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RURAL INDUSTRIES STUDY PROJECT

Case Study No. 4

INSTITUTIONAL FINANCING FOR RURAL INDUSTRIES IN BANGLADESH

by

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FOREWORD

The Bangladesh Institute of Development Studies (BIDS) carries out basic research on problems of development in Bangladesh. It also provides training on economic analysis and research methodology to the professional members of its staff and to members of other organizations concerned with socio-economic analysis and planning.

The present study on rural industries of Bangladesh was undertaken by the Institute to fill the gap in knowledge relating to this sector to facilitiate policy planning and project development. The research project, called Rural Industries Study Project (RISP), has been implemented under contract with the Bangladesh Small and Cottage Industries Corporation (BSCIC), coordinated by Bangladesh Planning Commission, and funded by the United States Agency for International Development (USAID). I wish to record our gratitude to these organization for their assistance and cooperation.

The results of the study are being put out in a series of reports; some of them are already available and others under preparation. This case study on Institutional Financing of rural industries is one of several that have been undertaken within the framework of the above mentioned study project.

The importance of a case study on finance lies in the fact that lack of adequate credit poses a critical bottleneck to sustained development of rural small scale and cottage industries which provide employment and income earning opportunities to large numbers of the rural poor, particularly the landless and the marginal farm families. Given comprehensive credit policies and an appropriate restructuring of the existing institutions administering such policies, the SSCIs may be made a viable and expanding source of employment and income in rural Bangladesh.

This report has discussed problems facing the SSCIs in raising credits from the existing financial institutions and highlighted issues relevant to appropriate restructing of the existing policies and institutions towards more meaningful directions.

Since the surveys were conducted over a long period of time the respondents had to spend lot of time to supply the information during repeated visits by investigators. The co-operation of local leaders, businessmen and officials facilited the data collection process. Our sincere thanks are due to all of them. The BIDS staff members engaged either full time or part time in RISP and all temporary employees of the project have worked hard to complete the study successfully and fruitfully.

BIDS, Dacca
20 October 1981

Monowar Hossain
Chairman, BIDS

PREFACE

The Rural Industries Study Project (RISP) was initiated in 1978 with the broad objective of generating detailed information on rural industries of Bangladesh relating to their technolgical, institutional, infrastructural, supply, marketing, management, linkage, cultural and socio-economic characteristics and setting, with a view to ascertaining their potential for growth, identifying constraints and problems, and preparing recommendations for formulation of policies, building of institutions and development of projects. The study is mainly based on surveys conducted in 11 thanas. A census of industrial enterprises was first mounted in the selected thanas; and then in-depth surveys on various aspects of rural industries have been conducted using a suitably selected sample of enterprises representing various industries. A report was prepared on the basis of census results (Phase I Report, May 1979), and an Interim Report was also prepared using information generated in Phase II in-depth surveys (Phase II Interim Report, March 1980). The other completed or planned reports include Phase II Final Report and a number of case studies on both specific industries and specific issues. In so far as the case studies are concerned information has also been generated from secondary sources and surveys conducted outside the selected thanas as deemed necessary in each particular case.

This case study, Institutional Financing for Rural(Small Scale and Cottage)Industries in Bangladesh, has been prepared by Momtaz Uddin Ahmed, Visiting Scholar to the BIDS and Research Associate, RISP, within the framework of RISP. However, it should be recognized that the efforts of all those who have worked in RISP in various capacities have either directly contributed towards, or facilitated, the preparation of this report

The report has critically assessed effectiveness of the present institutional arrangements geared to financing the credit needs of rural industries in Bangladesh with a view to providing a basis for necessary restructuring of the existing credit policies of the concerned agencies in such away as to help/ ease access of the rural industrial entrepreneurs to the formal credit market. We trust the findings of the study will enable the policy makers to identify the constraints and problems facing the SSCIs in so far as borrowing from the formal as well as informal credit markets is concerned and find appropriate solutions to tackle them.

Inadequate flow of institutional credit is found to have severely handicapped the growth and sustained development of rural industries in Bangladesh. Both Small and Cottage Industries have been found to suffer from restricted access to institutional sources of credit. In fact there is no provision

for cottege industries although they constitute the major segment of the rural industries. Absence of a comprehensive credit programme, inappropriate organizational structure of the credit giving agencies and their time-honoured security oriented lending policies appear to have been primarily responsible for the restricted flow of institutional credits to the rural industries. It is thus the contention of this report that in order to make rural industries a viable and expanding source of employment and income in Bangladesh serious afforts should be made to intensify institutional credit facilities for these industries through formulating comprehensive credit policies and developing an appropriate institutional network for implementing and administering such policies.

It is hoped that the report will be found useful by concerned project implementation agencies and policy makers, and interested analysts. Comments intended to contribute towards improving the value of the report will be welcome.

RISP, BIDS
Dacca
20 October 1981

Qazi Kholiquzzaman Ahmad
Research Coordinator
Rural Industries Study Project

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The generous co-operation extended by the officials of the nationalized commercial banks, other relevant agencies and organizations, and the entrepreneurs in supplying the information required for preparing this case study, is gratefull acknowledged. Thanks are also due to those colleagues and other staff members of RISP/BIDS whose assistance facilitated the completion of this study.

My special thanks are due to Mr. Taufique Ali, Mr. Sadrul Alam and Mr. Abdus Samad of RISP, who took painstaking troubles in collecting and processing the data. I am thankful to Dr. Zaid Bakht and Dr. Mahabub Hossain, Research Associates and Assistant Research Coordinators of RISP, who gave me time to have stimulating discussions with them on various issues.

Finally, I would like to express special gratitude to Dr. Q.K. Ahmad, Co-Director and Research Coordinator of RISP, who offered inspiring guidance, kindly read through an earlier draft of the report and made valuable comments and suggestions for its improvement.

MOMTAZ UDDIN AHMED

CONTENTS

CHAPTER

1. INTRODUCTION
   - 1.1 The Problem Setting
   - 1.2 The Purpose of the Study
   - 1.3 Definition of Small-Scale and Cottage Industries
   - 1.4 Survey Methodology and Data
2. THE SSCIS, PROMOTIONAL AGENCIES AND THE SPECIALIZED FINANCIAL INSTITUTIONS
   - 2.1 Institutional Network
   - 2.2 Bangladesh Small and Cottage Industries Corporation
   - 2.3 Bangladesh Shilpa Bank
   - 2.4 Bangladesh Shilpa Rin Sangstha
   - 2.5 Investment Corporation of Bangladesh
   - 2.6 Department of Industries
3. THE NATIONALIZED COMMERCIAL BANKS AND THE SSCIs LOAN PROGRAMMES
   - 3.1 The Small Loans Scheme
   - 3.2 The Special Credit Programme
   - 3.3 The NCBs and Other Credit Programmes
4. THE ENTREPRENEURS' VIEWS OF THE LENDING AGENCIES
   - 4.1 Entrepreneurs' Perception about the Financial Constraints
   - 4.2 Sources of Funds Used by the SSCIs for Financing Initial and Expansion Capital
   - 4.3 Factors Responsible for Limited Use/Availability of Institutional Loans - the Entrepreneurs' Views
5. SUMMARY, CONCLUSIONS AND POLICY RECOMMENDATIONS
   - 5.1 Summary of Findings
   - 5.2 Conclusions and Policy Recommendations

Chapter I
INTRODUCTION

1.1 The Problem Setting

The importance of a case study on financing rural small-scale and cottage industries (henceforward abbreviated as 'SSCIs') of Bangladesh hardly needs to be emphasized. In conditions of widespread unemployment and underemployment obtaining in the rural areas of the country and the rather limited scope for further expansion of employment in the backward agricultural sector, rural non-farm activities, particularly rural industries, assume a crucial significance as sources of employment and income for the rural poor. In so far as employment is concerned, the 1974 census data indicate that urban industries account for about 30 per cent of the total industrial labour force in the country, while rural industries take care of about 70 per cent. It may be noted here that rural industries, for all practical purposes, imply rural small-scale and cottage industries as the industries (defined to include manufacturing activities and repairing of manufactured goods) located in the rural areas are by and large small-scale and cottage type enterprises[1]. Again, while there are small-scale and cottage industries in urban areas also, the bulk of such enterprises in the country are located in the rural areas[2].

That these two sub-sectors of the economy together constitute the dominant source of non-farm employment generation in the countryside is also supported by the findings of the

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[1] This has been revealed by recent empirical studies in Bangladesh (IBRD, 1973) as well as in Africa (Liedsholm and Chuta, 1976).

[2] The African as well as the Bangladeshi study mentioned earlier indicated that well over 70 per cent of the total small-scale and cottage industries in these two countries operate in the rural and semi-urban areas.

Phase I survey of the RISP in respect of their relative contribution to employment of labour force in the eleven thanas of Bangladesh covered by the survey. It was found that while about 25 per cent of the total rural labour force of all the eleven thanas under study were employed in rural industries, this proportion varied between different thanas rising upto 55 per cent for Narsingdi. The contribution of these industries to industrial output is also commendable. For example, the rural small-scale and cottage industries were found to contribute 45 per cent of the officially reported total value added (Tk.9179 at current prices) contributed by the manufacturing sector in the country as a whole during 1977/78 (RISP, February 1981.) However, despite making significant contributions to national employment and output, these industries suffer from a critical shortage of necessary inputs.

Of the various constraints facing the rural industries, inadequate flow of credit particularly from the institutional lending agencies is commonly believed to be a crucial bottleneck impending their growth and expansion in Bangladesh[1] (H. Rahman, 1979; World Bank 1978) as well as other developing countries (Berna, 1980, Devenport 1967, Dunlo 1971, Ahmed 1976 and Steel 1977).

Those identifying lack of finance as a handicap facing the SSCIs, usually stress three major factors in support of their claim. First, small entrepreneurs often perceive finance to be one of their key bottlenecks when asked about their problems.

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[1] While non-availability of institutional credit is recognized as a major constraint facing the rural industries sector in Bangladesh . Bangladesh in general, it is assumed to be more serious for the cottage that for the small-scale industries. For the latter, the problem is regarded to be the lack of knowledge about availability of credit and procedural difficulties in obtaining it and not lacl of credit as such as in the case of the cottage industries. The observation remains to be verified in relevant sections of the subsequent analysis.

Second, funding of such enterprises both at foundation and during subsequent expansion is done mostly out of personal savings accumulated from the proprietors' previous occupations and through reinvestment of profits (Ahmed 1976, Liedholm and Chuta 1976 and Steel 1977). The limited use of credit by smaller enterprises is taken as evidence of their restricted access to sources of credit. Third, whatever little credit is used comes mainly from the informal sources (i.e. friends and relatives, money lenders, and input suppliers) which charge much higher rates of interest compared to formal sources. This leads to the observation that small-scale and cottage type enterprises are denied adequate formal credit and hence, are forced to depend on the informal sources of credit

Contrary evidence is also available (Schatz 1965 and Harper 1975), the general observation being that there is no shortage of capital for the SSCIs. The problem is identified to be rather limited availability of viable projects. It is even suggested by some (Harper 1975) that if financial assistance is preceeded by managerial advice ensuring efficient utilization of the limited funds, it may reveal that the perceived shortage of capital is largely artificial.

It is in the light of these controversies as well as the vital importance of the rural industries sector in the national economy of Bangladesh that an in-depth case study on institutional arrangements for financing the SSCIs in the rural areas of the country has been undertaken.

1.2 The Purpose of the Study

The purpose of the study is to evaluate effectiveness of the present institutional arrangements for financing the credit needs of the rural industries in Bangladesh with a view to providing a basis for restructuring the programmes and policies of the institutional lending agencies in such a way as to ease access of the rural industrial entrepreneurs to the formal credit

market. In achieving this broad objective, the study seeks to examine the present institutional set-up geared to financing the SSCIs focussing particulary on the mode of operation and orientation of the relevant institutional lending agencies towards servicing the credit requirements of the SSCIs vis-a-vis their large counterparts. The type of credit needed by the SSCIs, sources used, terms and conditions faced and the relative costs incurred in raising them from various sources are also analysed. Analysis of these issues will enable us to identify the constraints and problems facing the SSCIs in borrowing from the formal as well as informal credit markets and make recommendations for formulation of policies, creation of separate financial institutions and/or restructing the existing ones for solving the financially related problems of the SSCIs.

The issues analysed in the study are presented in five chapters. Chaper 2 starts with an introduction to the institutional network geared to promoting small-scale and cottage industries in Bangladesh. A critical review of the organizational structure and activities of various specialized agencies responsible for financing the SSCIs then follows. The mode of operation and the degree of orientation of the concerned agencies in meeting credit needs of the SSCIs vis-a-vis their large scale counterparts constitute the main theme of analysis in this chapter.

