

# Problems and prospects of smes in bd essay



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Problems and Prospects of Small and Medium Enterprises (SMEs) sector in Bangladesh Abstract: Small and Medium Enterprises (SMEs) have been recognized as one of the important means for providing better economic opportunities for the people of least developing countries like Bangladesh. The objective of this paper is to portray the present picture and provide some recommendations of SMEs sector in Bangladesh. The study was based on secondary data e. g. published journals & research articles.

Financial and policy constraints are the main obstacle for the development of SMEs sector in Bangladesh. Although the Government of Bangladesh has recently taken up programs to provide financial assistances to expand SMEs through commercial banks, financial assistances and credit facilities are insufficient compared to demand and necessity of the SME entrepreneurs. Again policy level, legal and regulatory constraints are rarely being concentrated by the Government. . 0 Introduction: The Small and Medium Enterprises (SMEs) are recognized worldwide as engines of economic growth. The commonly perceived merits often emphasized for their promotion especially in the developing countries like Bangladesh include their relatively high labor intensity, dependence on indigenous skills and technology, contributions to entrepreneurship development and innovativeness and growth of industrial linkages.

The case for fostering SME growth in Bangladesh is irrefutable as these industries offer bright prospects for creating large-scale employment and income earning opportunities at relatively low cost for the unemployed especially in the rural areas strengthening the efforts towards achieving high and sustained economic growth which are critically important prerequisites

for triggering an exit from endemic poverty and socio-economic deprivation. According to the European Union (2003) SMEs are defined as enterprises which have at most 250 employees and an annual turnover not exceeding 50 million Euros.

Further there is the distinction of small enterprises they have fewer than 50 staff members and less than 10 million Euros turnover and micro-enterprises (less than 10 persons and 2 million Euros turnover). According to the World Bank (2006) medium enterprises are defined as enterprises which have at most 300 employees and an annual turnover not exceeding 15 million US dollars. Further there is the distinction of small enterprises they have fewer than 50 staff members and up to 3 million US dollars turnover and micro-enterprises have up to 10 persons and \$100, 000 turnover.

In India the Small Scale Industries (SSIs) are industrial undertaking in which the investment in fixed assets in plant and machinery, whether held on ownership terms or on lease or by hire purchase does not exceed Rs. 10 million. The Small Scale Service And Business (Industry related) Enterprises (SSSBEs) are industry related service and business enterprises with investment in fixed assets, excluding land and building up to Ps. 1 million.

(Ministry of trade and Industry, Government of India) In Bangladesh

Industrial Policy 2009 defines SMEs as follows: Basis | Manufacturing activity | Non-manufacturing industrial activity | | | | | | | | Industry classification | | | | Value of fixed assets | Number of manpower | Value of fixed assets | Number of manpower | | | excluding land and building | | | excluding land and building | | | Tk. 15 million to Tk. 200 | 50-150 workers. | Tk. 5 million to Tk. 100 | 25-50 workers. | | Medium Industry | million | | million | | | Tk. 0. 5

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million to Tk. 15 | 10-50 workers. | Tk. 0.5 million to Tk. 5 | 10-25 workers. | | Small Industry | million | | million | |

2. Objectives: The main objective of the study is to draw the present scenario of SMEs sector, problems and prospects in Bangladesh. The objectives of this study are also as follows; a) To appraise the present situation of SME in Bangladesh. b) To identify the problems and prospects of SME in Bangladesh. c) To recommend solutions to overcome the problems.

3. Methodology: The study on Small and Medium Enterprises (SMEs) in Bangladesh was based mainly on secondary data. I collected and read some published journals and research articles related to business, management and economics field. I also visited website of different institutions both local e. g.

ICAB & international e. g. ADB and international journal publication authorities e. g. SSRN and collected articles related to my work. I also discussed with our course instructor and my friends to complete the work and took some instructions & guidelines. Descriptive method is used to provide findings and recommendations. Descriptive method is based as to current growth and development of SMEs sector in Bangladesh.

