Bank*

SME credit disbursement by financial institutions grew rapidly over the period 2003-2008. The situation accelerated in 2008-09. Total SME loans increased by Tk. 13441.85 crore (or 42.64 percent) to Tk. 44969.5 crore at the end of March, 2009, which was Tk. 31527.65 crore at the end of March, 2008. The loans increased in private banks by 41.88 percent, state-owned banks by 62.03 percent, NBFIs by 8.11 percent and SCBs by 3.31 percent during March, 2008 to March, 2009. Despite this huge surge in SME loan disbursements during last five years by banks and

NBFIs, the credit flow to SMEs by the majority of banks taken together still is not very significant compared to total loans. There are several reasons for such small share of institutional loans. *First*, the large industries' requirement for capital is far greater than that of SMEs. *Secondly*, SMEs approach the financial institutions very seldom for financing and at the same time meager amounts of money are disbursed to the SMEs. *Thirdly*, formal financial institutions prefer to extend credit facilities to bigger firms or to those firms which are gradually expanding and have a viable business record. Finally, the collateral-based SME loan process is complicated, for which entrepreneurs often fail to get loan from banks.

### **Some special credit programs by GOs**

Various government organizations including specialized banks are engaged in providing credit to the SME sector. A specialized bank, the BASIC Bank Limited (Bangladesh Small Industries and Commerce Bank Limited) was established in 1988 with the foremost objective of financing the small and cottage industries (SCI). The Memorandum of Articles of BASIC contains that at least 50 percent of its loanable fund should be invested in small scale industries. The Bank also offers below market interest rates on SME lending compared to most other banks.

Taka 150 crore has been allocated in the budget FY2008 for the development of agro-based industries. This credit will be channeled through Bangladesh Krishi Bank, Rajshahi Krishi Unnayan Bank, BASIC Bank and Karmasangsthan Bank. Earlier, the Karmasangsthan Bank took up programs to give loans to unemployed youth for setting up small enterprises. In FY2003, the bank disbursed a total of Tk. 28 crore to 9486 borrowers and recovered Tk. 26 crore.

The Ansar VDP Unnayan bank used to provide loans to members of the Ansar and Village Defense Party for setting up small enterprises. The bank disbursed Tk. 82 crore in FY2003 and Tk. 67 crore in FY2002. The default loans accounted for 2.08 percent of total outstanding loans in FY2003.

Moreover, some other SME financing initiatives were taken by various government organizations, such as the Directorate of Youth Development, BARD, BRDB etc.

### **Credit schemes/projects for women entrepreneurs**

Despite the negative image of women as entrepreneurs, institutional assistance with local and international support resulted in projects and programs aimed at furthering women entrepreneurship. Some of these are mentioned below.

*Women Entrepreneurship Development Project (WEDP)*: WEDP was the only program in the industry sector which was directly related to women entrepreneurship development. This was initiated by BSCIC in 1982 with the support from USAID and was discontinued in 2004-05. It was the first program to support women with larger amount than micro credit without collateral. The highest ceiling of the loan was Tk. 60, 000. The activities were to provide pre-investment counseling, assisting in project appraisal and feasibility studies, extending credit facilities, imparting training and providing marketing and technical support.

*Entrepreneurship development for women by JMS:* The Jatio Mohila Sangstha (JMS) initiated a project in 1998 in 64 districts for five years with assistance from UNDP to support potential women to become entrepreneurs. The project supported those who were graduates of various micro-credit programs of various agencies like the Department of Women's Affairs, Department of Youth etc. The project also aims to link the beneficiaries with institutional source of credit. Although the credit limit was from Tk30000 to Tk. 150,000, the highest disbursement was Tk70,000. Before extending credit management training was imparted to the entrepreneurs.

*Mainstreaming SME credit* In the last quarter of 1980's, Bangladesh Bank circular directed the commercial banks to lend at least 15 percent of their lending capital for industrial sector. Five percent was supposed to be spent for the Small and cottage industries. But there were no guidelines for women entrepreneurs.

