

# Problems and Prospects of SME Financing in Bangladesh

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## Abstract

To conduct a comprehensive study on the SME sector of Bangladesh of its present state, prospects, issues and emerging challenges this “problems & Prospects of SME Financing in Bangladesh” research is carried out. The **main objective** of the study is to find out the SME financing’s different types of strategies & policies in Bangladesh. The SMEs are playing gradually more significant role as a mainstream of economic escalation in Bangladesh as well as all over the world. The SME usually creates the opportunities of employment at lower costs and render flexibility to the economy. The SMEs are playing an indispensable role for overall economic development. Since this sector is a manual labor intensivewith the short period of time, usually it is capable of increasing the national income as well as hasty employmentcreation by achieving the Millennium Development Goals (MDGs) as well as the abolition of extreme poverty and starvation, gender equality and women empowerment. This SME sector has played a vital role intheeconomic progress of some prosperous countries of Asia. In national economy of Bangladesh SMEs play mainly vital role by making manufacturing enterprises by providing the employment of industrial workers and contributing to the over one-third of industrial value-added to gross domestic product (GDP) and become accustomed quickly to change the market condition, create employment, help diversify economic activities, and also make a significantcontribution to the exports and trade. The economic competence and the overall performance of the SMEs are considerably depended upon the policy of environmental and specific promotional policies pursued for their benefits. Consequently, the policies and initiatives to develop the condition of SMEs and toincrease their competitiveness are a main concern of Bangladesh.

**Keywords:** SME, Entrepreneurship, Business Entrepreneurship, Economy, GDP

## 1. Introduction

TheSmall and medium enterprises (SMEs) are playing increasingly important role as mechanisms of economic growth in many countries.The tectonic arrangements of the Bangladesh’s industries demonstrate several types of industries like the textile industries, the hand-operated welding, different types of food processing industries, leather, ceramics, electrics industries, essential metal and chemical engineering, paper and publication industries, small fabrication industry, battery industries, electrical devices, electronics, handicrafts, agro-based food industries, multilateral jute goods, silk industries, fruit processing, poultry farming, fisheries, tea gardening and processing, vegetable seed farming, and printing industries, construction industries, transportation, film and the photography, fast food, frozen food, the pathological laboratories, cold storage, furniture, etc, under the service industries, and many other sectors are included in the SMEs. Generally, in the Industrial Policy 2005 there are 11 different booster sectors of SMEs which are mainly Electrical, Software Development, Illumination engineering and Alloy works, Agro –business or Agriculture specialist, Farming or Tissue business, Leather related goods, Knitwear and ready-made garments, Plastics and other synthetics, Healthcare and diagnostics, Pharmaceuticals, Cosmetics, consumption goods.

## 2. Literature Review

Some foreign and national experts undertake some studies on the SME sector of Bangladesh. Some Bangladeshi’s institutions like the SME Foundation, the IFIC and some other financial institutions stated about SMEs potentialities that this SME is going up from micro to small and medium enterprise. Author Uddin (2008) has stated in his book about the SMEs total performance and economic efficiency in some countries mainly in the rising countries where these countries are noticeably dependent on the macro economic’s environmental & some of the promotional policies followed for their benefits. According to the context of Bangladesh Chowdhury (2007) emphasized on his book that

SME is featured by the low capitalization and inadequate assets, environmental diversity, the high morality, limited knowledge about SME, exceedingly restricted access to the credit's formal source as well as the strength of cash in some transactions, very inadequate documentation making a habit with meager monetary exposing on the account, taxes issues, very elevated risk insight has led to lofty borrowing costs. Miah (2007) stated that the main barriers for SMEs are the shortage of sufficient investment, insufficient modern technology, poor systems of bank loans, intermitten power supply, pitiable corporeal infrastructure, lack of proper information about the market requirements and opportunities, inavailability of needed raw materials, the shortage of trained technical expert and workers as well as limited facilities of research & development about SME in the context of Bangladesh.