The extent of involvement of the NCBs in financing the SSCIs in Bangladesh is examined in chapter 3. While the NCBs now operate a number of credit programmes in order to meet the credit needs of the SSCIs, our main focus has been on the Special Credit Programme (SCP) of Tk. 6 crore, introduced by the Bangladesh Bank in 1978. The main issues that have been analysed to assess the performance of SCP in meeting the credit requirements of the SSCIs include loan appraisal procedures, sanction, disbursement and recovery position of loans advanced under the programme. Analysis of these and other relevant issues bearing

on the operation of the SCP has been carried out in extensive details in order to facilitate appropriate restructuring of the programme, ensuring its effective continuation and future expansion. Attempts have also been made in this chapter to present and analyse the views and experience of the bankers in administering small loans programmes and the difficulties faced by them in supplying credits to the SSCIs.

The views of a large sample of small industrialists, operating in the rural areas of the country, about the formalities and problems involved in borrowing from the institutional lending agencies have been presented in chapter 4. The analysis in this chapter has been divided into two parts. In part I, the perception of the sample entrepreneurs about the financial constraints, type of credit needed by them to finance their operations, extent of their dependence on borrowed funds and costs incurred in obtaining such funds from the available sources have been analysed with a view to identifying their requirements for type of credit and their degree of accessibility to the existing institutional lending agencies supplying such credits.

The perceptions of the borrowers about the difficulties involved in getting institutional loans and the problems and complicacies actually encountered by them in obtaining such loans have been analysed in part II. Thus, the study having been built on the contignous views of the borrowers as well as the lending agencies about the problems involved in borrowing and lending is expected to correctly identify the forces underlying any disequilibrium (and the reasons thereof) that may exist between the demand for and supply of institutional credit and find appropriate solutions to tackle them.

The final chapter draws together the major findings and discusses their implications for policies.

1.3 Definition of Small-Scale and Cottage Industries

In making provision for better financial services to the SSCIs, a precise definition for them is needed with a view to distinguishing them clearly from their large counterparts. This is particularly important in developing countries like Bangladesh where the promotional incentives are bent more towards favouring the large-scale enterpirses and discriminating against the smaller ones. Unfortunately, there does not exist a universally acceptable definition for the SSCIs. While the definitions adopted often depend upon the objectives pursued by the analyst and the promotional agencies, there are well known ambiguities and measurement problems associated with various criteria (i.e. employment, value of capital and so on) chosen to define the size of an enterprise[1].

For purposes of the present study, the employment criterion has been used to differentiate small and cottage industries from large ones. Small and cottage industries together have been defined in this study to include all enterprises with employment size upto 50. As the sample enterprise in the present study are located in the rural areas and use relatively simple technologies, the difference between their sizes may arise with respect to employment size rather than technology or capital intensity.

Finally, the various criteria often used to distinguish cottage from small industry generally emphasise two basic characteristics of cottage industry, namely, predominance of family labour and extreme smallness of size. Incorporating these two features, cottage industry in this study has been defined as (i) any industrial unit with three or fewer workers or (ii) any establishment with 10 or fewer workers employing at most two hired workers.

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[1] For details on this point see, RISP Phase II Interim Report, Bangladesh Institute of Development Studies, March, 1980, pp.1-3.

1.4 Survey Methodology and Data

Data used in the present study came from two main sources(i) Phase II survey of a sample of small-scale and cottage industry units conducted by the Rural Industries Study Project (henceforward abbreviated as RISP and called the 'Core Study') and (ii) a special survey of a sample of commercial bank branches including their head offices and other specialized, government and semi-government organizations and agencies (i.e. Department of Industries, Handloom Board, Sericulture Board, BSCIC, Regional Development Boards, and so on) directly or indirectly involved in providing financial assistance to the SSCIs. This two-pronged approach based on information gathered from the recipients as well as from the suppliers of credit has been adopted with a view to identifying correctly the forces underlying any disequilibrium between the demand for and supply of credit. As a study so designed will be based on the contigous views of the parties on either side of the credit market, may enable us to make an acurate diagnosis of the problems and find appropriate solutions[1].

The information on the demand aspects of SSCIs financing (i.e. sources of credit used by the respondents, terms and conditions attached to them and problems of accessibility etc.) were collected from 1300 respondents through administering a predesigned questionnaire in eleven thanas of Bangladesh covered by the Core study. The eleven thanas, namely, Barlekha (District Sylhet), Chandanaish (Chittagong), Kaunia (Rangpur, Muradnagar (Comilla), Pabna Kotwali (Pabna), Sherpur (Jamalpur, Shibganj (Rajshahi) and Swarupkati (Barisal) were selected purposively bearing in mind the considerations of regional balance, general

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[1] Indeed, compared to most other studies in the field based either on the views of the lending agencies (S.P. Schatz 1965) or on those of the borrowers only (i.e. J.J. Berna 1960, Liedholm and Chuta 1976, Dunlop 1971, Steel 1977) the present study will have a much greater analytical strength in resolving such issues as whether or not the problem of finance identified by the small entrepreneurs is apparent or real.

concentration or rural industries, concentration of key industries, technique or production, accessibility and so on. The selection of enterprises was done on the basis of random sampling from the sample frame assembled through Phase I survey of the Core study. The size of the sample was dictated by the considerations of resource availability. Allocation of sample enterprises among different thanas and that within each industrial thana among different industries was done respectively in proportion to the number of industrial workers recorded in respective thanas and in proportion to the number of workers in broad industry groups within each thana[2].

Concerning the supply aspects of SSCIs financing, one needs to identify the institutions and agencies providing financial services to such enterprises. Among other relevant issues on the supply side, the distributive channels of the relevant institutions, their extent of involvement in terms of geographical coverage as well as share of SSCIs financing in their total lending operations, their lending procedures and the difficulties faced by them in dealing with the small borrowers are important. As it was not possible to collect these information through the questionnaire administered by the Core study because of its already voluminous length, a separate survey of a sample of the relevant institutions and agencies dealing with small industry financing was undertaken to fill the gap. The kind of information collected through the special survey is contained in the unstructured questionnaire appended to the study.

A number of institutions and organizations provide credit in varying degrees to the SSCIs in Bangladesh. The notable among them are the Bangladesh Small and Cottage Industries Corporation (BSCIC), commercial banks, specialized banks,

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[2] For further details on thana and enterprise selection procedures, one may see RISP Phase I Report, May 1979 pp.12-14 respectively.

district and divisional development boards, Department of Industries, cooperatives, and government and private foreign donor agencies, and international organizations. Of these, BSCIC and the Commercial banks have continued to dominate the scenario of SSCIs financing in one way or the other with other agencies playing by and large a complementary role.

BSCIC, by its functional characteristics, is primarily responsible for promoting the SSCIs. The commercial banks with their extensive branch networks, knowledge about local conditions, and easy access to the rural entrepreneurs in the remote corners of the country, are in a better position to meet the short-term financial requirements of the SSCIs.

Further the Bangladesh Shilpo Bank (BSB) and the Bangladesh Shilpo Rin Sangstha (BSRS) constitute the main source of long-term loans for the industrial sector of Bangladesh. In evaluating effectiveness of the institutional arrangements for financing the SSCIs, we shall thus concentrate mainly on BSCIC, the commercial banks and the specialized financial institutions directly involved in small industry financing.

The six commercial banks engaged in industrial financing operate through a large number of branches widely scattered over the entire country. A complete enumeration of all of them will itself constitute a major independent study. We, therefore had to make a purposive selection of 31 branches in addition to their six parent commercial banks and the two specialized banks. The criteria for selecting the sample has been as follows.

A minimum of one bank has been selected from each of the eleven survey thanas in view of the consideration that views of the entrepreneurs of the survey thanas regarding bank credits could be juxtaposed with those of the lending banks regarding their customers. This will also fulfill indirectly two important additional criteria i.e. that of striking a regional balance and

of inclusion of the thanas with concentration of rural industries as both of these important criteria were followed while making thana selection by the Core study. Indeed, this has also stretched the coverage of the study well upto the village level where institutional credit for industrial financing is most lacking.

We then selected a minimum of one bank from each of the twenty districts. The important underlying consideration was to include in the sample the "Lead Bank" of the district responsible for disbursing the loan funds to the small-scale and cottage industries under the "Special Credit Programme" of Tk.6 crore (enhanced to Tk. 11.45 crores subsequently) introduced by the Bangladesh Bank in February 1978. Under this scheme, one of the six commercial banks in each district was designated as 'Lead Bank' (by the Bangladesh Bank) to disburse the allocated loan funds in the district.

Inclusion of the special credit programme operations of the commercial banks over and above their normal involvement in small and cottage industry financing (through the Small Loans Scheme) in the study will provide deeper insights into the institutional arrangements for financing the SSCIs. These two criteria together gave us a sample size of 31 branches of the commercial banks in addition to six parent banks, the Bangladesh Bank, the BSCIC, specialized lending agencies, co-operatives, government departments and organizations engaged directly or indirectly in industrial financing. The sample frame as well as the size thus being reasonably broad in coverage, should enable us to shed enough light on the prospects and problems of institutional arrangements for financing the SCCIs in Bangladesh.

Chapter 2

THE SSCIs PROMOTIONAL AGENCIES AND THE SPECIALIZED FINANCIAL INSTITUTION

2.1 Institutional Network

The importance of small-scale and cottage industries sector in the national economy has been stressed in official documents and speeches of the national leaders ever since the days of Pakistani regime. Policy measures were also adopted from time to time including institutional arrangements, fiscal incentives and provison for finance to promote growth and development of these industries. The promotional measures undertaken were eventually integrated into the framework of industrial policy and institutional arrangements were made to implement these policies.

At present, a number of government and semi-government agencies and voluntary organizations are engaged directly or indirectly, in varying degrees in promoting small-scale and cottage industries in the country. These are :

Bangladesh Small and Cottage Industries Corporation (BSCIC)
Department of Industries (DI)
Bangladesh Handloom Board (BHB)
Bangladesh Handloom Goods Marketing Corporation (BHGMC)
Bangladesh Sericulture Board (BSB)
Divisional Development Board (DDB)
Chittagong Hill Tracts Development Board (CHTDB)
Directorate of Social Welfare (DSW)
Co-operative Department (CD)

Bangladesh Womens Rehabilitation and Welfare Foundation(BWRWF)
Export Promotion Bureau (EPB)
Trading Corporation of Bangladesh (TCB)
Bangladesh Standards Institution (BSI)
Bangladesh Industrial and Technical Assistance Centre(BITAC)

Bangladesh Council for Scientific and Industrial Research (BCSIR)
Bangladesh Management Development Centre (BMDC)
Central Testing Laboratories (CTL)
Industrial Advisory Centre of Bangladesh (IACB)
Investment Corporation of Bangladesh (ICB)
Bangladesh Shilpa Bank (BSB)
Bangladesh Shilpa Rin Sangstha (BSRS)
Nationalized Commercial Banks (NCBs)

In addition a large number of international official agencies (i.e. ADB, DANIDA, IDA, ILO, NORAD, SIDA, UNDP, UNICEF, USAID) and private organizations (i.e. CARE, CONCERN, HEED, World Vision of Bangladesh and so on) are also engaged in various capacities in promoting the growth of small-scale and cottage industries in Bangladesh[1]. A discussion of the activities of these agencies is outside the scope of this study. The assistance provided by the official agencies usually consists of financial grants for specific small and cottage industry projects. In contrast, the private voluntary organizations provide training facilities for development of artisan skills in different lines of small-scale activities and undertake small projects in both production and marketing with a view to creating jobs for the distressed people.

Of the various national agencies and organizations, BSCIC is the pioneering institution involved in promoting the SSCIs sector. Its promotional assistance comprises wide ranging issues like financial, technical, managerial and advisory services. Next to BSCIC, BSB and the NCBs are the important sources of finance for the small industry sector. Department of Industries, Bangladesh Shilpa Rin Sangstha and the Investment Corporation of Bangladesh, though play important role in the development of

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[1] For a comprehensive account of such agencies and organizations see, Clarence Malony, RISP Special Report No. 1. (Revised) June, 1979.

industries in the private sector, their involvement in SSCIs promotion is only indirect and hence difficult to be assessed. All the remaining organizations are also involved in small and cottage industry development in the country in one way or the other. Their activities relate to wide ranging aspects like training for development of artisan skills, marketing of small and cottage industry products and so on and have thus important bearing on the development of this sector. However, as the promotional services provided by most of such organizations are only incidental to their main operations and are also non-financial in nature, a review of their performance falls outside the purview of the present study[1]. Given that the purpose of the study is to evaluate institutional arrangements for financing the SSCIs in Bangladesh, we shall analyse the activities of those agencies at length which are responsible for financing the sector.

