

## **PRESENT SCENARIO AND STRATAGEM TO SMES DEVELOPMENT IN BANGLADESH**

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### **Abstract**

In the context of Bangladesh, Small and Medium Enterprises (SMEs) have assumed special significance for poverty reduction programs and potential contribution to the overall industrial and economic growth as well as lowering unemployment rate. The birth rate of SME refers to high rate of entrepreneurship skill, free flow and well distribution of available resources, technical innovation that turn to the rapid industrialization. This article reveals that SMEs have received disproportionately smaller support from the government in terms of policy or fiscal incentives. The contribution of SMEs in the development of Bangladesh economy has been significant, both in terms of contribution to GDP and creation of employment opportunities. But activities of SMEs of Bangladesh especially in terms of quality assurance, allocation of fund, marketing efforts have been found significantly below from the international standard. The study thus investigated the performance of the SMEs in the economy of Bangladesh, its problems and prospects and recommended measures to make the sector virile and vibrant in order to play the crucial role it is expected to play.

**Key-words:** SME, Capital, Employee, Pointers.

### **Introduction**

In Bangladesh, SMEs have performed below expectation due to a combination of problems as, environment related factors of SMEs growth, instability of government and frequent government policy changes and somersaults. In the context of Bangladesh, the development of Small and Medium Enterprises (SMEs) can be considered as a vital instrument for poverty alleviation and assurance of rapid industrialization. The ministry of industries, Government of Bangladesh identified eleven booster sectors. Those are- electronics and electrical, software-development, light engineering and metal-working, agro-processing/agro-business/plantation agriculture/ specialist farming/tissue-culture, leather-making and leather goods, knitwear and ready-made garments, plastics and other synthetics, healthcare & diagnostics, educational services, pharmaceuticals/cosmetics/toiletries and fashion-rich personal effects, wear and consumption goods.

### **Objectives of the study**

The paper addresses the factors that influence the development and growth of SME sector of Bangladesh. With reference to the following:

- The generic condition and contribution of the SME

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- Organizations associating the prosperity of SME in our country
- Role of SMEs in national economy
  - Promotion of SME
  - Current status of SMEs in Bangladesh
  - Constrains affecting the SMEs in Bangladesh

### **Methodology**

Following methods have been used in this study.

#### ***Content Analysis***

- Analysis of the budget documents of the government of Bangladesh to find incentive schemes given for SMEs.
- The past and the current industrial policies of Bangladesh (related to SMEs).

#### **Group discussion with Industrial Elites**

- The study carries out in-depth interview with eminent industrialists, entrepreneurs in 8 sectors to understand the problems related to SMEs in Bangladesh
- The study also carries out in-depth interview with government officials involved in SME sectors.
- The study also carries out in-depth interview with financial institutions involved in SME sectors.

#### **Questionnaire Survey**

- Information from the entrepreneurs has been collected and analyzed.
- The research involves a questionnaire survey. The questionnaire was asked in most questions by keeping in mind the time factor and the variation in educational background among the respondents. Majority of the questions are pre-coded to facilitate the analysis of data. In some cases, interviews were conducted using the questionnaire as a guide. At the same time, substantial amount of help was taken from the secondary sources like newspapers, magazines, books, and journals based on the relevance to the research.
- Data were analyzed mainly by applying tabular method. In certain cases, charts and simple statistical tools like averages, percentages, etc. were used for the precision of the data analysis.

#### **Review of literature**

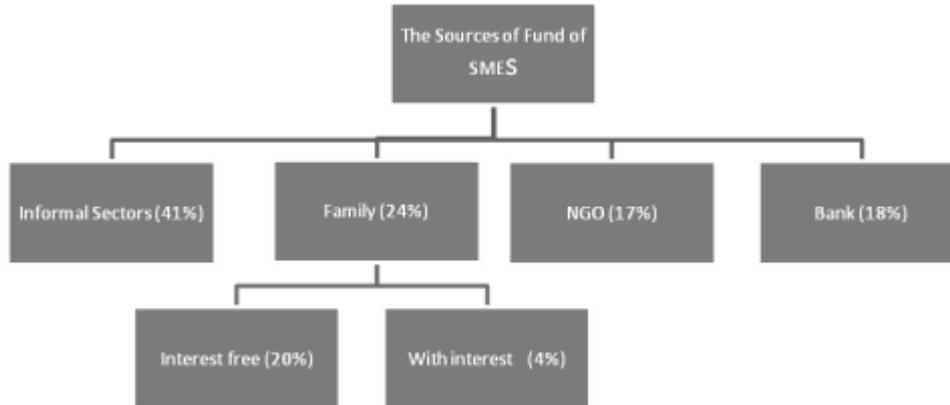
Small and Medium-sized Enterprises (SMEs) play a pivotal role in terms of economic growth, employment generation and industrialization. Small and Medium-

