Ensuring Revival for the Many

COTTAGE, MICRO, SMALL, AND MEDIUM ENTERPRISES IN BANGLADESH

ASIA’S PATH FORWARD

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INTRODUCTION

The Cottage, Micro, Small and Medium Enterprises (CMSMEs) sector is a significant emergent source of employment creation in Bangladesh. Due to its small scale of production and fragile entrepreneurship, it is also the most susceptible to economic shocks posed by the advent of the global pandemic and economic shutdown. Due to the outbreak of the Covid-19 virus, small businesses, including in the CMSMEs, have been scaling down and temporarily closing as consumers stay home to be safe from the spread of the highly infectious virus. As a result, many small businesses of Bangladesh are already on life support.

Small and medium scale entrepreneurs face a multifaceted challenge in terms of temporarily halting sales, whilst paying continuing expenses such as loan repayments, and not receiving easy access to credit hindered by stringent conditions imposed by banks. The government has introduced a working capital loan facility of USD 2.35 billion at a subsidized interest rate for the CMSMEs. The loss on two major occasions- Pahela Baishakh and Eid-ul-Fitr due to the lockdown has been a shock to the enterprises as they have lost their principal scope of business in a fiscal year. The fashion industry alone has lost a total of USD 0.71 billion worth of business.

The CMSMEs elevate economic growth as well as generating employment opportunities because the sector is labor-intensive and less time-consuming for production with less capital expenditure or lower establishment cost. Out of 7.8 million enterprises in Bangladesh, 88% (6.86 million) are cottage enterprises that employ 13.16 million people. A further 0.11 micro enterprises create employment of 0.56 million. CMSMEs together represent 99.84% of the total enterprises in the country. In aggregate, SMEs contribute 25% of Bangladeshi GDP. As of 2018 CMSMEs it stands at 79 billion USD and accounts for 40% of the manufacturing output.

The CMSMEs have been facing a significant crisis due to the global pandemic. About 52% of SMEs have closed after generating zero revenue, and a further 28% of SMEs have experienced revenue losses of at least 50%. In the Service industry, 40% SMEs experienced a heavy hit of considerable revenue loss by 50% or more. About 14% of SMEs have already laid off all their employees. Inadequate financial access was a major obstruction to SME development, and it has worsened the effect of the pandemic.

Female small business owners may be more adversely affected than other groups. Access to finance has always been a serious concern for women entrepreneurs. Women entrepreneurs are supposed to receive at least 15% of all credit within the SME sector as per the directive of the central bank. Despite this initiative, most women entrepreneurs are facing difficulties to acquire credit from banks and other NBFI. The key barriers are related to collateral requirements and guarantee, trade license and rigidity of loan procedures and lender bias against women entrepreneurs.
FROM ‘SURVIVAL AT STAKE’ TO RECOVERY MODE

For the economy to recover, it is vital that CMSMEs are able to recover and rebuild themselves. The current economic slowdown has seen small businesses struggle to survive as their operations are halted and revenues have diminished or gone negative. Reconstruction of the sector will require first assisting businesses with survival strategies and then equipping them to recover. SME recovery can be analyzed by examining four major support areas- policy based support, fiscal support, financial support and support for the women entrepreneurs.

Policy-based Support for Conducive Business Climate

The government-formulated SME Policy 2019 aims to increase the SME sector’s share of GDP from 25% to 32% by 2024, aiming to improve the SME business environment by increasing the scope of institutional funding for the SME sector, adopting ICT-based technology, developing marketing strategy and establishing SMEs as backward linkages of large industries. The pandemic has brought the inadequate business environment and non-adoption of digital support in the SME sector into stark relief.

The government has announced a stimulus package of USD 8.56 billion, equivalent to 2.52% of the country’s GDP, of which USD 2.35 billion is to be allocated to small and medium enterprises, including cottage industries. The government has given assurances that transparent loan disbursement and cooperation with microfinance institutions will make the stimulus packages more effective. Without a proper distribution policy for these stimulus packages, the enterprises which need support the most will never be able to access them. One way to speed recovery from the crisis would be a digital transformation of the economy, initiating a smart digital transformation engagement with MSMEs in specific regions. This may include integration with digital supply chains, digital financial solutions and access to digital credit. Embracing digital financial inclusion will ease mobility constraints caused by the pandemic.

Fiscal Support through Tax Waivers and Priority Allocations

Considering the adverse financial situation facing the CMSMEs, the Ministry of Finance should consider raising the FY20-21 tax-exempted yearly turnover limit for SMEs from USD 0.05 million USD to USD 0.11 million 5 million BDT to 10 million BDT. The Ministry of Finance could include a waiver of value added tax (VAT) at the domestic stage for the period of July-September 2020; deferred payment of quarterly advance income taxes for July-September quarter of FY 2020-21, and payment of corporate taxes for FY 2019-20 by instalments till March 2021. Companies which are incurring losses in FY 2019-20 may be
allowed to ‘carry back losses’ against taxable profits for the two previous years.

The Ministry of Industry was not accorded priority in budget allocations over recent years; indeed, its share in total budget allocation has been declining over the years - from 0.48% of total budget in FY16 to 0.29% in FY20. The annual development program (ADP) projects related to the development of the SME sector need priority in the budgetary allocations, and timely implementation. Given the demand, allocations for SME-related projects need to be increased.