4. Literature review: With respect to the SMEs sector of Bangladesh, national and foreign experts undertook some studies. Some of the notable ones are; Uddin (2008), Chowdhury (2007), Miah (2006), Ahmed & Chowdhury (2009), Ahmed (2006).

Uddin (2008) has stated that the economic efficiency and overall performance of the SMEs especially in the developing countries are considerably dependent upon macroeconomic policy environment and specific promotion policies pursued for their benefit. Chowdhury (2007)

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highlighted that in context of Bangladesh SME is characterized by Low capitalization and limited assets, geographical diversity and high mortality, poor credit knowledge, very limited access to formal source of credit, cash intensity in transactions, very limited record keeping habit, poor financial disclosure on account of tax issues, high risk perception has led to high borrowing costs.

In a study about SME sector of Bangladesh Miah (2006) stated that the major constraints for SMEs are lack of adequate investment, lack of modern technology, high rate of interest on bank loans, irregular and inadequate supply of power, poor physical infrastructure and high transportation cost, poor information about market opportunities and requirements, inadequate availability of raw materials, lack of skilled technicians and workers, lack of research & development facilities, absence of effective and transparent legal system, difficulties in accessing technology, credit constraints, low access to business services, constraint of quality of human resources, low awareness, low lobbying capacity, rapid changes in policy environment. Ahmed and Chowdhury (2009) highlighted that main problems of SMEs are resource scarcity, employee turnover, absence of modern technology, poor physical structure, financial constraint, lack of information, lack of entrepreneurship skill etc. Ahmed (2006) observed that availability of finance is a major constraint to formation and growth of SMEs in Bangladesh. Banks are reluctant to expand their SMEs credit portfolio because they do not consider SMEs lending an attractive and profitable undertaking.

This is so because SMEs are regarded as high risk borrowers because of their low capitalization, insufficient assets and their inability to comply with

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collateral requirements of the banks. Administrative costs are also higher because close monitoring and supervision the SMEs operation becomes necessary. 5. 0 Background: After Liberation of Bangladesh, intensive efforts were undertaken to accelerate the rate of industrialization in the country. At the beginning, import substitution and subsequently export-led economic growth strategy was pursued for industrialization. In order to attain this objective, large amount of industrial credit was funneled to the industrial sector. But the whole exercise of industrialization came to a halt with the massive diversion of resources to other non priority sectors. Policy makers, of late, have come to recognize the contribution of SME sector towards economic development in the country. SMEs have been recognized as one of the important means for providing better economic opportunities for the people of least developing countries like Bangladesh. A developing economy like that of ours suffers from many peculiar problems such as disproportionate pressure of population on agriculture due to lack of rural industrialization, unemployment and underemployment of human and materials resources, unbalanced regional development etc. The contribution of SMEs is the solution of these problems.

SMEs are particularly suitable for densely populated countries like Bangladesh where SME sector can provide employment with much lower investment per job provided. Out of 11% employment of the civilian labor force provided by the manufacturing sector, about two thirds are estimated to be provided by the small and cottage industries sector. Again, development of small industries facilitates the effective mobilization of capital and labor resources. They also help in raising standards of living of

people in rural areas. Contribution of SMEs sector to GDP remained above 4% during the period from 1985-86 to 1999-00. However, the present contribution of SMEs sector to production performance of manufacturing industries is significant.

The Quantum Index of Production (QIP) is an important tool for measuring the production performance of manufacturing industries. Data available from Bangladesh Bureau of Statistics (BBS) is shown below: FY 2002-03 to FY

Industry	2002-03	2003-04	Working Capital	Mid Term Loan	Long Term Loan	Total Loan	Industrial Loan	Commercial Loan	Service	Total																							
(a) Bangladesh Bank	235.00	555.83	250.85	1041.67	2804	6651	1743	11198	(b) IDA	64.74	112.80	93.84	271.38	981	1306	486	2773	(c) ADB	144.48	132.27	58.19	334.94	800	2096	368	3264	Total	444.22	800.90	402.88	1648.0	4585	10053