2.2 Bangladesh Small and Cottage Industries Corporation (BSCIC)

BSCIC, formerly known as East Pakistan Small Industries Corporation (EPSIC), was established in 1957 for promoting small and cottage industries in Bangladesh. Since then, it has been the key agency with an autonomous status to assist the growth of the small industries sector. Funded mainly by government grants, it also receives financial grants from different international donor agencies and foreign government agencies to be able to provide developmental assistance to the private investors.

Organizational Set-up

During its 24 years of existence since 1957, the organizational set-up of the BSCIC underwent major changes from time to time in response to demands of the circumstances[2]. For example,

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[1] For a brief introduction to the activities of the institutions involved only indirectly in the promotion of the SSCIs, the reader is referred to Rahman, H. et. al. (1979).

[2] For details in this respect see, Rahman, H. et. al. op. cit., chapter 3.

a major organizational change was introduced in the Corporation in 1973, bifurcating it into two separate bodies, namely, BSIC (Bangladesh Small Industries Corporation) and BCIC (Bangladesh Cottage Industries Corporation). Under the new arrangements, BSIC was responsible for assisting the small-scale industries and BCIC was entrusted with the task of promoting the cottage industries in the country.

None of the two Corporations could, however, function satisfactorily because of lack of autonomy, shortage of qualified and experienced personnel and a lack of motivation of the staff arising from their dissatisfaction with the changes introduced. Hence, in view of the chaos created by the above circumstances, the two corporations were again merged into a single agency in January 1976 leading to the emergence of BSCIC which started operation from March 16, 1977.

In its new form, the corporation is under the control of the Ministry of Industries and acts as an autonomous organization subject to policy-guidance by other government departments (i.e. Department of Industries) from time to time. It is managed by a Board of Directors comprising 6 members (including the Chairman as the chief executive) appointed by the government. The corporation has five functional divisions: Finance, Planning and development, Projects and Industrial Estates, Design and Handicrafts and an Administrative division; each headed by a full-time Director.

The Corporation has four regional offices located at four divisional headquarters namely, Dacca, Rajshahi, Chittagong and Khulna. These regional offices may be treated as branches of the central organization in that they perform similar functions as directed by the head office. In addition, they manage 18

industrial estates and operate pilot projects located in different parts of the country.[1]

Functions:

During initial years, the main function of the BSCIC has been to assist the growth of SSCIs through developing infrastructural facilities for private sector industries, providing technical assistance and advisory services, financing industries in the private sector and setting up industries in those lines where private initiative was lacking.

Promotion of SSCIs remaining the basic objective, the functions of the BSCIC underwent considerable changes over time. A review of BSCIC activities over time indicates that in the initial years, the corporation concentrated primarily on commercial activities like import of machinery and rawmaterials, distribution of such imports among the private investors and supply of small local currency loans for purposes of meeting fixed and working capital needs of the small entrepreneurs.

However, a gradual shift of emphasis from commercial to promotional activities in the functioning of the corporation occured during 1960s with the establishment of Small Industry Advisory Services (SIAS) in 1965. The promotional activities carried out under the scheme include identification of projects in new areas of investment, project appraisal, preparation of investment briefs, selection and procurement of machinery and rawmaterials for the investors and counselling and guidance to the entrepreneurs on operational problems. After reorganization

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[1] Yet another new dismension to BSCIC's organization and functioning has been added through creating twenty District Industries Centres (DIC) in tweenty districts, primarily for looking at the development and promotion of the SSCIs at the district level. The DIC - in charge is expeeted to work in close co-operation with the District Manager in each district, who is incharge of managing the industrial estates.

of the corporation in 1977, these promotional activities are performed by the Counselling and Industrial Studies Department (CISD). Through 1973 to 1976 and thereafter the promotional services offered by the BSCIC were further extended and promotion schemes like industrial estates, services and common facility centres, rural industries service, design centre and development of sub-constracting and so on were undertaken.

The scope of BSCIC's activities was further enlarged over time also on the commercial side with addition during 1973-1976 of such responsibilities as making provision for loans in foreign currency, sponsoring and licensing of new industries in the private sector and distribution of yarn to the weavers (the latter being) discontinued in 1977 and handed over to the Handoom Board subsequently). Needless to point out, a single organization having so much to do may hardly be expected to perform all its functions in an effective manner. However, as our purpose is to evaluate BSCIC's activities geared to financing the SSCIs, we turn to analysing these issues next.

Financial Operation of the BSCIC

BSCIC has been extending financial assistance to the SSCIs under three separate loan programmes:

a) BSCIC lending programme from its own resources;
b) BSCIC lending programme in association with BSB;
c) BSCIC loan operations in association with the consortium of commercial banks.

A brief review of the lending operations conducted under these three different programmes is attempted to highlight the nature and extent of financial support services offered by BSCIC to SSCIs.

BSCIC Loan Programme:

The programme started in the fiscal year 1957-58 with an initial authorised capital of Tk. 0.75 million which was latter raised to Tk. 5.75 million in 1961 by the then East Pakistan Provicial Government. The purpose was to enable the Corporation to meet specific requirement and special needs of the small investors through revolving re-use of the repaid loans.

Loans sanctioned under this Programme were in local currency (with no foreign exchange component) mainly for purposes of constructing factory building, buying local machinery and procuring local rawmaterials. Normally, no loan for working capital would be sanctioned under this programme, although provision was there to allow 25 per cent of the total loan to be used for working capital purposes in exceptional circumstances.

The duration of the loans was for five years with an average interest rate of 7 per cent per annum and was repayable in half-yearly instalments. Compared to other programmes, loans available from BSCIC's own fund were more popular among the borrowers, because the borrowers equity (25%) and documentation requirements were minimum.

The Corporation being the sole authority for appraisal and approval could process the loan applications quickly and disburse the funds expiditiously, usually within 2 to 4 months. The other positive aspect of this loan was that it encouraged the use of indigenous technology through making the loans available only to these borrowers who would use locally produced machinery.

During 18 years from 1957 to 1975, a total of 923 loans were sanctioned under this Programme amounting to Tk.11.6 million with an annual disbursement of Tk.0.64 million (Rahman, H. et. al. 1978). The total volume of lending was thus small because of the fact that the fund made available to the Corporation through government grants was limited.

The recovery position of the loans sanctioned under this Programme is considered unsatisfactory. Out of the total loans sanctioned only 32 per cent could be recovered till June, 1977; 38 per cent are living cases and the rest 30 per cent are considered bad debts. Lack of organized efforts to enforce financial discipline and regularize the accounts is regarded the primary factor responsible for unsatisfactory recovery position of the loans. The subsequent shift in the financial support system from local to foreign currency loans and consequent dependence of the Corporation on foreign credits and grants made its first lending programme gradually non-operative.

BSCIC - BSB Loan Programme:

BSCIC started a second loan programme in 1961 in conjunction with the former IDBP (now BSB) under which loans were available in both local and foreign currencies. A Central Government grant of Tk.5.00 million placed at the disposal of IDBP for small industry financing and the grants (Tk.5.75 million) furnished earlier to the BSCIC by the then Provincial Government together constituted the source of funds for this loan programme. The purpose of loans were the same as under the BSCIC Loan Programme except that the foreign currency component of the loan could now be used for importing machinery from abroad.

Loans sanctioned under this programme also were for a period of 5 years and repayable at half-yearly instalments with 1 year grace period as before. The rate of interest on Taka loan was 7 per cent and that on foreign currency loans varied between 7 and 9 per cent depending on the terms and conditions under which such credits were made available to government by the donor countries. The items of security against the loans comprised registered mortgage on project assets. The equity requirement varied from 30 to 35 per cent depending respectively on whether the enterprise was located in the proprietor's own premise or in the rented premises.

Over nine years from 1963 to 72, a total amount of Tk.25.8 million (comprising Tk.9.7 million in local currency and 16.1 million in foreign currency) was disbursed under this Programme with an annual disbursement of Tk.2.86 million. A BSCIC report (BSCIC, 1969) indicated that the process of disbursement was slow and the average amount disbursed against the loans was much less than the amount requested by the applicants.

Unlike the BSCIC Loan Programme, the BSCIC - BSB joint programme involved lengthly processing, ranging between 8 to 12 months or more depending on whether the loans were in Taka or foreign currency. The documentation requirements of the loans against foreign currencies in particular were so strict and complicated that many borrowers failed to comply. Many of the IDBP loans and the foreign currency loans requiring approval of IDBP's head office at Karachi had to be sent to West Pakistan and involved consequently such larger waiting time as to render the credits unusable to the borrowers. As a result many of the sanctioned foreign currency loans remained unutilized (BSCIC, July 1969). Further foreign credits available from particular donor countries were obtained by the government under terms and conditions unfavourable to the borrowers. Even the local currency loans required considerably longer processing time as decision-making was split between two different agencies with BSCIC processing the applications and BSB making the disbursements.

The procedureal difficulties and lack of clear understanding between BSCIC and BSB as to their relative stake in the drive for recovery left bulk of the loans in arrears for long. A BSCIC handout (BSCIC, 1978) reports the overdue position of the loans sanctioned under this programme to be around 64 percent as on 30-6-77. Lack of effective supervision, inadequate drive and division of risks between BSB and BSCIC (i.e. 25% and 75% respectively) are noted as factors responsible for unsatisfactory recovery position of the joint BSCIC - BSB lending programme.

Because of these problems, the programme was discontinued later in mid 1970.

BSCIC - Consortium of Commercial Banks' Loan Programme:

The BSCIC - Consortium Lending Programme started in 1967 through bilateral agreements reached between BSCIC and the commercial banks with a view to expanding the volume of long term equity capital for small scale industries in both local and foreign currencies. Setting up of new projects and balancing modernization and expansion of the existing enterprises were the main purposes of this joint lending programme.

As per contents of the agreement, BSCIC was to receive loan applications from the private investors, process them after carrying out techno-economic feasibility studies and recommend them to the commercial banks. Commercial banks on the other hand had to examine credit worthiness of the applicants, provide bank guarantees in their favour, sanction Taka loans and assume the responsibility for documentation, disbursement and recovery. Though recovery of the loans was a bank responsibility, BSCIC had to supervise loan utilization and share 50 per cent of bad debts or losses with remaining 50 per cent to be borne by the banks.

Under this programme, loans would be available for a period of 20 years repayable in half-yearly instalments with a grace period of 18 to 24 months, if the borrower could provide 30 per cent of the total project cost. In case of loans against foreign credits received by the government and made available of BSCIC, operation of the loan begins with the pledge of taka component by the commercial banks and submission of bank guarantee to the tune of 30 per cent of the project cost by the applicant.

Initially, the average annual rate of interest varied between 7% and 8% which was 2% and 3% respectively above the

existing bank rates with BSCIC retaining 1% and the Banks 2%. At present, the annual rate of interest charged on the loans advanced under this programme is 11%. The items of security usually comprise registered mortgage on entire project assets and occassionally on equitable mortgage.

During the 10 year period between 1967 and 1977, a total amount of Tk.94.40 million was disbursed under the consortium arrangements with an annual disbursement of Tk.9.44 million. These loans were made available to the borrowers against foreign credits received from the USAID and the IDA and were used primarily for financing imports of machinery and equipment for cold storage plants, automatic rice mills, printing press, bakeries and other allied small industries. Loans for financing working capital requirements were not usually available under this programme. Even if provided under exceptional circumstances, it did nor exceed 25 per cent of the total requirements.

Compared to two previous programmes, the recovery position of the loans advanced under the BSCIC - consortium programme is said to be satisfactory. Out of 149 projects financed by this programme till June, 1977, 45 units are reported to have fully paid their loans and the remaining 104 cases are in the loan portfolio. The repayment of the loans started in different phases during 1969, 1970 and 1975 and was to be completed by next ten years. However, due to set-backs caused to many units by the Liberation War, the repayment schedule has been rephased and it is expected that the outstanding dues of most units will be paid up as per the rephased schedule. Among other favourable features which helped the BSCIC - Consortium arrangements to be relatively more successful than the previous lending programmes, the following are worth mentioning.