*Separate bank branches for women.* Some public sector banks have women banking branch but their role is to generate saving rather than encourage investment. Though not legally required, banks and credit programs insist on husbands' or other male relative's consent as guarantee before providing loans. Sonali Bank is a pioneer bank which opened a few women branches in the country to promote saving habit of women. It initiated a project named "Credit for Urban Women Micro Enterprise Development" which offered loan between Tk 50 thousand to two lakh without collateral. To be eligible for loan, viability of the project, hypothecation and a personal guarantee were the necessary requirements. The formalities were considered to be difficult for women and the amount was too small to establish a small enterprise. Janata Bank has good facilities in providing collateral free loans up to Tk 5 lakh, but these are available only in Dhaka.

## **Government Support to Financing Schemes**

### ***SME Cell and SME Foundation***

Considering the importance of small enterprise financing, a SME cell has been created in 2003 in the Ministry of Industries (MoI). The cell has announced that 80 percent of total resources available for SME would be allocated specially for small enterprises. The SME cell also decided that BASIC and BRAC bank will be working together as lead banks and will be responsible for distribution of credit and venture capital fund in the short run.

The SME Foundation (SMEF) is an independent organization established in 2007 with a view to making it an Apex body for looking after the SME sector. The SMEF is capitalized by the Government of Bangladesh with a total endowment of Tk.2 billion. In order to facilitate low cost credit to SMEs, the SME Foundation started credit wholesaling program of Tk. 2.00 crore and it is being implemented by MIDAS Financing Ltd. and Shakti Foundation on a pilot basis. The Foundation developed guidelines for conducting its credit wholesaling program so that SMEs can receive credit at a single digit interest rate under Program through partner organizations. The SME Foundation expects that the SME credit wholesaling guidelines would enable it to reserve

refinancing funds and give it to banks and financial institutions at rates lower than that of the Bangladesh Bank.

The Women Entrepreneurship Development Wing of SMEF seeks to promote the creation of favorable environment for women entrepreneurs through capacity building and bring them in the mainstream of development process and facilitate effective support for these target groups as well as lend support to women's led trade bodies/associations for their building institutional capacity and competitiveness.

In a recent move, the government handed over a Tk. 210 crore ADB grant received in 2004 to the SME Foundation. Under this program, banks and non-bank financial institutions will get funds from SMEF at 3-4% interest, while the entrepreneurs will be entitled to loans at 8-9%, in lieu of the present 13-16%.

### **BASIC**

Various government organizations including specialized banks are engaged in providing credit to the SME sector. A specialized bank, the BASIC Bank Limited (Bangladesh Small Industries and Commerce Bank Limited) was established in 1988 with the foremost objective of financing the small and cottage industries (SCI). It functions through 17 selected NGOs due to the high cost of operations. BASIC is mandated to provide 50 percent of loanable fund to small and medium industries and to follow strategies of Industrial Policy 2005. The bank also offers lower interest rates on SME lending compared to most other banks.

The following funds are now in operation in Bangladesh governed by different entities like Bangladesh Bank, SME Foundation & Ministry of Finance (Banking & Financial Institutions Division):

#### **i) Bangladesh Bank Fund:**

- a) Total fund Tk.600.00 crore (Revolving).
- b) 17 Banks & 23 Non-bank Financial Institutions have signed Participation Agreement.
- c) Tk. 853.15 crore is refinanced up to 31.12.2009 to 17 Banks and 21 Nonbank Financial Institutions signed the agreement.
- d) Total number of Enterprises:- 8317.

#### **ii) EGBMP/IDA Fund:**

- a) Total fund Tk. 116.00 crore (Revolving).
- b) 18 Banks & 23 Non-bank Financial Institutions have signed Participation Agreement.
- c) Tk. 244.14 crore is refinanced up to 31.12.2009 to 14 Banks and 14 Nonbank
- d) Total number of Enterprises:- 2541.

#### **iii) ADB Fund:**

- a) Total fund Tk.202.00 crore (Revolving).
- b) 13 Banks & 15 Non-bank Financial Institutions have signed Participation Agreement.
- c) Tk. 334.94 crore is refinanced to 9 Banks and 7 Non- bank Financial Institutions. Institutions up to 31.12.2009.
- d) Total number of Enterprises: - 3264.