sized Enterprises (SMEs) ensure the back linkage of large industries by supplying the raw or semi raw materials to those industries. Although the role of SMEs varies at different stages of economic development, their role is particularly important in developing countries and LDCs like Bangladesh. With respect to the SME sector of all over the world and Bangladesh, foreign and national experts undertook some studies.

Global experiences show that an efficient SME sector is conducive to foster industrial growth (Hill, 2001) and it is now an important issue to overcome current financial recessions. Exploring the development of the South African Llyod (2002) analyzed SME sector over the 1980 to 2000 period and found that expanded small-businesses were playing an increasingly important role in the manufacturing, construction and trade sectors in South Africa, but their role declined in the agriculture, transport and storage sectors. According to Hallberg (2002), a stable macro-economy, an open trade and investment regime, and a competitive financial sector are the most essential ingredients for a vibrant private sector.

Causes of complex or long processing formalities and non-professional attitudes of the financial institutions, a study (2004) by Micro Industries Development Assistance and Services (MIDAS) revealed that sources of finance are mostly from friends and family members in case of SME. MIDAS tried to identify the sources of funds of SMEs. These are:

Figure 1



Source: A study report of MIDAS, 2004.

Beck, Kunt, and Levine (2005) found a strong correlation between SME development and GDP that make sure the economic ultimate goal, but the relationship between growth and the overall business environment for SMEs overshadows the former relationship though SMEs require low capital per unit of output.

An analysis of the data from the Small Enterprises Fund (SEF) Administered by the Bangladesh Bank and Naeem Chowdhury (2007) 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 (2007) stated that the major constraints for SMEs are lack of adequate investment, lack of modern technology, high rate of interest on bank loans, irregular/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, intense competition, 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. From a analysis of Naeem Chowdhury & Mohammad Ayub Miah (2007) identified the re-financing through the Small Enterprise Fund (SEF) into scheduled banks between 2004 and May 2007 are:

Figure 2 : (Tk. millions)

Name of banks	Disbursement of proceeds from Bangladesh Bank				Disbursement of proceeds from IDA				Disbursement of proceeds from ADB			
	WCF	MTF	LTF	Total	WCF	MTF	LTF	Total	WCF	MTF	LTF	Total
NCC	19	97	8.8	124.8	1	55.9	41.3	98.2	1.6	2.2	1.9	5.7
Jamuna	59.6	11.7	1.4	72.7	65.8	8.1	3.8	77.7	-	-	-	0
NBC	6	0	-	6	4	-	-	4				0
One	5.8	29.1		34.9	3.3	11.4		14.7	41.2	27.5	9	77.7
Premeir	121.9	21.8	9.4	153.1	71.5	2.7		74.2				0
BRAC	38.7	309		347.7	10	328.8		338.8				0
Southeast	27.9	1.5		29.4	53.3	1.7	3.5	58.5				0
DBBL	3.1	0		3.1	85.2	1.3		86.5				0
Mercantile	0	17.4		17.4				0				0
Eastern	0.3	154.6		154.9				0	114.3	0.5		114.8
DBL				0	19.9	21		40.9	62.3	17		79.3
Prime				0				0	118.9	8.7	2.4	130
Sub total	282.3	642.1	19.6	944	314	430.9	48.6	793.5	338.3	55.9	13.9	407.5

Source: Economic Review, Ministry of Finance, GOB, 2007.

WCF=Working Capita Finance, MTF=Medium Term Finance, LTF=Long Term Finance

This table shows the income from SMEs that distributed to the fund providers by different banks.

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.

### **An overview of SME**

Though the abbreviation of SME is Small and medium enterprises but the range of SME vary in context from organization to organization, country to country. So to make proper focus on SME at first to identify the basic difference of SME in different aspect.