The programme containing the provision for loans in both local and foreign currencies had encouraged many entrepreneurs to enter into industry and could generate considerable private investment in the form of equity. Accoring to a BSCIC estimate

(BSCIC, 1969) the programme had the impact of raising the level of investment in small industry to more than Tk.20.0 million a year during 1967 - 68 to 1968 - 69. Processing time on loans through the consortium was reduced to 2 to 4 months as against 8 to 12 months in case of the other loans. Further, careful scrutiny of the project viability and credit worthiness of the borrowers in different phases by both BSCIC and the commercial banks ensured greater efficiency in utilization of the loan funds.

However, the programme was not entirely without deffects. The overall administration of the programme by BSCIC and the commercial banks led to inadequate co-ordination and consequent inefficiencies. For example, there occured discripancies between the estimated and actual taka cost of the project approved and consequently the bank's pledges to meet the local currency requirements fell shorter than needed in many cases. While this resulted in additional commitment of funds by the commercial banks, they found it difficult to block more funds in long term investment than permissible by their liquidity position. In case of inflated project costs, the borrowers also found it difficult to provide the equity and hence to arrive at mutually agreeable terms with the original sponsoring bank. Finally, the projects financed under this lending programme were mostly in the upper range of the small industry definition and were primarily concentrated in one sector, namely, food and allied industries. The relatively smaller units as well as the cottage enterprises were, therefore, left out of the financing stream under the BSCIC-Consortium lending programme.

To sum up, BSCIC provided a total amount of Tk.131.80 million as loans to roughly 1,500 units in the small-scale sector under its various lending programmes upto 1977. Assuming a debt - equity ratio of 70 : 30 on average for all the three loan programmes, BSCIC's financial assistance to the small industrialists appears to have generated an estimated private investment of Tk.56.6 million in the form of equity.

However, so far as recovery position of the loans is concerned all the three lending programmes appeared to have met with only limited success in that roughly 30 per cent of the loans disbursed is reported to have been paid back. Even if the lenders optimism about possible recovery (i.e. to the tune of 70 per cent with the remaining 30 per cent being bad debts) comes true, the large number of outstanding cases indicates lack of organized efforts on the part of the lenders towards ensuring better recovery and that of proper utilization by the borrowers. The reasons underlying these problems facing the financial operation of the BSCIC are not far to seek.

BSCIC, being by and large a promotional agency, lacked in the kind of expertise and dynamism required to meet financial requirements of the small industrialists. For example, till 1969-70, there was no separate division/department in the Corporation for handling the financial operations.[1] More important, lack of adequate funds both in terms of cash foreign exchange and local currencies made the Corporation's lending capacity extremely limited. As BSCIC has always been dependent on grants from the government and various international donor agencies, the magnitude and direction of its lending operations have been influenced by the availability of such grants. Irregular and inadequate availability of loanable funds had thus drastically curtailed the Corporation's ability to meet financial requirements of the small borrowers in any effective manner.

The gradual shift of BSCIC's lending operations from advancing local to foreign currency loans (particularly through the introduction of joint BSCIC-BSB loan programme) had not only made it overdependent on foreign credits (and thus curtailed its lending capacity) but also discouraged the use of local

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[1] At present, the Corporation does not handle any lending operations directly by itself, but participates in the SSCIs lending programmes (i.e. SCP) indirectly through involving in joint appraisal of loan applications and recovery of loans with the NCBs.

resources and local technology by small industrialists. Further, whatever funds were available for disbursement under the BSCIC-BSB lending programme, major portion (96.07 per cent) went to the public sector enterprises falling within the upper range of the small industry definition during the period 1972-75.

The bias against smaller enterprises in the disbursement of funds through the BSCIC - BSB lending programme may be caused by the fact that IDBP, the predecessor of BSB, was geared primarily to financing the larger industrial enterprise. It is thus unlikely that BSB might have developed the kind of organizational set-up at the ground level which is needed for assisting the small entrepreneurs of modest means.

An indirect bias against lending to the relatively small and cottage enterprises was also caused by both the BSCIC-BSB and BSCIC Consortium joint programmes in that they adopted, by and large, a rigid and conventional approach to lending. Their operations appeared to have exhibited urban-orientation, adhearenceto stringent collateral requirements, extensive documentations and cumbersome official formalities. This situation may be improved only if the financial operations of the concerned agencies are decentralized and their present conservative approach to lending is changed for a dynamic and flexible approach guided by missionary zeals ,through seeking to bring the prospective entrepreneurs and investment opportunities together. Whether this can be accomplished by the existing institutional set-up geared to financing the SSCIs or entirely new institutional arrangements are needed for the purpose, will form the main thrust of our analysis in the subsequent parts of the study.

Another important shortcoming affecting all the three loan programmes is that they made inadequate provisions for working capital loans. Given the constant cash-flow problems of the typical small entrepreneurs, this must have adversely affected their operative efficiency.

Finally, the bad recovery position of the joint lending programmes appears to have resulted from the split of responsibilities in areas that are interrelated (i.e. follow-up and collections). Different institutions making decisions on different aspects of a project during appraisal resulted in the institutions blaming each other for mistakes without taking responsibility for failures. Sometimes, lack of a clearcut demarcation of responsibilities as to the recovery of loans under the joint financing programmes led to inadequate supervision leaving bulk of the loans in arrears.

The following suggests that BSCIC's lending operations have not been able to meet financial requirements of the SSCIs in any effective manner. Lack of adequate loanable funds, inappropriate organizational structure and inadequate expertise for effective handling and administration of the financial operations appear to be the important factors responsible for limited success. While frequent changes in the organizational set-up, lack of operational autonomy and shortage of qualified staff might also have aggravated the problems, the basic functional orientation of the Corporation has also not been towards financing activities. It might thus be desirable for BSCIC to concentrate more on promotion and extension work leaving the banking operations to be effectively handled by other appropriate agencies.

2.3 Bangladesh Shilpa Bank (BSB)

The Bangladesh Shilpa Bank (BSB) was set-up in 1972 by merging the former IDBP and the Equity Participation Fund under the Presidential Order No. 129 of 1972 to provide credit facilities and equity support to industrial concerns including small scale industries in Bangladesh.

The main objective of the BSB is to mobilize resources for investment in industries and to stimulate industrial activities through extending financial and advisory services for establishing

new projects and for balancing, modernization, replacement and expansion of the existing industries both in the public and private sector.

Financial assistance offered by the BSB comprises medium-term and long-term loans advanced to industrial enterprises in both local and foreign currencies; short-term loans for meeting working needs are also granted to those enterprises which had already received medium or long-term loans from the BSB. Working capital loans do not, however, exceed 25 per cent of the total term loans received by an enterprise earlier. In addition, the BSB also performs the function of underwriting the issue of stocks, bonds and debenture by industrial enterprises for purposes of meeting their equity needs.

The promotional assistance offered by the BSB to the prospective investors covers wide ranging issues, such as project identification, preparation and evaluation of projects, supply of techno-economic information to the entrepreneurs, guidance in selecting and procuring machinery and equipment, pre and post-investment counselling and supervision and training of officers for entrepreneurial development and so on.

BSB's Involvement in Small Industry Promotion:

BSB's involvement in small industry promotion is only incidental. It does not have specific programme to extend financial and other support assistance to the SSCIs. The SSCIs receive financial assistance from the BSB in view of the fact that such industries fall within the purview of the bank's lending limits. The upper limit of the banks lending to private sector industries is Tk.100 million per borrower. There being no lower limit, it can extend loans to small scale and cottage industries which are defined as units having fixed assets upto Tk.2.5 million. The SSCIs should also find it easier in borrowing from the BSB in view of the fact that they fulfil the bank's criteria of attaching priority in lending to those

private sector industries which are import substituting, labour intensive and dependent on local rawmaterials.

Available information (collected from the bank officials) indicate, however, that the bank generally discourages small loans below Tk.0.10 million primarily because of difficulties involved in handling such small loans. This is also supported indirectly by the data in table 1.

TABLE 1

LOANS SANCTIONED BY BSB TO SMALL INDUSTRIES(WITH FIXED ASSETS UPTO TK.2.5 MILLION) DURING 1978-79

Industry sector	No. of projects approved	No. of Loan's sanctioned		Amount sanctioned		Total Loans* sanctioned to private sector industry	
		Local currency	Foreign currency	Local currency	Foreign currency	Local currency	Foreign currency
Food & allied products	6	5	4	1.50	1.22	-	-
Textile	5	4	5	1.85	3.59	-	-
Paper & printing	2	2	2	0.45	0.45	-	-
Wood products	2	2	-	0.35	-	-	-
Rubber & Rubber products	1	1	1	1.25	0.40	-	-
Metal products	3	3	2	1.00	1.04	-	-
Machinery & spare parts	2	2	2	0.79	1.16	-	-
Transport equipment	36	36	-	28.33	-	-	-
Chemicals & Pharmaceuticals	4	5	3	1.72	1.73	-	-
Petro-chemicals	2	2	2	0.40	0.95	-	-
Service Industries	10	9	6	5.90	2.28	-	-
Miscellaneous	-	-	-	-	0.05	-	-
Total Small Industries	73	71	27	44.04	12.87	263.80	238.10
		+ 98		+ 56.91		+ 501.90	

Source: Column 1 to 3, Department of Statistics, BSB Column 4 - Resume of the Activities of the Financial Institutions, 1979-80, Ministry of Finance, Finance Division.

Note* : The total loans sanctioned to all private sector industries amounted to Tk.530.30 million including working capital loans of Tk.28.40 million not shown in this column because of lack of breakdown of this amount into local and foreign currencies.

which illustrates BSB's involvement in small industry financing during the financial year 1978-79. It is observed from the table that BSB sanctioned a total amount of Tk.56.91 million as loans to the small industries during 1978-79 which constituted only 10.73 per cent of total loans (Tk.530.30 million) extended to private sector industries in the same financial year.

That small industry financing constitutes rather insignificant proportion of total lending by the bank to private sector industries is also supported by the findings that over the six year period between December 1971 to December 1977, only 9.23 per cent of BSB's total financial assistance to private sector industries went to the small industrialists (Rahman et. al 1979 and RISP Special Report No. 1, 1979).

Though BSB's contribution to small industry financing may be little higher taking into consideration it collaboration with the BSCIC lending programme, the bank's overall financial operations are, in general, oriented towards relatively large unit within the private sector. Further, the bank's policy to discourage loans below Tk.0.10 million (Tk.10,000) implies that it has no provision at all for financing the cottage industries. Finally, the high debt-equity ratio, security requirements as well as extensive documentation requirements set by BSB like the commercial banks also make it extremely difficult for the SSCIs to approach it for financial assistance.

2.4 Bangladesh Shilpa Rin Sangstha (BSRS):

BSRS was established in 1972 (replacing the erstwhile Pakistan Industrial Credit and Investment Corporation) with a view to providing credit facilities and promotional assistance (i.e. advice and guidance in project formulation and implementation) to projects with fixed cost of Tk.2.0 million and above in the private sector and to any project in the public sector with no limit on the size of fixed assets. BSRS, as a leading

source of long-term capital for industrial concerns in Bangladesh, puts special emphasis on promoting industrial investment in the less developed areas of the country.

An overwhelming proportion (98 per cent) of BSRS's loan assistance went to the private sector enterprises during the period 1972-72 to 1978-79. But this might not have benefitted the small-scale and cottage enterprises at all in view of the fact that the bank's operational loan floor is Tk.2.5 million in fixed assets, which is much higher than the official lending limit of Tk.2.0 million. Not to speak of cottage industries, even those small-scale units with Tk.2.5 million as fixed assets, migh not have received loans from the BSRS given that the bank generally discourages lending to the small industrialists.

2.5 Investment Corporation of Bangladesh (ICB):

In addition to loan finance, availability of equity finance poses another major problem facing the small industrialists. Under the existing rules, guiding lending operations of the financial institutions, the public limited companies are required to contribute 50 per cent of the 60:40 equity portion (i.e. 20 per cent of the project cost), the rest coming from the public issue underwritten by the Investment Corporation of Bangladesh.

The ICB, established in october 1976 had an authorised capital of Tk.200 million. At present, the total resources at the disposal of the corporation is Tk.192.50 million which consists of its paid-up capital of Tk.50 million and a long-term loan of Tk.142.50 million from the government and other international financial agencies operating in Bangladesh. However, since its inception till March 1980, the corporation had made commitments of Tk.405 million for providing underwriting/debenture financing to 125 projects (against 194 applications received for a total equity support of Tk.1051.60 million) indicating thereby a resource gap of Tk.212.50 million. Such resource

constraints have led to only limited participation by the ICB in providing equity support and underwriting facilities to the private sector industrialists.