### Refinancing Scheme of Bangladesh Bank

To overcome the financial constraints of the SME sector and induce banks and Financial Institutions to provide credit facilities to SME, Bangladesh Bank introduced a refinancing scheme for SMEs in 2004 using three sources of funds: Tk.100 million of Bangladesh Bank's own fund, US \$20 million from IDA under the Enterprise Growth and Bank Modernization Project; and US \$30 million from ADB. Later the Bangladesh Bank owned fund was raised to Tk 500 crore. All schedule banks and financial institutions can avail of this facility at the Bank rate subject to fulfilling the stipulated conditions against their financing of SMEs. Under the Bangladesh Bank's refinancing scheme for the small enterprise sector, any industry/business entity having a maximum total fixed investment up to Tk 10 million has been considered as a small enterprise. The fund was to provide enhanced access to credit by SMEs, especially small enterprises. Disbursements made by financial institutions and leasing companies into small-enterprises were refinanced from the proceeds of the SEF. ADB provided loan from its special funds resources with a term of 32 years, including a grace period of 8 years, with an interest rate of 1 percent per annum during the grace period and 1.5 percent per annum thereafter. The loan period was for 5 years, expected to end on June 30, 2010. The loan agreement between the Government of Bangladesh and the Asian Development Bank had an explicit gender dimension. At least 10 percent of the funds of the SEF would be earmarked for women borrowers and women borrowers will be provided with assistance and advisory services for their loan applications.

Bangladesh Bank has reserved 10 per cent of its SME sector refinancing fund for women entrepreneurs at a maximum annual interest rate of 10 percent in an attempt to enhance more female participation in trade, commerce and productive sectors.

The central bank has mobilized a fund of about Tk 3.4 billion (US\$49.28 million) contributed by the government and development partners as refinance facilities for the commercial banks to lend small and medium enterprises (SMEs).

In spite of allowing refinance facility by BB, the banks and FIs have extended only about 20.6 percent of their total loans and advances to the SME sector. The contribution of SME loans in total loans is the highest in case of NCBs (33.3%) followed by SCBs (20.9%), PCBs (17.9%), non-bank FIs (13.7%) and FCBs (8.1%). It is observed that among the participating banks, BASIC Bank, BRAC Bank and Exim Bank disbursed a lion's share of their total loans and advances to the SME Sector.

**Table 04: Share of SME Loans in Total Loans by Banks and FIs**

Types of Banks	Amount of Loans/Advances (Million Taka)		
	Total	SME Sector	%
NCBs	495016	164982	33.3
PCBs	1387764	248773	17.9
FCBs	150741	12193	8.1
SCBs	153777	32153	20.9
All Banks	2187298	458101	20.9
Non-banks/FIs	123357	16851	13.7
All	2310654	474952	20.6

*Note: Data as of 30 June 2009; Source: Agricultural Credit and Special Programs Department, Bangladesh Bank*

*Extending microfinance operations into SME finance and cluster finance* The successful intervention of micro credit program in the last two decades has helped entrepreneurs particularly women entrepreneurs to receive loans beyond the narrow limits of microfinance, as some NGO-MFIs have started lending to this segment with loans ranging from Tk. 25,000-Tk,500,000. PKSF has extended collateral free financing of loan of Tk. 30,000 to Tk. 300,000. Among them about 90 percent of the borrowers were women entrepreneurs. Cluster finance by regions has also been observed, such as poultry finance to entrepreneurs in Savar, Gazipur and Bogra, livestock finance in Noagaon, Rangpur, and finance for weaving in Tangail, Gaibandha, Narayanganj etc (Mahmud 2007). The advantage of micro finance institutions is that it is committed to that particular segment, the staffs are trained up, they are used to dealing with borrowers who do not have financial information and records. Hence, these institutions addressed the new entrepreneurs who had been in business for two years.

*Down scaling financial institutions.* Consequent upon the issuance of Prudential Guidelines for Small Enterprise Financing of Bangladesh Bank in 2004, there has been a development in the formal financial institutions in introducing small and medium business finance windows in commercial banks. They addressed longer-term maturity, but have failed to address the need of a gestation period before a project can generate cash flow. Of these, BRAC Bank's devotion to SME banking is noteworthy. The financial institutions have also come up with innovative financial products for SME finance like "Prothoma Rin" by BRAC, "Mukti" by Eastern Bank Ltd., "Bhagyoboti" of Mutual Trust Bank, "Aparajita" of AB Bank, and "Nakshi" of City Bank which is operated by women entrepreneur. The product offers terminating loan facilities for the purpose of working capital finance and/or fixed assets purchase. BRAC Bank has a total of 80 female *Relationship Managers*, of which about 50 *Relationship Managers* are located in Dhaka, and the rest in Chittagong. They also started to target SME women entrepreneurs in Cox Bazaar, Narayanganj, Savar and Comilla. Other commercial banks have also opened SME financing.