### 3. Methodology

The study is conducted primarily based on the secondary data. The needed data have been gathered from the diverse resources of sources like websites, books, publications like Bangladesh Bank's publications, Ministry of Industrial sectors as well as the different SME policies of South Asian country's different types of SME policies and some scholars's pertinent writings. In order to carry out our research we did exploratory as well as descriptive research. We have conducted the exploratory research because we need to obtain information to conduct our research. We also conducted the descriptive research to analysis the policies and recommend some suggestions for the improvement of SMEs in Bangladesh. The population size is all South Asian countries where sample size six South Asian countries have taken i.e. Bangladesh, India, Pakistan, Nepal, Bhutan and Srilanka.

### 4. Small Enterprise

When a business is operated and owned independently and not dominated in its field is called Small Enterprise. (Small Business Act 1934). A business is called a Small Enterprise when a small firm has, relatively a small share of profits in the market (Bolton Report on small business firms 1977). When a business is owned and managed often with very few employees working at a single location which is mainly locally owned (Stoner, Freeman & Gillbert, 1995). The US Government is defined that a small business is one with fewer than 500 employees.

### 5. SME in the Context of Bangladesh

#### 5.1 Small Segment

The Small Enterprise means that a firm or a industry which is not a public limited company as well as the value of fixed assets (excluding building & land) up to Tk. 5000000 in case of manufacturing enterprise and maximum 25 workers in trading or service enterprise.

Table 1. The Small Enterprise criteria

| Serial No. | Sector   | Fixed Asset other than Land and Building (Tk.) | Employed Manpower (not above) |
|------------|----------|--|-------------------------------|
| 01.        | Service  | 50,000-50,00,000                               | 25                            |
| 02.        | Business | 50,000-50,00,000                               | 25                            |

#### 5.2 Medium Segment

The Medium Enterprises refer to the organizations/firms which are usually not public limited companies and values of fixed assets (except land & building) up to Tk. 100000000 in case of manufacturing enterprise and maximum 50 workers in trading or service enterprise.

Table 2. The Medium Enterprises criteria

| Serial No. | Sector   | Fixed Asset other than Land and Building (Tk.) | Employed Manpower (not above) |
|------------|----------|--|-------------------------------|
| 01.        | Service  | 50,00,000-10,00,00,000                         | 50                            |
| 02.        | Business | 50,00,000-10,00,00,000                         | 50                            |

### 5.3 SMEs in Bangladesh

Dissimilar countries with some organizations delineate the Small & Medium Enterprise in various ways where the government of Bangladesh has divided the SME into two wide classes:

- Manufacturing enterprises
- Non-Manufacturing enterprises

#### 5.3.1 Manufacturing Activities

There are two broad types of manufacturing activities;

**Small Enterprise:** A small enterprise is an enterprise when its current market prices of the placement costs of the plant, the equipment, different components, fittings, maintaining utilities and technical involvement services without the fixed assets like land and building are usually up to Tk. 5000000.

**Medium Enterprise:** When the market current prices, the replacement cost of plant as well as the equipment and other essential parts & fittings with supporting effectiveness and associated mechanical services apart from the land and building are usually up to Tk. 10000000 then an enterprise would be called as a medium size enterprise.

#### 5.3.2 Non- Manufacturing Activities (Like Trading or Other Services)

The Non-Manufacturing activities are usually trading or other services. The Non-Manufacturing activities can be divided into two wide categories;

**A) Small Enterprise:** An enterprise would be treated a small enterprise if an enterprise has less than 25 full time or equivalent.

**B) Medium enterprise:** If an enterprise has between 25-50 workers, then it would be treated as **Medium Enterprise**.

### 6. Different SME strategies & Policies in South Asian Countries

The SMEs are the mainstream of South Asian economies where this SMEs have emerged as mainly growth, production, export and import of different sectors. The South Asian countries execute their some SME advancement strategies especially in six crucial areas like Environment of Business, Entrepreneurship, admittance of finance, Research & development. It is designed to provide as a training for the entrepreneurs and trainers for increasing SME building capacity.