In order to diversify its resources as well as to spread risks among a greater number of financial institutions, the ICB constituted a consortium with the six nationalized commercial banks, BSB and BSRS and the Sadharan Bima Corporation so that equity support to the private sector enterprises could be enhanced. However, due to tight liquidity position of the commercial banks and lack of marketability or inadequate return from investment (because of underdeveloped nature of the capital market) in company shares in Bangladesh, the consortium members have not displayed enough willingness to actively participate in the underwriting/debenture financing commitment towards ICB's equity support programme for the private investors. An effective solution to this problem would require greater participation by BSB abd BSRS in equity financing and further enhancement of liquid resources at the disposal of the ICB.

2.6 Department of Industries:

The Department of Industries, operating under the Ministry of Industries is the other important government agency engaged in promoting private sector industries in Bangladesh. It's main promotional activities include formulation of industrial investment policy, preparation and implementation of industrial projects, publicity for promotion of foreign and local private investment and survey of industrial units for issuing import licenses and infrastructural facilities to both local and foreign private investors. The DI also provide long-term finance in the form of equity participation in public sector enterprises.

The promotional assistance offered by the DI particularly to private sector industries has, however, been limited because of its preoccupation with the control functions. DI's responsibility to issue initial approval to all investment proposals

submitted to the financial institutions and to ensure tight control on imports through estimating import requirements for all such projects before issuing them licenses, allows the Department rather limited time to play an effective promotional role[1]. An Industrial Promotion Centre has thus been set up within the Department of Industries to assist the prospective entrepreneurs in identifying viable projects, obtaining finance from the financial institutions and in completing the post-sanction formalities like incorporation of companies, raising of paid-up capital and so on. The Industrial Advisory Centre of Bangladesh has also been reorganized recently in order to provide the private investors with basic promotional assistance such as preparation of feasibility reports and general guidelines on the procedures involved in setting up new industrial units.

DI's assistance to the small private investors is difficult to assess. It has no special cell dealing exclusively with the promotion of SSCI's. The three surveys conducted by the Department since liberation till 1977, are reported (Rahman et. al 1979) to have identified 6689 industrial unit of which 6530 were small scale units. The results of these surveys help the DI to ascertain import requirements of the units surveyed and issue import licenses for importing raw-materials and necessary spare parts and machinery. While this constitutes important promotional assistance to the private sector industrialists particularly with respect to scarce foreign exchanges allocations, it is suspected that the SSCIs might not have received proper attention by the Department in the absence of a special programme to service the needs of such units.

Indeed, as the 6530 units identified by the DI comprises only insignificant proportion of the vast small industry population in the country; overwhelming majority of such enterprises remain outside the scope of its operation. Not surprisingly, this will adversely affect efficient operation by those import-oriented small-scale units (i.e. handloom, metals and chemicals) which fail to receive foreign exchange allocations for importing essential imports and suffer consequently from under-utilization of capacity.

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[1] A viable solution to the problem could be to delegate greater power to the financial institutions to sanction projects without further reference to Depart of Industries or the Investment Board. This will help speeding up the approval and sanctioning process and also avoiding unnecessary duplication of efforts by the agencies concerned with investment appraisals.

CHAPTER 3

NATIONALIZED COMMERCIAL BANKS (NCBs) AND THE SSCIs LOAN PROGRAMMES

It is difficult to assess contributions of the NCBs to small industry financing. None of the six commercial banks, all in the public sector, has separate programme for financing SSCIs. Lending to SSCIs by the NCBs except under the joint BSCIC-Consortium of Commercial Banks Programme is, in essence, incidental in that they advance short-term loans to small firms and non-farm enterprises under the directives of the Bangladesh Bank. For example, the Commercial banks are at present involved in two lending programmes - "Small Loans Scheme" and the 'Special Credit Programme' (SCP) introduced by the Bangladesh Bank in 1978 for financing the SSCIs. In addition, some of the NCBs (e.g. Janata and Sonali) are designated by the Bangladesh Bank from time to time to distribute such loan funds to the SSCIs as are available occassionally from various international donor agencies (e.g. IDA and SIDA).

However, with recent shift of emphasis on private sector development, the government is taking steps to increase the flow of bank credits to private sector industries. Lending to private industry as proportion of total industrial credit by the commercial banks and other specialized agencies is reported (World Bank 1980) to have increased from 23 per cent in 1977-78 to 26 per cent in 1978-1979. While increase in the share of the

private sector industries in commercial bank advances overtime is consistent with government's objective of promoting small private sector industries, loans to SSCIs (including small business) are reported (World Bank, 1978) to comprise only 2 to 4 per cent of the total commercial bank advances. Cottage industries, in particular, find it most difficult to have access to any such lending programmes though they constitute an important subsector of the national economy. It is thus imperative that the existing as well as the future programmes of increasing financial assistance by the commercial banks to the industrial sector should pay much greater attention towards meeting financial needs of the SSCIs.

The commercial banks, having extensive branch networks covering the entire country, are in a better position to handle SSCIs financing more effectively than any other agency as most much industries operate in the rural areas of the country. The NCBs were thus designated by the Bangladesh Bank for administering the "Small Loans Scheme" as well as the "Special Credit Programme", so that financial services provided through these Programmes could reach the intended beneficiaries even in the remotest village. While it is too early to appraise the success of these lending programmes in adequate detail at the present stage of their operations, attempts will be made to provide at least a rough indication of their (particularly of the SCP) effectiveness in meeting financial requirements of the SSCIs.

3.1 The Small Loans Scheme (SLS)

With a view to meeting credit requirements of the small borrowers including small scale and cottage industries and self-employed persons, particularly, in the rural and semi-urban areas, the Bangladesh Bank introduced the Small Loans Scheme in February, 1978. Under the Scheme, each of the nationalized commercial banks was required to disburse 2 per cent of the total demand and time liabilities as small loans in two phases - during July-December 1978 and January-June 1979 (Bangladesh Bank, 1979-80). The maximum limit of small loans per borrower was fixed to be Tk. 50,000 for the small traders and the self-employed persons and Tk. 100,000 for small scale and cottage industries. As indicated by the ceiling limit, loans under the Scheme, were intended to finance credit requirements of the cottage type enterprises in the small-scale sector. Indeed, this constitutes an important step in the direction of promoting the really small industrial enterprises which account for an overwhelming majority (87 per cent RISP - BIDS, 1981) of the SSCIs in the rural areas of the country, but are hardly covered by the existing institutional arrangements for financing the small-scale sector.

The share of various categories of borrowers covered by the overall small loans programme as laid down by the Bangladesh Bank, is shown in table 2. As shown by the table, small scale and cottage

TABLE 2

RELATIVE PERCENTAGE SHARE OF VARIOUS CATEGORIES OF BORROWERS UNDER THE SMALL LOANS SCHEME

Categories of borrowers	Percentage share in the targeted disbursement
Small Scale/Cottage Industries	50.00
Retail traders	25.00
Self-employed persons	20.00
Rural electrification	5.00
Total	100.00

industries have been given relatively high priority compared to other categories covered by the Programme. The operationally significant issue is, however, to examine how effectively the programme was executed by the designated agencies. This is done in table 3 by comparing the estimated amount to be disbursed to each category of borrowers with the amount actually disbursed during the given time period. The amount available for disbursement to various categories of borrowers is estimated by calculating their respective shares in the total demand and time liabilities (e.g. Tk. 21,134.0 million, 2% of which is Tk. 422.68 million) of all banks during the period 1978-1979.

TABLE 3

DISBURSEMENT OF SMALL LOANS TO VARIOUS CATEGORIES OF BORROWERS UNDER THE SMALL LOANS SCHEME, 1978-79

Categories of borrowers	Estimated amount (in million Tk.) available for disbursement as per targeted share of the borrower	Amount actually disbursed (in million Tk.)	3 as % of 2
Small/Cottage industries	211.34	37.00	17.51
Retail traders	105.67	208.80	198.09
Other self-employed persons	84.54	16.30	19.28
Rural electrification	21.13	0.80	3.79
Total	422.68	262.90	62.19

It can be observed from the table that except for the retail traders (for whom the actual disbursement has exceeded the estimated amount available for disbursement by nearly 100 per cent) the actual disbursement has fallen substantially below the planned target for all categories of borrowers including the small scale and cottage industries. As reported by the concerned banks (RISP Special Report No. 1, 1979), while many of the eligible SSCIs did not approach them either because of their ignorance about the availability of such loans or because of their unwillingness to borrow from a bank, lack of adequate security and various problems (i.e. absence of an independent lending policy for the SSCIs, lack of trained staff and supervisory personnel

and so on) involved in small loans made the designed banks generally reluctant to implement the Small Loans Programme. In this context the observation made by the Bangladesh Bank on the success of this programme is worth mentioning. A handout (BB 1978) issued by the Banking Control Department of the Bangladesh Bank pointed out that complicated disbursement procedures prohibited the SSCIs from getting adequate credit under the Special Loans Programme.

The consequence, as exhibited by the figures in table 3, was substantial underutilization of the funds earmarked for disbursement among the intended beneficiaries of the Scheme. This (and the evaluation of the special Credit Programme in the subsequent sections) implies that both the specialized financial institutions and the NCBs lack in the kind of organizational set-up, initiative, expertise and orientation that are required for financing the SSCIs. This is indirectly supported by the fact that most of the financing banks reported the recovery rates of small loans under the scheme to be as high as 90 per cent of the amount disbursed. Indeed, the information supplied by five of the six NCBs implementing the SLS indicate that of the total amount disbursed (262.90 million), only Tk. 53.18 million (20.2 per cent) was overdue for repayment. While this corroborates the banks' statement of good recovery position of the loans under the SLS, reluctance to lend to such enterprises may thus reflect their in-built allergy for not dealing with the SSCIs. This also indicates that the alarm of the NCBs towards safety of the small loans may not always be well-founded.

3.2 The Special Credit Programme(SCP)

The Special Credit Programme of Tk. 6.00 crores (raised to Tk. 11.45 crores subsequently) was launched by the Bangladesh Bank as an extension of the Small Loans Scheme from February 1978 with a view to intensifying financial assistance to the SSCIs. The SCP was introduced for purposes of :

a) meeting short-term working capital requirements of the SSCIs;

b) setting up of new small and cottage industries ; and

c) expanding activities of the existing SSCIs.

Principal Features of the SCP

The important features of the SCP, as outlined by the Bangladesh Bank in its circular issued to the 'Lead Bank' on January 25, 1978 are as follows:

Loans under the scheme will be provided in local currencies to all small and cottage industries except those which are already enjoying normal credit facilities from the commercial banks.

The maximum amount of loan per borrower will not exceed Tk. 1 lakh (0.1 million). However, in case of co-operatives or associations of SSCIs, the maximum lending limit may be raised as per requirements of the borrowers.

Unlike the loans available under normal financing arrangements from the existing financial institutions, loans provided under the SCP will be production-oriented and not security

oriented. The security of the loan will be hipothecation of stocks of raw materials and/or machineries. The rate of interest charged on loans will be 11 per cent per annum with the provision for a maximum margin requirment of 25 per cent. The duration of fixed capital loans will be 5 years and that for working capital loans will vary between 2-3 years. While fixing repayment terms, a reasonable grace period will be recommended depending on the gestation period of the project and the normal time lag between production and marketing of the commodity.

The nationalized commercial banks are responsible for operating the SCP. One of the six NCBs has been designated as the "Lead Bank" in each district and made responsible for disbursement of loans, supervision of end-use of the funds, and recovery of the loans as per repayment schedule. Apart from supervision of end-use of the loans by the financing bank, BSCIC will render appropriate technical and marketing assistance to the borrowers for ensuring proper utilization and timely recovery of the outstanding dues from the borrowers. In case of bad debts, the financing bank will be able to recoup 30 per cent of the bonafide loss through the credit Guarantee Scheme introduced by the Bangladesh Bank for loans advanced under the SCP.