### **Fiscal and Financial Incentive Support for SMEs by Government**

Besides institutional and policy support for finance, the government also offers a number of fiscal and financial support to the industrial sector including SMEs. The government has lowered duty on import machinery. Businesses exporting 80% or more of goods or services qualify for duty free import of machinery and spares. Value Added Tax (VAT) is not payable on import of capital machinery and spares. Facility of 90% loans against letters of credit is allowed. The government also decided in 2009 that small and medium manufacturing units would get a complete VAT exemption on utilities including electricity and phone, and insurance services.

### **Financing and other related constraints to SME Development in Bangladesh**

SMEs are heterogeneous by their characteristics, mode of operation and types of SME products and processes. As such it is difficult to make sweeping generalization about constraints facing SME entrepreneurs. However, some of the constraints are discussed below:

### **Lack of Investment Finance and Working Capital Finance**

It goes without saying that access to finance particularly working capital finance and investment finance to enable them to expand their business is a prime constraint facing the SMEs. Banks in general do not consider SME financing as profitable activity. SMEs are also regarded as high risk borrowers because of their low capitalization, insufficient assets and high mortality rates, and consequently banks are not keen to offer them credit at comparable interest rates. SMEs in the export sector also face problems of access to working capital.

### **Enabling environment for Trade and Business**

Although trade and business activities are carried out by the private sector independent of government control, existence of enabling environment like supportive regulatory framework, congenial tax regime, developed transport and communications infrastructure is vital for SME development. Bangladesh has made some progress in this direction but it still falls short of present day needs.

Other constraints of a general nature are inefficient infrastructure support especially power, widespread tariff anomalies, low productivity of labor, low level of technology, lack of research and development and low level of education of SME entrepreneurs in general.

### **Non-Tariff Barriers (NTB) and Changes in World Trade Regimes**

Liberalization of industrial and trade regimes in the wake of globalization are likely to have significant effects on Bangladesh's SMEs. Over the past decade there has been a significant change in the world trade regime with new regulations coming into effect. WTO agreements such as Application of Sanitary and Phytosanitary Measures (WTO SPS Agreement) to trade in agriculture products puts NTB restrictions on trade. WTO agreements not only cover the traditional goods sector, but also new sectors like services. Lack of knowledge about the current status of WTO Agreements hampers trade and business. Long-run economic prosperity will critically hinge upon turning the challenges of globalization into opportunities.

### **Barriers in access to finance for women entrepreneurs**

Discrimination still exists regarding access to finance by women entrepreneurs. Studies on the subject noted that women contribute around 26 per cent in total deposit of the banking system but their access to credit is below 2 per cent of the total outstanding loans. This is an unfortunate situation. Access to finance is one of the most critical constraints faced by women entrepreneurs. Although most of the banks have SME banking, few women apply for the bank loans as they need to submit a number of statements such as bank statement of the enterprise, reference of guarantor etc. for collateral free loans. Problems were more pronounced for women entrepreneurs in the informal sector. A recent study noted that about 79 percent of women entrepreneurs in this sector had no access to formal financial institutions and depended on own savings and family as source of capital to start a business (Chowdhury, Farzana, 2008).

Banking system is not adequately focused on women-owned enterprises. Banks usually consider women entrepreneurs in SME to be high-risk borrowers. The kind of collateral usually considered by banks as appropriate security is land and building. Women usually lack ownership of land and hence the collateral requirement of land and building is a constraint for them to access institutional finance. Lack of collateral makes women entrepreneurs more risky for banks. Although women have proved their repayment capacity with a repayment performance of 90 percent in the field of micro credit, commercial banks perceive them to be of high risk. Most of the small women entrepreneurs do not have a credit history, and so there is no CIB report on them. These barriers induce female entrepreneurs to take recourse to informal sources of finance, which has a negative impact on their growth potential.

### **Inability to Market SME Product**

The present and future growth prospect of any product depends to a large extent upon marketing activity. This requires having a well-planned marketing strategy including advertisement campaign as well as resources for implementing that strategy. Unfortunately, SME entrepreneurs are at the bitter end in this respect as they cannot make adequate investments in marketing and also lack necessary marketing skills.