Financial Support for Credit Accessibility

Financing SMEs is vital for the development of the enterprises. Banks and non-banking financial institutions (NBFI) altogether have disbursed an amount of USD 13.62 billion against 512,539 SMEs in 2018 (Up to September). On the other hand, 46,162 women-led SME enterprises received financing of USD 0.48 billion in the same period from Banks and NBFI (Bangladesh Economic Review 2019). During the first half of 2019, cumulative loan disbursements from the financial sector from January to June 2019 to 402,008 CMSMEs throughout the country is USD 9.42 billion. Of these, 29,587 were women-owned enterprises, which received 7.35% of the total CMSMEs loans. Also, out of 65,350 new enterprises, 10.45% are new women entrepreneurs.

The government has announced a stimulus package of USD 2.35 billion, of which USD 1.17 billion is exclusively allocated for SMEs as credit line facility at a subsidized interest rate of 2%. Of the total package, the share of micro and small industries would be 70% and the remaining 30% would go to medium-sized industries. SMEs would get a working capital loan at 9% interest with a 5% subsidy. How these packages are being distributed is a matter of concern.

Most of the enterprises are unable to access to the loans provided by the banks and the NBFI due to the existing clientelist culture and as a result, the pandemic has resulted in creating shortage of cash flow to the entrepreneurs. Increasing cash flow is the most important factor in the survival of the SMEs. To do so, effective and corruption-free ‘loan packages’ ought to be provided from which they can borrow at a low rate of interest. Repayment of loans can be made more tolerable and easier. Interest-free loans and other cash buffers to pay workers and keep store fronts open are much essential and should be dispensed. Concessional loans can be supplied by the inclusion of the microfinance institutions to have a wider reach in providing credit. Refinancing and providing capital at minimum cost to the marginalized SMEs and ensuring better access to finance are the need of the hour.
Specialized Support for Women Entrepreneurs

To ensure loan facility for women entrepreneurs, at least 15% of the total Small Enterprise Refinance Scheme has been allocated for them at an interest rate cap of bank rate + maximum 4% spread (currently maximum 9%). In order to mainstream women in economic activities, banks and NBFIIs have been instructed to provide credit to new women entrepreneurs under cottage, micro and small sectors. (Bangladesh Economic Review 2019).

5% of the credit of the announced stimulus package of USD 2.35 billion 200 billion BDT, of which USD 1.17 billion 100 billion BDT is exclusively allocated for SMEs as credit line facility at the subsidized interest rate of 2%, would also be distributed to women entrepreneurs.

Interest free loans to the small and medium women enterprises and concessional loans at a one-to-two percent interest rate may aid women entrepreneurs in recovering from the losses. A higher allocation of stimulus funds would improve the chances of survival for women-owned enterprises. The government should embark upon ICT-based capacity building for women entrepreneurs. This may include providing digital, virtual, and mobile-based business training, coaching, and mentoring related to economic recovery, digital marketing and communication channels, and overall digital financial literacy.

In order to address the massive changes of the post-COVID era, mobilizing CMSMEs and start-ups is one of the major tasks necessary to recover the economy. With the objectives of employment creation, product diversification, value addition for economic growth, supporting the stability and sustainability of the CMSMEs is a must for the government. Rigorous policy formulation and institutional follow up is vital to prevent a drastic economic decline.
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Dr. Rashed Al Mahmud Titumir is a Professor of Economics at the Department of Development Studies of the University of Dhaka. He has worked in diverse constituencies, namely, academia, governments, think-tanks, international organizations and media. He is engaged in research for pioneering approaches to developmental public policies and innovative solutions on the ground. He has led numerous projects for diverse organizations including governments, development partners and international organizations at home and abroad. Prof. Titumir holds Ph.D. in Economics from the University of London, M.Sc. in Development and Financial Economics from the University of London, Certificate in Trade Policy and Commercial Diplomacy from the Universities of Carleton and Ottawa, BSS (Hons.) from the University of Dhaka, and HSC and SSC from Jhenidah Cadet College. As a senior staff member and a senior advisor, Dr. Titumir has working experience with international organizations, civil society and NGOs in multicultural, multinational and diverse environments at home and abroad. He has provided advisory services to governments on multilateral negotiations such as WTO, UNFCCC, UNCBD. He has been contributing as a member of committees of experts of different UN bodies. Professor Titumir is on boards of different organizations and is the founding Chairperson of the Unnayan Onneshan, a multidisciplinary independent think-tank. He served on the Syndicate, the decision-making body of a university, and was Joint Secretary General of Bangladesh Federation of University Teachers' Association. He also has taught at the Royal Holloway, University of London and the Bangladesh Open University. He also acts as an Independent Director in publicly traded private companies and Member of Board in different social welfare organizations. He has written books and articles on implications of structural adjustment, poverty reduction strategies, world trading system, regional economic cooperation, climate change, and in the areas of state formation, macroeconomic and sectoral policies, agriculture, biodiversity, education and health. Prof. Titumir is currently researching on ideas of state and policymaking in developing countries, focusing on five areas, namely expansion of productive capacity, fiscal and monetary policies, social policies, natural resource management, and agrarian transition.