According to the World Bank, SMEs include micro enterprise with maximum 10 persons and \$100,000 turnover in a year, small enterprise with maximum 50 employees and up to \$ 3,00,00,00 turnover and medium enterprise with maximum 300 employees and annual turnover not exceeding \$15,00,00,00.

In the USA, the definition of small business is set by a government department called the Small Business Administration (SBA) as Size Standards Office. The SBA uses the term “size standards” to indicate the largest a concern can be in order to still be considered a small business and therefore able to benefit from small business targeted funding. The most common size standards are

- 500 employees for most manufacturing and mining industries
- 100 employees for wholesale trade industries
- \$7 million of annual receipts for most retail and service industries
- \$33.5 million of annual receipts for most general & heavy construction industries
- \$14 million of receipts for all special trade contractors
- \$0.75 million of receipts for most agricultural industries

In UK, sections 382 and 465 of the Companies Act 2006 define a SME for the purpose of accounting requirements. According to this a small company is one that has a turnover of not more than £6.5 million, a balance sheet total of not more than £3.26 million and not more than 50 employees. A medium-sized company has a turnover of not more than £25.9 million, a balance sheet total of not more than £12.9 million and not more than 250 employees. It is worth noting that even within the UK this definition is not universally applied.

In India, Industries are classified into the following categories, according to size: Large-scale industries (LSI); Medium-scale industries; Small-scale industries (SSI) and Tiny sector. Medium-scale industry refers to the units whose investment falls between Rs 3 crores (US\$ 750,000) to Rs 100 crores (US\$ 25 million). SSIs are units whose total investment in plant and machinery does not exceed Rs 3 crores (US\$ 750,000). The definition of investment does not cover money spent on buying land and erecting buildings and workshops, nor does it include working capital. The investment limit is revised upwards from time to time; the single exception is the revision being done currently to revise it downwards from US\$ 750,000 to 150,000. Tiny sector units, as the name suggest an investment limit of Rs 25 lakhs (US\$ 62,500). This is also likely to be revised downwards.

**Criteria used to define SMEs in South-East Asian countries**

	<b>Employees (No.)</b>	<b>Capital (in thousands of US\$ - approx.)</b>	<b>Turnover (in thousands of US\$- approx.)</b>
Brunei Darussalam	Small 1- 10 Medium 11 - 100		
Indonesia	SMEs < 100	SMEs < 84 (totalassets)	SMEs < 1,000 (sales)
Lao PDR Small < 10	Medium 10 - 29	Depends on the no. of establishments in sector	
Malaysia	SMEs < 76 Small < 198	Medium 198 – 939	
Myanmar	Small < 50 Medium 50 - 100	Small < 167 Medium 167 – 835	Small < 417 Medium 417-1,670 (production)
Philippines	Small 10-99 Medium 100 – 199	Small < 570 Medium 570 - 2,282	
Singapore	(services sector) SMEs < 100	(manufacturing sector)SMEs: < 8,570	
Thailand	(labour-intensive industries) Small < 50 Medium 50 - 200	(capital-intensive industries:fixed assets) Small < 781 Medium 781 - 3,905	
Viet Nam	Small < 50 Medium 50 - 100	Small < 4 Medium 4 – 18	

The ceiling for being considered as SME throughout each of the countries in the region – in terms of numbers of workers – is 29 (Lao People’s Democratic Republic), 75 (Malaysia), 100 (Brunei, Indonesia, Myanmar, Singapore and Viet Nam), and up to 200 workers (the Philippines and Thailand). For countries that distinguish between "small" and "medium", the category of small enterprises ranges in size from up to 10 workers (Brunei and Lao People’s Democratic Republic), 50 workers (Myanmar, Thailand and Viet Nam), and up to 100 workers (the Philippines). These data show the variations that occur even among countries in the same region, some of which are at similar stages of development. For example, in Malaysia, an enterprise with 80 workers is not an SME, but it is in the Philippines. Similar variations exist in terms of applying the criteria of value of capital and of turnover.

The Bangladesh Bank has defined the small and medium enterprises (SMEs):

#### *Small enterprise*

Service concern: Total fixed asset Tk 50,000 to 3 million excluding land and building; number of employees less than 20 persons. Trading concern: Total fixed asset Tk 50,000 to 5 million excluding land and building; number of employees less than 30 persons. Manufacturing concern: Total fixed asset Tk.50,000 to 10 million excluding land and building; number of employees less than 60 persons.