### 7. SME Policies & Strategies in Bangladesh

When some rules or principles usually guiding the decisions in order to get intended balanced outcomes is called policies. Generally, policy means some sets of guiding principles or rules of taking right decisions which is very essential to attain balanced outcomes. It is important that the government policies & strategies should be observed by almost all the ministers as well as the different government institutions & agencies or else the intended cogent outcome might not be attained. As a result the Government has adopted different types of SME policies & strategies the government has taken. The "Policies & Strategies of SME-2005" usually identified 11 crucial sectors for promotion. Where, these gave a significant emphasize as a thrust sector for the development of Small and Medium Enterprises (SMEs) for the intended proper and sustainable industrial growth with a vision for facing some burning issues of globalization and economic market through the contributor monetary resources made available particularly to aid with the implementation of the SME policies & strategies. According to the availability of whole resources only 20% may be commenced for medium enterprises where the rest biggest percentage around 80% will be commenced for only small type enterprises. The modalities which are very crucial of how to execute both the credit-fund and the venture-capital fund will be determined by the Misistry of & the Advisory Panel. The Development of SME Policoes & Strategies 2005 has played crucial role to the development of the SME sector where only 19.01% industrial sector contributed to the GDP.

#### The Wide Objectives of Policy Would Be to:

- Recognize the SME as vital thespian in the growth speeding up and poverty diminution as well as proper commitment which is very crucial to formulate policy & its implement The policies and strategies of SME will be entrenched in a wide sense and incorporated manner.
- Establish a good governance with some codes of ethics as well as management of Technology & Information based knowledge and consumer superiority in the markets in order to motivate and induce the development of private sectors as well as promote the growth of FDI.

- Recognize and set up an apposite corporeal and Technological infrastructural and some institutional delivering methods which will facilitate the SME promotion.
- Re-introduce the presented financial as well as the authoritarian construction and the government support of different institutions towards facilitating achievement SME policy's specific goals. In order to deliver the very needed services, goods, leadership with proper commencement, analysis, mentoring and tutoring the nurture as well as the civil society institutions partner have appreciable management teams.
- Create pioneering means that the meritocratic planning so that the commendable small enterprises with most wanted commercial track record and the promises can be offered as financial rewards within the industries .
- Aid to execute the procedures of argue settlement that the proactively defend the small businesses particularly from the much authorized costsas well as the subtle harassment.
- Take the procedures to form platforms to activate the liability without collaterals to match in order to aid the small enterprises in the efficient dealing with their invasive lack of access to finance.
- Systematically accord the precedence to small versus medium enterprises within the limitations of government's resources where everyone is facing the resources limitations.
- To tie together the information & the communications technologies which are very crucial for the better performance of SME.

### 8. Data Analysis & Findings

The contribution of SMEs to the total economy differs from country to country. The SMEs contribute to the total performance of GDP is 20%-25 % in Bangladesh while in India the SMEs contribute surprisingly almost 80% to the total GDP but in Pakistan only 15% of the total GDP comes from SMEs performance in Pakistan. In Bangladesh almost 80% of the entire enterprises are usually come from SMEs where in Pakistan 60% of the whole enterprises are usually come from SMEs.

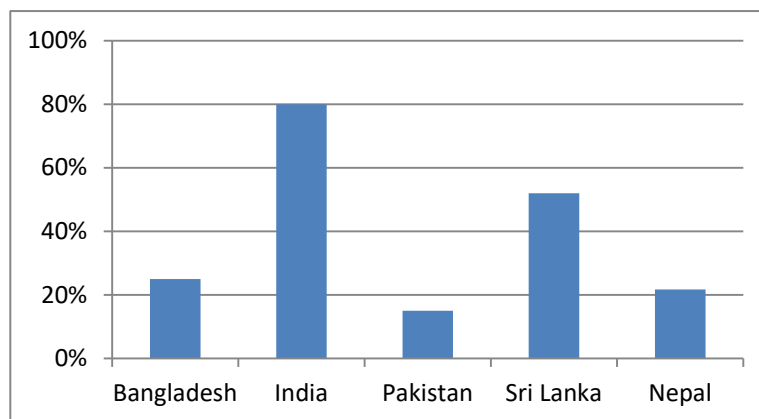


Figure 1. Contribution to Country's Economy

#### 8.1 Labor Force Employed in SMEs

Bangladesh employs 40% of its labor force in SMEs Bangladesh employs around 40% of its total labor force while 80% of its total labor force employs in SME sector in Pakistan but only 40% of its total labor force in India.