The processing of the loan applications and final sanction of loans in each district will be done by a District Committee (DC) comprised as follows[1]:

i) Deputy Commissioner/ Additional Deputy Commissioner(Development)	Chairman of the Committee
ii) Regional/District Manager of the Lead Bank	Member of the Committee
iii) Representative of Department of Industries in the District	Member of the Committee
iv) Representative of the Chambers of Commerce and Industry	Member of the Committee
v) Regional Chief/District Manager, BSCIC	Member - Secretary

Applications for loans have to be made in prescribed forms which may be received either by the concerned Lead Banks or by BSCIC and forwarded to the Member-Secretary of the District Committee who, after making initial appraisals in consultation with the representative of the concerned Lead Bank, will convene a meeting of the afforsaid committee within one month from the date of

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1 As per recommendations made in a Review Meeting held on 29.1.1981 under the Chairmanship of the Deputy Prime Minister in charge of Industries and review of such recommendations made in another meeting held under the Chairmanship of the Governor, Bangladesh Bank, held on 25.2.81, some important changes wer introduced in the procedures of administration of the SCP. Among important charges, the compsition of the District Committee was enlarged through co-opting a representative of the Power Development Board (Resident/Executive Engineer). Other important changes include the enhancement of maximum ceiling of loan per borrower from Tk. 1.00 lakh to Tk. 2.00 lakhs and discontinuation of the practice of issuing working capital loans to the on-going projects except the handicrafts.

receipt thereof for final selection of the loanees. The Committee, on receipt of the loan applications after initial apprasial will make final selection in the light of the considerations of techno-economic viability of the projects, skill, honesty, integrity and risk-bearing capacity of the applicants and communicate its decision to the concerned branch of the Lead Bank of the district along with concrete recommendations as to the amount, duration and repayment schedule of the financing bank of the district. The entire exercise from the date of receipt of application to final decision on the loan proposal should not exceed two months.

Finally, the lending branch (the financing bank) of the Lead Bank in the District (located in close proximity to the borrower) on receipt of decision from the District Committee has to disburse the loan within one month from the date of decision after completion of the requisite formalities.

The foregoing suggests that considerable official formalities are involved in getting a loan under the SCP. Even if everything follows smoothly at each stage between making the application and getting the loan, the minimum time required will be around three months. More important, filling a five-page application form supported by a large number of documents will hardly be possible by the intended beneficiaries of the scheme, majority (60 per cent; Phase I Report, RISP-BIDS, April 1979) of whom are illiterate. The documentation requirements for loans under the SCP which vary

between different financing banks, are inextricably complicated in that a borrower has to submit a large variety of papers and certificates (e.g. nationality certificate, bank guarantee, personal guarantee, balance sheet statement, import licence and so on). In case of the borrowers requiring imported raw materials, applications for working capital loans have to be submitted along with import licence. As is well known, however, given the complicated procedures for issue of import licences, it might be extremely difficult or altogether impossible for a small entrepreneur, to obtain such a licence and then apply for a loan.

However, despite these complicacies, the SCP is claimed to have attained considerable success within a relatively short span of time since its inception. We now turn to examine the progress of the SCP in the areas of sanction, disbursement and recovery of loans advanced under the Programme.

Approval, Sanction and Disbursement of Loans under the SCP

It is observed from Table 4 that since its inception till end of December 1979, a total of 5224 applications were received by the financing banks for loans under the SCP, of which 3093 (59 per cent) came from small scale enterprises and 2131 (41 per cent) from cottage enterprises. Of the total applications received, 2081 (39.8 per cent) cases were approved(the percentage of approval being relatively large in case of cottage (46.27) than in case of small-scale (35.4) enterprises) and 3143 cases (60.2 per cent) were rejected. Incomplete applications, lack of

techno-economic viability of the proposed projects, non-inclusion of the projects in Governments Investment Schedule, inability of the applicants to present import licenses and so on, were found to be the important reasons for rejection of the loan applications.

The same trend of approval and rejection of the loans applications is also found to persist overtime from a recent study[1] carried out by the auother on the SCP for the BSCIC. As

TABLE 5

DIVISIONWISE STATEMENT OF THE LOAN APPLICATIONS, RECEIVED, APPROVED, REJECTED AND PENDING, AS ON 30TH JUNE 1981

Divisions	Applications Received	Applications Approved	Applications Rejected	Applications Pending
Dacca	1233	443	609	181
Chittagong	3634	1096	1452	1086
Khulna	1467	709	584	174
Rajshahi	1494	898	296	300
Total	7828	3146	2941	1741

Source : Ahmed M.U. August, 1981

seen from the Table, out of a total of 7828 applications received 3146 cases (40.19 per cent) were approved and 2941 cases (37.57) were rejected by the credit allocation committees of various divisions. It is to be noted here that the rate of rejection would

1. Ahmed M.U., "Evaluation of Special Credit Programme for Small and Cottage Industries, Report submitted to BSCIC, August, 1981

rise substantially if the cases pending for approval are taken into account. When compared divisionwise, the incidence of rejection is found to be the highest(slightly below 50 per cent) in Dacca Division being followed by that in Chittagong(40 per cent) Khulna (39 per cent) and Rajshahi division (19 per cent respectively.

Out of the total 1741 pending cases shown in the table, 1029 cases (13 per cent) were found to be pending for appraisal by the DCs in various divisions and 712 cases (9 per cent) were pending for disbursement of the loan cases already approved by the DCs. While inordinate delays and irregularity in holding meetings by the DCs appeared to have been their main reason for such large number of loan applications remaining pending for approval by the DCs, lack of adequate co-operation between the BSCIC and the Lead Bank officials appeared to have caused such delays. In many cases, the initial appraisal of the loan applications made jointly by the BSCIC and the Bank representative took much longer time than warranted. The banks being commercial organization wished to ensure creditworthiness of the borrowers, whereas the BSCIC being essentially an extension agency wished to get funds moving and industries started. It is due to this clash of interests between the BSCIC and the Bank representatives that many of the loans sanctioned by the DCs were not disbursed by the financing banks for a long time.

However, so far as disbursement of the sanctioned loans under the SCP is concerned, the Programme appears to have attained considerable success. As shown by the data in Table 5, since inception to December 1979, out of the total sanctioned amount Tk. 6.34 crores, 5.25 crores (82.8 per cent) have been disbursed among the borrowers[1]. The proportion disbursed was the highest in Rajshahi division reaching nearly 90 per cent of the sanctioned. In terms of both amount sanctioned and disbursed, 70 per cent of the loans advanced under the SCP went to small scale enterprises. compared to only 30 per cent received by the cottage enterprises[2]. This may be regarded as

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1. While the same rate of disbursement was found to continue till recently, the amount disbursed under the Programme reached Tk. 8.41 crores as on 30th June 1981(Ahmed M.U.1981)

2. As seen by the author in the earlier quoted recent study on the SCP, the relative share of the cottage enterprises in both amount sanctioned and disbursed has, in fact, gone further down overtime reaching 20 per cent of the amount sanctioned and disbursed.

TABLE 5

DIVISION-WISE STATEMENT OF LOANS SANCTIONED AND DISBURSED UNDER THE SCP BY INDUSTRY TYPE TILL DECEMBER 1979

(TK. in 000)

Divisions	Amount sanctioned			Amount disbursed		
	Small	Cottage	Total	Small	Cottage	Total
Dacca	5650.00	3286.00	8936.00	5328.56	1805.46	7134.01
Rajshahi	14838.00	10247.30	25085.30	13688.50	8493.00	22181.50
Khulna	9015.33	3732.21	12747.54	7081.04	2180.62	9261.66
Chittagong	13642.00	2964.00	16606.62	11124.62	2803.50	13928.12
Total	43145.33	20229.51	63374.84	37222.72	15282.58	52505.31
Row per cent	(68.07)	(31.93)	(100.0)	(70.89)	(29.11)	(100.0)

an uneasy feature of the SCP in view of that fact that though nearly 90 per cent (RISP Phase II Report, February 1981) of the rural industries in Bangladesh are cottage enterprises, their share in institutional credit is substantially below that of the small scale enterprises. As noted later, the practice of adharing to a high minimum loan floor, stringent collacteral requirements and discentinuation of the working capital loans appear to have restricted the access of the cottage enterprises to the credit facilities offered under the SCP.

Thus, like in the case of other Programmes of institutional financing for the SSCIs (discussed earlier), the SCP also appears to have failed in making adequate credit provision for the cottage enterprises. Before elaborating further on the reasons for such anomalies affecting the operation of the SCP, the performance of the designated banks in operating the Programme in their respective areas needs to evaluated.

Table 7 analyses the performance of the designated banks in handling the Programme in their respective areas of operation as of the end of February 1981. Several observations can be made from the table. In fourteen (such as Dacca, Bogra, Comilla, Khulna, Chittagong, Rangpur, Rajshahi, Jessore, Barisal, Patuakhali, Kushtia, Tangail, Pabna and Sylhet) of the twenty districts both sanction and disbursement of loans have been satisfactory in the sense that the entire amount of funds allocated initially for distribution, has been exhausted and subsequently new funds have been supplied. Of the remaining six districts, the most dismal performance has been recorded by Chittagong Hill Tracts, Followed by Jamalpur, Faridpur and Noakhali both in terms of sanction and disbursement.

Of the six Lead Banks operating the Scheme, Sonali and Janata appear to have performed relatively better compared to other banks interms of both sanction and disbursement of loan funds allocated to them. While Janata could have exhausted the allocated funds in all the four districts, Sonali did the same in three of the five districts where it was designated as the Lead Bank. While similar

variation in the performance of the banks with respect to outstanding loans is found to exist, the overall oustanding loans under the SCP is around Tk. 8 crore.

The observed variation in the performance of the Lead Banks with respect to sanction and disbursement of loans under the Programme is explained below using information collected from the Lead Banks and their financing branches.

So far as processing of the loan applications is concerned, it has often been too complicated. The three-tier processing machanism (i.e. BSCIC and Bank Representative District Committee Financing Bank) has made the decision-making process both lenghty and complicated. In most cases, the time period involved between processing the application and final sanction of the loan has, on average, extended to three months and more under the SCP compared to only one to two months for loans under SLS. Due to differences in the attitude towards SSCIs lending, the BSCIC and the Bank representative failed in many cases to become unanimous about the viability of the projects and took longer time in decision-making.

A second bottleneck facing the processing machanism and mentioned by most lead banks is the high-handedness displayed by some members of the District Committee, particularly Chambers of Commerce and BSCIC. Such undesirable interference of the members of the District Committee is reported to have resulted in considerable misuse of the loan funds in the sense that loans

TABLE 7

STATEMENT SHOWING SANCTION AND DISBURSEMENT OF THE AMOUNT OF FUNDS ALLOCATED (BY THE BANGLADESH BANK) TO THE LEAD BANKS IN VARIOUS DISTRICTS, AS ON 28.2.1981

(Taka in lakhs)

Name of the District	Designated Bank	Amount Allocated	Loan cases sanctioned	Amount sanctioned	Amount Disbursed	Amount Outstanding[1]
Mymensingh	Agrani	30.00	45	29.40	12.00	14.00
Jamalpur	Agrani	20.00	20	6.00	3.00	2.00
Faridpur	Agrani	30.00	27	14.00	9.00	10.00
Barisal	Agrani	30+15 = 45.00	74	43.34	24.71	26.00
Patuakhali	Agrani	20+20 = 40.00	72	34.17	30.00	30.00
Sub-total	Agrani	165.00	238	136.51	78.71	82.00
Pabna	Janata	30+20+20 = 70.00	385	68.00	66.00	63.00
Rangpur	Janata	30+30+15 = 75.00	155	60.00	55.00	57.00
Jessore	Janata	30+30 = 60.00	203	59.08	42.00	43.00
Rajshahi	Janata	40+25 = 65.00	82	40.00	38.44	37.00
Sub-total	Janata	270.00	825	227.08	201.44	200.00
Chittagong	Pubali	40+40+40+20 =140.00	513	124.65	116.86	115.00
Sylhet	Pubali	35+35 = 70.00	112	69.67	49.59	53.00
Sub-total	Pubali	210.00	625	194.32	166.45	168.00
Noakhali	Rupali	30.00	62	26.35	22.04	23.00
Khulna	Rupali	40+40 = 80.00	234	68.08	48.45	47.00
Tangali	Rupali	20+20 = 40.00	82	36.25	28.38	25.00
Sub-total	Rupali	150.00	378	130.88	98.87	95.00
Bogra	Sonali	30+30+30 = 90.00	135	90.00	70.00	64.00
Chittagong H.T.	Sonali	15.00	25	13.73	12.00	12.00
Kushtia	Sonali	35+35 = 70.00	143	56.00	50.00	43.00
Comilla	Sonali	35+35 = 70.00	193	67.00	62.00	59.00
Dinajpur	Sonali	35.00	104	33.00	29.00	27.00
Sub-total	Sonali	280.00	600	259.73	223.00	205.00
Dacca	Uttara	45+25 = 70.00	278	45.00	44.12	46.00
Grand Total	All Banks	1145.00	2944	993.52	812.59	796.00

Source : Ahmed M.U. 1981

Note : 1 Figures in this column relate to period ending 31.12.80

were, in some cases, granted to dishonest and unenterprising borrowers.