#### *Medium enterprise*

Service concern: Total fixed asset above Tk 3 million to 10 million excluding land and building; number of employees less than 50 persons. Trading concern: Total fixed asset above Tk 5 million to 20 million excluding land and building; number of employees less than 50 persons. Manufacturing concern: Total fixed asset above Tk 10 million to 50 million excluding land and building; number of employees less than 100 persons.

### **SMEs and the national economy of Bangladesh**

Any precise quantitative estimation of the importance of SMEs in Bangladeshi economy is precluded by non-availability of comprehensive statistical information about these industries at the national level. The latest BSCIC suggest that there are currently 55,916 small industries and 511,612 cottage industries excluding handlooms. Including handlooms, the number of cottage units shoots up to 600,000 units indicating numerical superabundance of the SCIs in Bangladesh. Quoting Informal Planning Commission estimates, the SMDF puts the number of medium enterprises (undefined) to be around 20,000 and that of SCIs to be between 100,000 to 150,000. This wide variation in the BSCIC and Planning Commission estimates of the numerical, size of the SMEs might be due to at least two reasons: (a) different set of definitions of the SMEs and (b) different coverage of SME families. This strongly suggests the need for adopting and using an uniform set of definitions for SMEs by all Government agencies to help formulation of pro-active SME promotion policies.

Whatever the correct magnitude, the SMEs are undoubtedly quite predominant in the industrial structure of Bangladesh comprising over 90% of all industrial units. This numerical predominance of the SMEs in Bangladesh's industrial sector becomes visible in all available sources of statistics on them (Ahmed, M.U 2001).

Together, the various categories of SMEs are reported to contribute between 80 to 85 per cent of industrial employment and 23 per cent of total civilian employment (SEDF, 2003)<sup>2</sup>. However, serious controversies surround their relative contribution to Bangladesh's industrial output due to paucity of reliable information and different methods used to estimate the magnitude. The most commonly quoted figure by different sources (ADB, World Bank, Planning Commission and BIDS) relating to value added contributions of the SMEs is seen to vary between 45 to 50 per cent of the total manufacturing value added. While the SMEs are characteristically highly diverse and heterogeneous, their traditional dominance is in a few industrial sub-sectors such as food, textiles and light engineering and wood, care and bamboo products. According to SEDF sources quoted from ADB (2003), food and textile units including garments account for over 60% of the registered SMEs. However, as identified by various recent studies, (Ahme, M.U. 2001, ADB 2001, US-AID 2001) the SMEs have undergone significant structural changes in terms of product composition, degree of capitalization and market perpetration in order to adjust to changes in technology, market demand and market access brought by globalization and market liberalization.

### **Structural transformation of SMEs**

In terms of number of establishment, the SME sub-sector has exhibited notable dynamism, registering reasonably high growth rates over the decades of 1980s and 1990s. This numerical expansion of the SMEs has contributed towards substantial new business creation in the industrial economy of Bangladesh. Available evidence (Ahmed M.U. et.al. 1992) suggests that the SMEs were responsible for giving birth to 60 percent of the new industrial enterprises during 1980s.

Growth in SME employment seems to have been even better during the same period. The dismal performance in value added growth is explained by the weak and

faulty data base used by the BBS to estimate the parameters. This phenomenon of gross underestimation of SME value added resulting from weak estimation procedures used by the BBS has been confirmed by many researchers (Bakht 2001).

Indeed, when revised estimates of value addition in the SMEs are made using the new system of national accounts<sup>3</sup>, the annual compound rate of growth of value added by the SME sector not only shoots up to 7.7 per cent per annum during 1989/90 and 1994/95, it exceeds that of the large-scale industries during most of the 1990s. This trend exhibits dynamism and vibrancy of the SME sector except in late 1990s when growth of the sector tapered off slightly due to extensive damages caused to the sector by the 1998 floods, especially to its production and capital stock.