2597 | 17235 | | Source: Bangladesh Bank 6. 2. 2 Project Preparation and Evaluation: The first problem entrepreneur's face in seeking institutional finance is with regard to preparation of the project proposal. In spite of directives from the central bank to follow standardized procedure, the loan application process has still remained lengthy and cumbersome. The entrepreneur often lacks the ability to formulate a proper project proposal. Even when he prepares the proposal drawing on outside expert services, there is no guarantee that the proposal will be evaluated properly as the financial institutions themselves lack adequate capability for proper project evaluation. 6. 2. Collateral Requirements: One of the main factors that have hampered flow of institutional finance into SMEs is banks' pre-occupation with collateral based lending. Traditionally banks have used fixed asset

ownership, particularly land ownership as the basis for judging credit-worthiness. This puts SMEs at a relative disadvantage, as large entrepreneurs are often able to get around the problem because of their influence and contacts by putting up collateral of dubious valuation. The solution to this problem lies in banks seeking deposit relationship with owners of SMEs and using cash flow rather than asset ownership as the criterion for credit-worthiness. An expanded credit guarantee scheme will have to play a vital role in this regard.

### 6. 2. Bureaucracy and Corruption:

Because of lack of proper autonomy and accountability the public sector financial institutions are beset with inflexibility, inefficiency, political interventions and corruption. Since the performance of the bank officials is not properly evaluated they lack the incentive to bring a large number of suitable borrowers, particularly those in the SME sector, within the fold of institutional financing. They adopt a passive and inflexible attitude towards the borrowers either to avoid the risk of making an inappropriate lending or to force the borrower to make side payments for more favorable handling of the loan application.

Until necessary reforms in the public financial institutions are carried out, the SMEs will continue to bear the brunt of this institutional malice.

### 6. 3 Legal, Regulatory, and Administrative Constraints

As mentioned earlier, policy reforms of the past decade have brought about substantial relaxation in the investment sanctioning procedure. No prior approval is now required for investments involving own finance. However, there is scope for further improvement in the following procedural aspects relating to investment



regulations. 6. 3. 1 Trade License: Investors are required to procure trade license from local government bodies by paying statutory fees.

The process involves unnecessary delays, harassment and side payments. The procedure needs to be simplified and the issuance of the license made automatic subject to payment of requisite fees and declaration by the investor that the proposed investment is in conformity with the rules and regulations and zoning restrictions of the local government authority. 6. 3. 2 Registration under Factories Act: According to the Factories Act 1965, all manufacturing units employing 10 or more workers are required to be registered with the office of the Chief Inspector of Factories and Establishments. The job of the Factory Inspector is to keep an eye on the working condition and safety measures in the factory.

In practice, the regulation has proved to be a major source of delay, harassment and unofficial payments for the investors particularly for those in the SME sub-sector as the existing regulations do not differentiate between different size categories with respect to safety and working conditions requirements. To relieve the investors of these problems the requirements relating to safety and working conditions should be defined separately and realistically for the SMEs and the discretionary powers of the Inspector should be minimized. Registration should be automatic once the investor has declared that the requirements have been complied with. 6. 3. Clearance from the Department of Environment: All industries are also required to obtain a certificate from the Department of Environment in respect of proper arrangement for anti-pollution and safety measures. Here again, the requirements should be clearly stated for the type and size categories of

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industry and the investor should be allowed to go ahead with investment on the basis of the undertaking that the requirements will be complied with. 6.

3. 4 Registration with Sponsoring Agency: Registration with sponsoring agencies such as the Bangladesh Small and Cottage Industries Corporation (BSCIC), Board of Investment (BOI) or Bangladesh Export Processing Zone Authority (BEPZA) is voluntary unless an enterprise wants to avail itself of government incentives.