### **Inability to Maintain Product Quality**

A major constraint to the sustainability of SME growth in Bangladesh is the inability to maintain the quality of SME products. At present Bangladesh produces mostly common consumer goods which are labor-intensive and require relatively simple technology. But due to poor quality these products cannot stand competition from imported products. The challenge for Bangladesh today is not in competing with high-tech products of developed countries but to make its SME sector survive competition from its rivals.

### **Lack of Skilled Technicians and Workers**

Lack of skilled manpower is a perennial problem in Bangladesh. This problem is particularly acute for small and medium scale export oriented enterprises. Bangladesh has made large inroads in the world's apparel market through commendable performance of RMG sector. However, the value addition of the products is low. Despite high demand, Bangladesh cannot make much entry into high value fashion wear exports due to dearth of trained workers. Supply capacity is thus constrained by non-availability of skilled workers.

### **Poor Management Skills of Entrepreneurs**

In the modern day economy, managerial skills for undertaking planning, marketing, and cash-flow management are vital for survival of an industry, small or large. SME entrepreneurs in Bangladesh are very much lacking in managerial skills and are not used to strategic planning. It is natural that they are unable to survive market failures. The concept of managerial training for SME entrepreneurs is yet to take root in Bangladesh.

## **Suggestions and Recommendations**

SMEs will continue to be the major driving force for income and employment generation in Bangladesh. The future for entrepreneurship appears to be very bright. We are living in the age of the entrepreneur, with entrepreneurship endorsed by government, business community, educational institutions, society, and corporations. Development of SMEs in Bangladesh is the need of the hour to raise the standard of living of the people of our country. The modest suggestions and recommendations are given below:

### **Enhancing Access to SME Finance**

Access to institutional finance for SMEs is still greatly limited. Less than 30% SMEs have access to institutional loans. Enhancing access to institutional finance by 50% of SME entrepreneurs may be a target within next five years through strengthening SME foundation, motivating institutional sources of financing to provide access to the deserving loan applicants.

### **Development of SME Infrastructure**

Infrastructure development is a prerequisite to efficient development and financing of SMEs. Currently, the most severe constraint that hinders the development of SMEs is the lack of infrastructure (e.g., roads, gas and electricity), limited access to market opportunities, technology, expertise and business information and communication. Providing appropriate infrastructure for SME growth should be given priority.

### **Quality of SME Products**

Poor quality of products is a big setback for expansion of SME business and SME sector as a whole. Measures for quality improvement and standardization of SME products have to be one of the targets. The BSTI may be made more effective in monitoring quality of product both for domestic market and for exports.

### **Training Facilities for SME workers and Entrepreneurship**

Bangladeshi workers are very good at learning production skills and copying them. However, training facilities for SME workers and development of entrepreneurial skills are not adequate in our country. Some training institutes like the Training Institute of BSCIC impart training but it is not utilized properly. Special programs are to be undertaken for the establishment of training institutes regarding entrepreneurship development.

### **Organizing Trade Fairs, Symposiums, Workshops on SMEs on Regular Basis**

At present workshops and symposiums on SMEs are held by different organizations and think tanks, but these are held infrequently and not in any systematic manner. A plan for holding seminars, workshops, trade fairs, etc. on a regular basis should be formulated.

### **Setting Help Desks in Banks and Business Promotion Bodies with Internet Facilities**

To extend the outreach of SME development particularly in respect of women entrepreneurs, a Help Desk with computer and internet facilities should be set up in bank branches dealing with SME finance as well as in all chambers of commerce and industry and other trade promotional bodies.

**Conclusion**

Development of entrepreneurship, new business creation and development of inter-sectoral linkages should be given top priority. The government should define a secure and pragmatic policy for the development of SMEs in the country. In order to frame a policy for SMEs, data collection needs to be updated. Provision should be made to develop separate and specialized institutions in three areas: (a) finance, (b) technology, and (c) skill development, in addition to rationalizing existing policies and institutions. The concept of public private partnership (PPP) in the sphere of development and growth of SMEs can also be explored. An enabling economic environment comprising of sound macroeconomic and structural policies, good infrastructure, fair policy of competition, and efficiently functioning financial institutions also need to be created and strengthened.

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