It will be noted that broadly four industry categories such as food and allied products, textiles and apparels, and engineering and fabricated metal products are currently dominant in the SME sector. However, at the disaggregated levels, important structural changes appear to have taken place in the sector between 1978 and 1991. For example, at the four-digit level, while three out of the top ten industries accounted for 82% enterprises and 63% of gross output in 1978 and 70 % of enterprises and 53% of gross output in 1991, the number of top industries has shot up to seven, spreading over light engineering, readymade garments, printing and publishing and wood and wood products.

The other new industries which have grown in importance in the SME sector in the recent years are plastic products, electrical goods, electronics, artificial jewelers, wooden and steel furniture, television and radio assembling and soaps and detergents. This is reflective of a structural change taking place in the SME sector from traditional to relatively modern product categories, perhaps with higher capitalization and use of better production techniques.

Summarizing the findings of various major studies the SMDF lists the following important positive changes taking place in the situation of the SMEs in Bangladesh:

- SMEs have diversified their activities.
- Entry and exit into the sector has become easier.
- The RMG industry has contributed significantly to SME development by providing them with orders for accessories and packaging materials.
- The development of the footwear industry has increased subcontracts to SMEs.
- Small-scale entrepreneurship has grown significantly in agro-processing in general and in poultry in particular.

### **Stage of SMEs Development**

Through four key stages one after another a business develops its life cycle. From different scholars these stages are named in different names. From Vesper Karl H in his paper that appeared in the Harvard Business Review (57.no.4) in 1979 identified the following 4 stages: 1. Pre-start-up, 2. Start-up, 3. Early growth, 4. Later growth.

According to Vesper Miller Harry the four stages run: 1. Survival, 2. Growth, 3. Shaping, 4. Maturity.

Now a days a household or an employed person can introduce himself as a successful business person by selling something in a small number of pieces, in his locality, without any cost bearing advertisement to earn some profit. At early period this business no need any standard business plan or other obligations. So that it may act as seed bed for a new venture.

### Contribution of SMEs in Bangladesh

SMEs contribution to the overall GDP in Bangladesh, we saw that when less than 10 people are working or doing business jointly than total contribution increased to the GDP. When more than 50peoples are doing business, contribution is comparatively less.

#### Contribution on SMEs in the GDP on Bangladesh:

Numbers of Workers	Total Contribution to GDP (Taka)	Percentage of Total Contribution
0-1	193 996 555 714	26
2-5	379 663 897 358	51
6-10	73 120 983 681	10
11-20	45 183 240 157	6
21-50	33 960 498 076	5
51-100	15 138 922 373	2
<b>Total</b>	<b>741 064 097 360</b>	<b>100</b>

Source: ICG/MIDAS Survey, 2003

We have also seen that manufacturing sectors contribute more than 38% of SME in GDP of Bangladesh and agriculture, wholesale & retail trade contribute 24% and 23% respectively in GDP.

#### Sector wise contribution of SMEs in GDP of Bangladesh

Sector	Total Contribution to GDP (Taka)	Percentage of Total Contribution
Agriculture	177 729 637 637	24
Fishing	32 872 674 464	4
Manufacturing	282 344 700 575	38
Construction	7 196 460 200	1
Wholesale and Retail trade	171 335 861 390	23
Hotels and Restaurants	28 599 263 975	3
Transport, Storage and Communication	8 950 171 356	1
Real state, Renting and Business activities	13 771 436 794	2
Education	151 808 506	1
Health and Social Work	2 743 049 893	1
Other Service activities	15 632 094 785	2
<b>Total</b>	<b>741 327 159 609</b>	<b>100</b>

Source: ICG/MIDAS Survey, 2004.Note: US \$ 1 = BDT 69.00

We have found that growth pattern of SMEs are increasing day by day. Growth percentage of small enterprise in 2000-2001 was 7.69%, in 2005-2006 it was 9.21% and in 2008-2009 it is 11.34%.