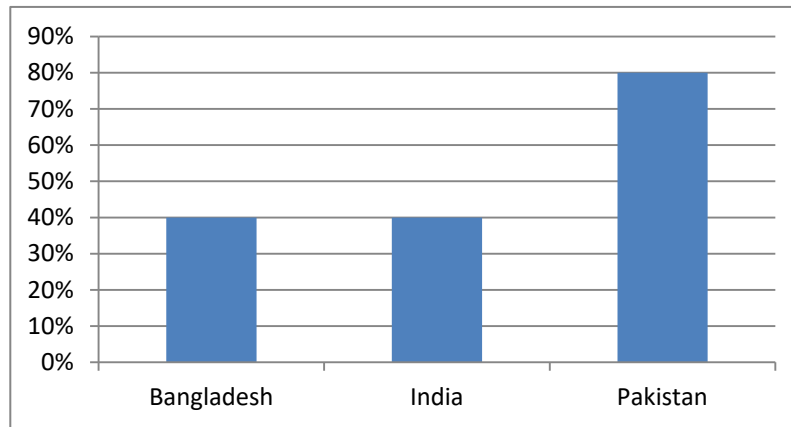


Figure 2. Labor force employed in SMEs

### 8.2 Credit Limit

Generally, in Bangladesh the Priorities are given to all entrepreneurs especially to small entrepreneurs like SME. The limit of credit will be from Tk. 500000 to Tk.5000000 usually for all the small entrepreneurs where in India the SME borrowers are given bank loan up to Tk. 5 crores which is quite high than that of Bangladesh. On the otherhand, in Bhutan, the rate of getting the SME loan is quite lower as only 48 get out of 198 entrepreneurs.

### 8.3 Tax Rate

High tax rate is one of the major reasons for firms to float into the informal economy in Pakistan. According to the recent research 67% of enterprises which are known as the tax regulations as the most challenging for firms. The government of Sri Lanka Recently the government of Sri Lanka has sanction a tax exclusion for some specific sectors of the SMEs with a minimum of 25 million where the tax rate is 12%.

### 8.4 Credit Guarentee

If the lender fails to pay back the intended loan in India the fund of credit guarantee covers only up to 85% while the Royal Government of Bhutan along with the two financial institutions formed the credit guarantee schemes to provide the sufficient loans to the eligible applicants. The Sri Lankan government introduced a credit guarantee insurance scheme in 2008 to assist 50 SMEs engaged in gems and jewellery sector.

## 9. Conclusion

Over the years the SME sector of Bangladesh has grown rapidly. Actually, the SME sector has broadened in Bangladesh but the depth has to be achieved in true sense. Usually, the SMEs performance in Bangladesh is found drastically below the level of international standard. The different sectors have to be made investor's investment forthcoming environment otherwise the strength of the SME's sector cannot be achieved. Though the government of Bangladesh has taken some initiatives. Though in order to ensure the growth of SME sector the government of Bangladesh has taken some essential steps but these steps are not adequate at all for ensuring the ultimate growth of SME sector. Nevertheless, the government has already shown its positive approach towards this potential SME sector. The government of Bangladesh as well as the people should prolong to give more focal point on some desired areas. The government should come forward in order to identify realistic and secure policies for the development of SME sectors in the country. The provision should be made In order to improve the separate and specialized institutions in three vspecific areas like: (a) finance, (b) technology, and (c) skill development for making a policy for the SMEs the condition should be made as well as to downsize the existing policies, strategies and institutions. We are completely hopeful that the potentialities SMEs of Bangladesh will get a boost if the suggested measures are implemented.

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