The third and important defect identified by the financing banks in the sphere of loan processing is that the member-secretary of the DC, though responsible for making initial appraisal of the loan applications, was mostly found incompetent for the job. While this may partly reflect the lack of training on the part of the BSCIC representative in appraising credit-worthiness of a borrower, the bottleneck facing timely processing of the loan applications also seemed to be adversely affected by at least two other reasons. First, the DIC-in charge or the district manager of BSCIC does not have adequate staff to help him in the job of processing the loan applications. Second, the lack of co-operation between the bank and the BSCIC representative also aggravated the problem considerably. Thus, while the BSCIC representative in the DC should be provided with adequate supporting staff, a division of tasks between the BSCIC and the bank representative is also urgently necessary for ensuring prompt and efficient appraisal of the loan applications. The proposed demarcation of responsibilities between the two officers should be such that while the bank officer may be responsible for appraising financial viability of a project, the BSCIC-man may be made responsible for appraising techno-economic viability of the relevant project.

The fourth shortcoming adversely affecting the operation of the SCP seems to have been the rigidity of the banks in certain areas of operation of the Scheme. To start with, the documentation requirements set by most banks in support of the loan applications were, in general, too cumbersome, taxing too heavily on the time and ability of typical small entrepreneurs to procure and submit them all. Preparing balance-sheet statement, procuring a personal guarantee, an import license and so on, can hardly be expected to be possible on the part of the small industrialists who rarely keep records of their operations or have their businesses registered with the government. While the degree of complicacies relating to documentation requirements was found to vary between different financing banks, the more closely they were adhared to by the concerned banks(i.e. Rupali and Agrani), the lower appeared to be the progress achieved by them in terms of sanction and disbursement of loan funds allocated to them.

Indeed, this, is also supported indirectly by the fact that while the primary reason for rejection of the loan proposals was in most cases incomplete application, the latter was found to be a consequence of the inability of the borrowers to submit the necessary papers and documents. Not surprisingly, given the contrasting features of small (relatively more formal) and cottage industries (mostly informal and unregistered) this would act as a deterrant to receiving formal credits more for the

latter than for the former. While this explains in part, the differential access of the small and cottage industries to loans under the SCP , it might be further accentuated by different loan floors set by the lead banks in various areas.

Though the Bangladesh Bank initially set only a maximum ceiling of Tk. 1 lakh per borrower on loans under the SCP, most Lead Banks were found to adopt a minimum loan floor of Tk. 5,000 to 20,000 in case of fixed capital loans and that of Tk. 2,000 to Tk. 10,000 for working capital loans in various operating zones. What is more interesting, these minimum loan floors were found to vary between different districts and between different banks. Obviously while such high minimum ceiling of loans might have excluded many cottage units from receiving credit facilities under the SCP, the variation in the floor might have resulted in the geographical variation of the progress achieved by different banks in respect of sanction and disbursement of funds allocated to them.

Finally, though the financing banks were instructed by the Bangladesh Bank not to have insisted upon collateral security for loans provided under the SCP, all the concerned banks were reported to have adhared to the practice of asking for collateral securities. This also is bound to prohibit the smaller units from having easy access to the credit facilities provided under the Programme.

True, part of the onus for not getting an institutional loan rests also on the borrowers themselves because of their reluctance to look for it, to approach a bank, and also because, of submitting ill-conceived proposals. Above all, the borrowers lack of knowledge about the banking principles further widens the existing gap between the loanees and the loan giving agencies. While increased publicity of the fund availability as well as training of the entrepreneurs in appropriate directions may raise their consionsness about investment opportunities and credit facilities, the agencies and institutions distributing such facilities should be more decentralized and brought to the door steps of the potential entrepreneurs (i.e. the point of operation of the SCP may be shifted from the District to the Thana level).

Recovery Position of Loans Under the SCP

The success of any credit programme has to be adjudged through analysing its recovery position, because mere disbursement of loans will do little until effective utilization and timely recovery of the loans disbursed can be ensured. Further, poor recovery will not only lead to misuse of scarce capital resources but also intensify the inflationary process through liberal refinancing.

The divisionwise recovery position of loans advanced under the SCP as on May 1980 is shown by the data in Table 8. The results obtained from the table are self-explanatory. The overall

TABLE 8

RECOVERY POSITION OF LOANS UNDER THE SCP UPTO THE PERIOD ENDED MAY 1980[1]

(Tk. in lakh)

Divisions	Amount disbursed	Amount due for repayment	Amount recovery	% of recovery (3 as % of 2)	Amount overdue	% overdue (5 as % of 2)
Dacca	80.83	35.33	4.13	11.68	30.14	85.31
Chittagong	227.14	56.72	14.53	25.66	42.19	74.38
Khulna	147.90	36.38	13.71	36.71	23.47	64.16
Rajshahi	225.71	79.07	28.17	36.44	50.90	64.37
Total	681.58	207.70	60.26	29.01	146.70	70.64

Source : Ahmed M.U. 1981

Note : 1. Figures for Patuakhali and Barisal districts of Khulna division and those for Mymensingh, Jamalpur and Faridpur of Dacca division relate to period ending August 1980.

recovery position of loans in all the divisions has been highly unsatisfactory, reaching roughly 30 per cent of the amount due for repayment. Among the four divisions, the rate of recovery in Dacca has been the lowest in that the percentage of overdue loans is more than 80 per cent of the amount due for repayment. On a districtwise basis, the recovery rate of the loans due for repayment was found to be the highest (47 per cent) in Rajshahi, followed (46 per cent) by that in the Kushtia district.

The overall unsatisfactory performance recorded by the SCP in recovering the overdue loans appeared to have resulted from a complex of factors, of which the following are important.

First, so far as the financing NCBs are concerned, they do not have adequate experience in dealing with SSCIs lending. Nor do most of the banks except Sonali and Janata have any trained staff to appraise industrial loans. It is only Sonali and Janata banks, which are reported to have formed special cells of about fifteen officers during the end of 1978 for processing and appraising small industry loans and the II-IDA credit programme which came into effect from September 1978. Both the banks are also reported to have sent some of their officers to India for training in the relevant field.

Thus, while the banks usually depended on the BSCIC personnel for appraising the loan applications in the absence of their own expertise, the latter in their turn do not have training to examine the projects from the banking angle. It is, therefore, possible that many unbankable propositions might have received financing under the Programme and turned into cases of bad debts.

Second, the problem is reported to have been further aggravated by the fact that those loan cases whose eligibility were decided by the amount of bribes paid to the concerned officials and not by their techno-economic and financial viability, also turned into bad debts pushing the overall recovery position further down.

Third, due to lack of trained extension staff, the banks fail to make adequate arrangements for follow-up and supervision of the end-use of loans. Indeed, most of the financing banks admitted that they faced considerable difficulties in administering the SCP because of lack of trained personnel and of supervisory staff who could check progress of implementation of the sanctioned projects and ensure proper utilization of the loans.

Fourth, the effective monitoring of the sanction, disbursement and recovery of loans under the SCP also appears to be adversely affected by lack of necessary co-operation between the BSCIC officials and the Bank personnel in all these areas. The two different institutions making joint decisions on different aspects of the projects during appraisal and also having joint but not clearly defined responsibilities in respect of recovery of the loans, appear to have resulted in the institutions blaming each other for mistakes without taking responsibility for failures.

Thus, besides arranging for training of the concerned officers of the Lead Banks and of BSCIC in respect of the objectives and spirits of the SCP and appraisal, sanction and disbursement of loans under the Programme , a demarcation of responsibilities between the two agencies with respect of follow-up and supervision of end-use of the loans may ensure better recovery. While the BSCIC officers at the district level may be responsible for moniotring progress of implementation of the sanctioned projects through providing them with necessary technical services and

extension facilities relating to management and marketing, the supervision of the end-use of the loans may be the inclusive responsibility of the financing banks. In this direction, granting of more autonomy to the branch officers of the Lead Banks in overall administration of the programme, including sanction, disbursement and recovery may also be of help.

Finally, as reported by various groups operating the SCP, the borrowers themselves are partly responsible for bad recovery position of the loans. Wilfull default and diversion of funds for unproductive purposes by the borrowers appeared to have important bearing on their inability to repay the amount borrowed. However, while lack of motivation and business experiences on the part of some of the borrowers may lead to defaults by them, the diversion of funds to non-productive use may at least partly reflect other important problems such as inadequate amount borrowed, lack of working capital loans & ill-concerned projects, all of which combine together to lead to misuse of the borrowed funds.

In the light of the difficulties faced and experiences gathered in dealing with the small loans programmes, the concerned banks indicated the need for adopting several measure towards ensuring speedy and efficient sanction, disbursement and recovery of loans, of which the following are important.

i) Processing of loan applications should be made easier and less time-consuming. In this context, the financing banks operating more closer than any other agency to the borrowing unit,

should have greater autonomy in appraising credit worthiness of the borrowers;

ii) All banks should have separate cells, staffed by adequate number of trained personnel for administering the small loans. Recruitment of trained, field-level supervisory staff was particularly emphasized for ensuring effective utilization and safety of the loan funds through close supervision of end-use as in the case of Tk. 100 crore Special Credit Programme for the small farmers;

iii) The maximum loan size per borrower should be raised above the present level and grace period for both fixed and working capital loans should be extended further to make the repayment schedule more practical,so that the borrowers have the opportunities to make proper use of the funds and repay them in time;

iv) Guarantee provided by the Bangladesh Bank under its credit guarantee scheme for small loans ensuring recovery of 30% of the bonafide losses as bad debts under the SCP should be enhanced to at least 70-80% as in case of the lending to small industries under the third IDA Credit Programme.

v) Making adequate provision by the government for basic infrastructural facilities such as improvement in transport, regular and increased supply of electricity, machinery and equipment in the small townships and rural areas was emphasized towards ensuring better utilization of installed capacities and marketing of the products of the small industrialists. All these

would guarantee increased productivity, increased sales and better repayment capacity of the small borrowers.

vi) Finally, proper training of the borrowers in areas such as filling of application forms, conceiving viable projects and making correct estimates of credit requirements along with motivating them for making proper use of such credits was also suggested by most lending banks.

3.3 NCBs and Other Credit Programmes:

Besides SLS and SCP, Janata and Sonali Bank also administer small loans programmes either independently or jointly in collaboration with BSCIC, as introduced by the government from time to time. Such credits include Cash Foreign Exchange Allocation of Tk. 10 million and 15 million started in December 1977 and May 1978 respectively for setting up export-oriented small industries; SIDA grant of Tk. 8 million introduced in April 1977, first IDA credit (353 - BD) of US $ 3 million (Tk. 46.8 million), introduced in 1970 and reactivated in 1973, the Second IDA Credit (825-BD) of US$ 7 million (Tk. 109.2 million) starting with effect from 15th September 1978 and the Third IDA Credit (SSI-III) Programme of US $ 35.00 million starting with effect from January 1981.

In the first four of these credit programmes, the Janata bank participated in Taka counterpat financing in collaboration with BSCIC as per bilateral agreement entered into by the bank

and the BSCIC. Under these joint financing schemes, the bank financed 38 small industry projects (mainly in synthetic textiles and oil mills) involving an amount of Tk. 27.31 million.

In addition, Janata also participated in other credit programmes (i.e. Italian Suppliers Credit, US - AID financing scheme and so on) through which it financed 25 small industry projects for setting up new ventures or for balancing and modernization of the existing units involving an amount of Tk. 23.35 million. Janata bank's share in all such special credit programmes for financing small industries either independently or in collaboration with BSCIC during 1974-1979 in addition to its stakes in the SLS and SCP, stood roughly at Tk. 91.26 million of which Tk. 55.51 million (55.51 per cent) was sanctioned. While this indicates considerable participation by the bank in the small industry financing programmes, an evaluation of its success in handling the credit operations needs to be verified through analysing actual disbursement of the sanctioned amounts and recovery of the loan funds. In the absence of accurate information on these aspects, however, only a few general comments can be made.

As noted earlier, most of the joint financing programmes achieved only moderate success because of lack of emphasis on project identification, promotion and extension work. For example, the overdue loans financed under the first IDA credit (353-BD) are reported to be heavily in arrears, mainly due to lack of

proper supervision. As of February 28, 1980, arrears have been reported (World Bank, 1980) to constitute about 35 per cent of the amount due for repayment.