To keep track of private investment in various sub-sectors, it would be useful to make registration with the sponsoring agency mandatory. However, to relieve the investors of possible hassles, registration procedure should be simplified requiring minimum information to be provided by the investor, and registration should not be held up until the proof of investment has been produced as the current practice appears to be. 7. 0 Recommendations: In order to prevail over the above mentioned problems and constraints the following suggestions are recommended; 7. 1 Government must have to take ample measures to ensure the uninterrupted supply of raw materials for SMEs both from local market and global market. 7. Government needs to take appropriate measures to fix the minimum wages of the employees of SMEs. That will help to minimize the employee turnover and increase employee satisfaction. 7. 3 Government, financial institutions, nonbanking financial institutions and Non Government Organizations (NGOs) may provide adequate financing facilities for modernization and technological advancement. Again Government through Bangladesh Bank and other international financing assistant agency e. g. IDA, ADB should take up sufficient programs to provide financial assistance to expand SMEs through

commercial banks. 7. 4 Development of infrastructure is indispensable for the optimum growth of SMEs.

So government of Bangladesh needs to take appropriate policy strategy for the infrastructure development of Bangladesh. 7. 5 Due to the absence of uniform definition the policy formulation and implementations are not possible. Government should take initiative to develop a uniform definition of each category of SMEs considering the amount of capital investment and number of man power used. 7. 6 Government of Bangladesh should take the initiative to develop web pages exclusively for SMEs and an integrated SMEs database. It will reduce the barriers to SMEs access to global market.

Conditions for taking credit from banks and nonfinancial institutions should be stated and updated. 7. In order to ensure the retention of skilled workforce the government should make the entrepreneurial career attractive by minimizing the uncertainty and several training programs can be arranged for entrepreneurs on behalf of the Government. 7. 8 In order to encourage women entrepreneurship Government may involve women entrepreneurs in policy formulation and implementation, arrange funds for women entrepreneurs and provide necessary training to women entrepreneurs in rural and urban area of Bangladesh. 7. 9 For minimizing red tapes and accelerating the growth of SME government may provide one roof service under the SME foundation. 7. 10 Appropriate legal framework is necessary to ensure the development of SME of Bangladesh. 7. 11 In this era of intense competition continuous planning and quality improvement act as a prerequisite for the survival of SMEs.

In order to improve the quality SMEs can follow the Just in Time (JIT) philosophy and use Total Quality Management (TQM) and can ensure the improvement of quality and productivity at a time. 7. 12 Government should establish a credible certification authority especially for SMEs so that this sector can obtain a technical evaluation of the quality of their products within a shortest possible time. The certification of the authority should be worldwide accepted. Government may also provide support to SMEs during the certification process and promote the importance of product certification for international acceptance among the SMEs. 8. 0 Conclusion: Small and medium enterprises (SMEs) act as a crucial player for the economic growth, poverty alleviation and rapid industrialization of the developing countries like Bangladesh. SMEs are significant in underlying country's economic growth, employment generation and accelerated industrialization. Government of Bangladesh has highlighted the importance of SMEs in the Industrial Policy-2009. SME has identified by the Ministry of Industries as a ' thrust sector'. As the SMEs sector is labor intensive, it can create more employment opportunities. For this reason government of Bangladesh has recognized SMEs as a poverty alleviation tool. SMEs also foster the development of entrepreneurial skills and innovation. Along with poverty alleviation SMEs can reduce the urban migration and increased cash flow in rural areas.

As a result it will enhance the standard of living in rural areas. Performance of SMEs in Bangladesh is comparatively found below the level of international standard. Although government of Bangladesh has taken up some initiatives to ensure the growth of SMEs but those steps are not enough at all. But government shows its positive attitude towards this

sector. Bangladesh government should continue to give more focuses on some areas, such as arrangement of finance, provide infrastructure facilities, frame appropriate legal framework, establish national quality policy etc.

From the sequence of the work it seems that for the economic development of Bangladesh, SMEs can contribute an important role.

We are quite optimistic that if the above mentioned suggestions are implemented then the growth of SMEs sector in Bangladesh will be

accelerated soon. References Ahmed, K. and Chowdhury, T. A. (2009).

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