<b>Year</b>	<b>Growth percentage of small enterprise</b>
2001-2002	7.69
2002-2003	7.21
2003-2004	7.45
2004-2005	7.93
2005-2006	9.21
2006-2007	10.28
2007-2008	10.89
2008-2009	11.34

Source: Bangladesh Economic Review 2008-2009

### **Constrains to SME growth**

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. Given an excessive heterogeneity and almost a bewildering diversity in the type, composition and characteristics of the members of the SME facilities it is exceedingly difficult to have any precise diagnosis of their operational constraints. Over the years many studies have been carried out to identify the operational bottlenecks encountered by the SME entrepreneurs. One of the most recent studies (Sarder, J. 2001) based on a small sample of 19 entrepreneurs identified the following (as perceived by the respondents) as the major difficulties faced by them:

- Lack of modern technology
- Lack of adequate investments
- Irregular/inadequate supply of power
- High rate of interest on bank loans
- Inadequate availability of raw materials
- Absence of clear-cut government policies
- Fierce competition
- Lack of skilled technicians and workers
- Lack of research and development facilities.

**Different types of problems faced by SMEs at a glance:**

Nature of problems	Frequency	Percentage
Poor transportation facilities	50	83
Lack of entrepreneurship education and training	40	66
Financial assistance	35	58
Hartal (strikes) 60 100	60	100
Law and order situation	50	83
Bureaucracy	45	75
Lack of control of corruption	50	83
Lack of adequate investment	50	83
Lack of government support and assistance	35	58
Lack of research and development	50	83
Inadequate information	50	83
Inability to forecast demand	40	66
Frequent power failure	60	100
Inadequate telecommunication services	50	83
Fear of failure	50	83
Lack of technology	45	75

Source: Review of the ministry of industries Dhaka, July 14, 2007.

**Proposed agenda for action**

The economic arguments for SMEs should be more broad-based and emphasize the various special merits intrinsic and specific to their smallness.

1. A uniform set of definitions should be designed and used by all pertinent agencies (i.e. BBS, Ministry of Industries/ BSCIC, Planning Commission and NBR) with respect to classification of enterprises by size. In this context, a well-thoughtout decision is needed to ascertain whether "SME" is the correct term to identify 'Small', 'Cottage' and 'micro' industries in Bangladesh.
2. A sufficiently large sample survey should be carried out to generate a benchmark national level data base both for accurate estimation of the SME contributions to the national economy and for formulation of comprehensive policies for the sector.
3. To make successful the vision of SME sector, the Government should give privilege the young educated qualified and recently passed students to give the loan assistance.
4. Given heavy reliance of the national economy on the SMEs for generating employment and income especially for the poor in the rural areas, development of entrepreneurship, new business creation and development of

intersectional linkages the SMEs should be declared as a ‘priority sector’ and backed by formulation of a proactive SME development policy.

5. Within the SME sector, the fast growing sub-sectors exhibiting greater dynamism and prospects for sustained future growth should be declared as ‘thrust sector’ and supported by adequate incentives on a priority basis.
6. The Government should give the opportunities to the young entrepreneurs as well as qualified business persons to visit the developed countries those are doing practice of SMEs and use low cost modern technologies.
7. To strengthen SMEs sectors, the government may consider providing credit guarantees on SME loans. Such credit guarantee schemes, which are common in many countries, may specifically target prospective sectors especially having export potential.
8. The updated information like group distribution of SME loan for women must be circulated properly and make sure that potential clients are well informed.
9. Special SME development fund may be created to subsidize projects to be carried out by potential entrepreneurs. The banks and Financial Institutions may provide institutional credit and credit facilities under special programs and the special funds may be earmarked for SMEs through targeted support schemes, like new entrepreneurs fund, women entrepreneur fund, and similar other innovative programs.
10. In the proposed SME development policies, provisions should be made to develop separate and specialized institutions in three areas: (a) finance (b) technology and (c) skill development, in addition to rationalizing the existing policies and institutions. In this context, a strategic ‘Public-private Sector’ partnership and cooperation should be carefully developed keeping in view the current emphasis on fostering industrial development through private enterprises systems.

## **Conclusion**

SMEs are the sine-qua-non for economic development of a country like us. As a least developed country only SMEs can play a vital role for further industrialization and to make a successful entrepreneur. The studies reviewed reveal that SMEs have received disproportionately smaller support from the government in terms of policy or fiscal incentives. SMEs, as a group, are weak in echoing their needs and demands. There need improvement in the sanctioning and other administrative procedures affecting SMEs. Further simplification, transparency, and accountability are necessary to promote SME development. A wide array of constraints faced by SMEs has been briefly discussed in this report. It is apparent that problems related to power and credit is the most significant scenario. Legal barriers, poor law and order conditions, are some of the other problems that have adverse affect on SME development.

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