In case of most of the joint financing schemes, both apprasial and follow-up procedures were also cumbersome and industrial units operating at the lower end of the small industry definition (particularly cottage units) had limited access to the programmes. It is reported that the projects financed under the Programme were mostly medium scale industries located in the major cities. It is in consideration of these problems that the second IDA credit (825-BD) programme seeks to strengthen promotion and extension work and to clearly define the roles and responsibilities of the implementing institutions (i.e. BSCIC, Janata and the Sonali Bank). The programme is also proposed to be directed towards smaller type enterprise including cottage industries in small towns and rural areas.

The second IDA credit programme of US $ 7 million, which works out to a total amount of Tk. 158.8 million including the contribution by the local sponsors of 49.6 million(i.e. government of Bangladesh, BSCIC and the NCBs) came into effect from 15th September, 1978. The actual disbursement started, however, in 1979, expecting to be completed within the last quarter of 1982. The project will finance establishment of new SSCIs as well as balancing, modernization,replacement and expansion of the existing units through supplying both fixed and working capital loans in

foreign as well as in local currencies. Under the project, about 200 small scale units and 1,000 cottage units are proposed to be financed with an average cost of Tk. 440,000 and Tk. 20,000 respectively. This implies that unlike most other credit programmes, the second IDA credit programme is biased significantly towards financing smaller enterprises and cottage units. Provision is also there for covering half of the entrepreneur's required equity of 30 per cent in case he is not able to provide it.

Another positive aspect of this lending programme is that the responsibilities (i.e. processing of loan application, appraisal of credit worthiness, providing extension services and supervision and follow-up etc.) of the various implementing agencies have been clearly defined and demarcated for ensuring timely sanction, disbursement, utilization and recovery of the loan funds. For example, while BSCIC is responsible for providing promotion and extension services to the borrowing units, sanction and disbursement as well as follow-up and supervision of the loans will be taken care of by the NCBs.

However, the joint appraisal of the loan application at the initial stage like in the cases of other joint financing schemes, may make the appraisal procedure cumbersome and create unnecessary delays. This problem might however, be transitional in that the project appraisal was to be a sole responsibility of the NCBs

after a period of 18 months from the time of inception of the programme, pending the banks setting up their own cells for the purpose. Further, the operating NCBs - Sonali and Janata, besides opening small industry cells at their Head offices, have also allowed sanctioning authority to their regional offices for small industry projects costing upto Tk. 100,000 per borrower. While this is an important step towards decentralization of lending process of the NCBs, it should ideally be extended upto the local branch level so that the entire process of sanction and disbursement can be made more easier and the programme can be made open to a more wider range of clientele.

Given the time schedule for disbursement of the loan funds under the Programme, evaluation of its impact on SSCIs promotion and development remains to be examined at a later period. According to latest information available from the two administering agencies, 146 projects have been financed under the Programme involving an estimated US $ 6.2 million by June 30, 1980. While the commitments under the Programme appear to have proceeded well ahead of schedule, the projects financed have also been varied, geographically dispersed, more labour intensive and also more dependent upon local inputs compared to those financed under the first IDA Credit Programme. However, as expected, the transitional phase of joint appraisal is reported to have been cumbersome particularly since BSCIC was initially rather relucant to relinquish control over SSCIs financing programmes.

So, far as the III-IDA Credit Programme is concerned, the programme being in operation since January 1981, can not be evaluated yet. It may, however, be expected that since the programme will build on the experiences gathered from two previous ones, the financing agencies (i.e. Sonali, Janata and Agrani banks) should have performed better and be able to meet credit needs of the SSCIs more effectively.

As pointed out earlier, limited financial assistance is also rendered to the SSCIs through such specialized organizations as BHB, BHMC, Co-operative Department and the Divisional Development Boards. For example, the BHB established in February 1978 under the Ministry of Textiles to take over handloom responsibility from BSCIC, arrange credit facilities to the weavers' co-operatives through the commercial banks to buy looms, machines and spares and accessories.

Bangladesh Handicrafts Marketing Corporation(BHMC) is handling part of the second IDA credit programme of US $ 7 million through the NCBs since 1978. The purpose is to assist the artisans in jute, bamboo, cane and ceramic industries in 12 thans of the country with credit for marketing their products. Loans under this programmes may be sanctioned without collateral. It is reported that (World Bank, 1980) as of June, 1980, BHMC organized about 1500 jute, cane and bamboo artisans into associations and helped improve production methods and qualities of their products under the Programme.

The Rural Development Projects I and II operated by the IRDP in 22 thans of the country and funded by the World Bank, conduct rural industries development programmes for providing marketing assistance to such traditional rural industries as blacksmithy, oil pressing, bee keeping and so on.

Finally, while BKB (Bangladesh Krishi Bank) also advances some small loans to the agro-based SSCIs in different areas of the country, the four Divisional Development Boards also grant loans to small and cottage industries for setting up new units and modernizing the existing ones in their respective divisions. Among other facilities made available by the Boards to the SSCIs, provision is also there for extending pre- and post-investment counselling, extension and advisory services.

However, available information suggests that the Boards' assistance to small industry development has so far been largely inadequate and ineffective. So far as financial assistance is concerned, no organized programme appears to be in sight for helping the SSCIs. For example, the SSCIs share in the total development outlay of the Chittagong Hill Tracts Development Board (CHTDB) during 1979-80 was only 1 per cent. This is, however, hardly surprising in the sense that it is very much in conformity with the SSCIs share in the total public sector allocation(e.g. 1 to 2 per cent) made by the government in all the five year development plans of the country ever since Pakistani days (Ahmed M.U. 1980). Again, whatever financial assistance was rendered by

the CHTDB to the SSCIs, it did not benefit the really smaller enterprises requiring financial help to the tune of a few hundreds.

Lack of a clear-cut development strategy for the SSCIs at the national level, proper definition of such units and an inadequate co-ordination among the relevant agencies responsible for promoting small industries, are reported to have created serious operational contraints for all the Development Boards in determining the promotional needs of the SSCIs and providing them with promotional services.

Both the SLS and the SCP discussed in the foregoing, were introduced by the Bangladesh Bank as pilot schemes on experimental basis. The purpose was to intensify credit facilities to the SSCIs and to develop in the process, expertise of the NCBs in financing small scale and cottage industries particularly in the rural areas of the country. While the success achieved by the NCBs in implementing the schemes has been moderate, it became clear that the banks as profit-seeking organizations, are particularly worried about safety of the loan funds and hence practice utmost caution in lending to the SSCIs.

What seems to be important, the organizayional structure and mode of operation of the commercial banks are such that they have an in-built allergy for not lending to smaller enterprises and are less optimistic of the potential contributions of such

enterprises to the national economy. While the banks had their own views and observations on small industry lending, these need to be juxtaposed with those of the entrepreneurs about the banks and other financial institutions, so that the bottlenecks prohibiting free flow of formal credits to the small scale sector can be properly identified and appropriate solutions found out. It is to these issues we turn next.

CHAPTER 4

THE ENTREPRENEURS VIEWS OF THE LENDING AGENCIES

The analysis in this part of the study examines the views of the sample entrepreneurs about the formalities and problems involved in borrowing from the institutional lending agencies. The entrepreneurs are, as noted earlier, the respondents from the eleven survey thanas covered by the Core study.

However, the attempt to examine the respondents' attitude towards the lending agencies needs to be preceeded by an analysis of a number of important issues. These include the entrepreneurs' perception about financial constraints, type of credit (i.e. fixed or working capital) needed by them to finance their operations, extent of their dependence on borrowed funds in raising both initial and expansion capital, sources of funds used, and costs incurred in obtaining funds from the available sources. This will help identifying the respondents' requirements for type of credit and their degree of accessibility to the institutional agencies supplying such credits.

4.1 Entrepreneurs' Perception about the Financial Constraints

On the question of problems faced in starting their enterprises, the majority of the respondents identified lack of adequate funds for acquiring fixed assets and for meeting working capital needs as a major constraint irrespective of their locational characteristics.

The distribution of the respondents by problems faced in different locations is shown in Appendix Table A. 1. It is seen from the Table that of the total problems stated by the respondents[1], finance is stressed as the major obstacle in more than two-thirds (68 per cent) of the cases in all locations. The same was found to hold good for the majority of the respondents irrespective of their occupational origin and type of industries owned and operated by them[2].

Though the respondents perceive both fixed and working capital to be their major initial constraints, lack of funds for meeting working capital needs appears to be their primary concern. In ascertaining different areas of assistance sought from the government[3], the majority of the entrepreneurs express their need for working capital (Table 8). As revealed by the data in table 8, more than 80 per cent of the entrepreneurs, irrespective of location and industry type, indicate their need for working capital assistance.

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1. Because of citing multiple problems by many respondents as the first, second and thrid initial constraints, total number of responses (i.e. 1238, in appendix table A.1) exceeded the number of respondents (949).

2. Cf. "Finance" - Chapter 9, Phase II Final Report, RISP-BIDS, February 1981

3. The questions asked to the entrepreneurs were, (i) Do you need any assistance from the government in running your enterprises? (ii) If yes, identify three fields in which you need most assistance.

TABLE 8

DISTRIBUTION OF THE ENTREPRENEURS INDICATING THE NEED FOR DIFFERENT TYPES OF ASSISTANCE BY LOCATION AND INDUSTRY TYPE

Types of assistance needed	% of the entrepreneurs indicating the need for assistance			
	Rural (N=932)	Urban (N=199)	Small (N=236)	Cottage (N=953)
Obtaining machinery and other fixed assets	48.9	100.0	55.1	78.4
Obtaining raw materials	70.5	50.3	68.9	61.4
Credit for working capital	84.8	82.4	85.3	77.5
Domestic marketing	29.9	6.0	28.3	12.3
Technical know-how and improved product designs	15.3	8.0	16.1	4.7
Infrastructural facilities (electricity, gas, water)	10.3	15.1	9.5	13.1
Staff training	1.4	5.5	1.3	5.5
Protection from large industry and imports	8.3	4.5	6.8	11.1
Tax relief	2.8	7.5	2.0	8.5
Export facilities	10.8	6.5	9.3	10.6

Note : N= Number of respondents.

That the financial constraints of the small entrepreneurs relate largely to their working capital needs is also supported indirectly by the pattern of utilization of funds borrowed by them from institutional sources (Table 9). It is seen from the Table that the lion's share of the institutional loans received by the borrowers has been utilized for meeting the working capital needs irrespective of their location.

Though the proportion utilized to meet working capital needs is found to be 79 per cent for all locations, it is as high as 93 per cent for the enterprises located in the market place.

TABLE 9

PROPORTION OF INSTITUTIONAL LOANS USED FOR VARIOUS PURPOSES

Heads of loan utilization	Location			
	Village	Market place	Town	All locations
Building for the enterprise	(0.5)	-	(5.6)	(4.6)
Purchase of machinery and equipment	(26.2)	(6.6)	(10.2)	(11.7)
Working capital	(70.1)	(93.4)	(79.8)	(79.6)
Consumption	(2.9)	-	-	(0.3)
Others	(0.3)	-	(4.4)	(3.7)
Total	(100.0)	(100.0)	(100.0)	(100.0)

Note: '-' Indicates nil.

Further, except for two size groups (with 2 and 20 and more employees) more or less similar picture emerges also from the data in Table 10. In the case of most of the size groups of enterprises, major proportion of the borrowed funds is found to have been utilized for meeting working capital needs followed by the proportion utilized for purchasing machinery and equipment and construction of factory buildings.

TABLE 10

PROPORTION OF INSTITUTIONAL LOANS USED FOR VARIOUS PURPOSES BY SIZE OF ENTERPRISES

Size groups (No. of workers)	Heads of loan utilization					Total
	Building for the enter-prise	Purchase of machi-nery and equipment	Working capital	Consumption	Others	
1	-	-	-	-	-	-
2	(15.00)	(40.0	(35.0)	(10.0)	-	(100.0)
3	-	(39.7)	(45.4)	-	(14.9)	(100.0)
4 - 5	(19.5)	(32.1)	(47.7)	(0.7)	-	(100.0)
6 - 9	(2.3)	(8 .5)	(88.2)	(0.8)	(0.2)	(100.0)
10 - 19	-	(5.9)	(91.6)	(0.3)	(2.2)	(100.0)
20 +	(33.6)	(39.6)	(10.8)	-	(16.0)	(100.0)
All sizes	(4.7)	(11.7)	(79.6)	(0.3)	(3.7)	(100.0)

Note: '-' Indicates nil.

On the contrary, the fact that very small proportion is spent on working capital and nothing on consumption by the largest size group may suggest that the bigger enterprises suffer relatively less from cash - flow problems. That this might be a valid approximation is also indicated by the fact that the largest size group has spent the highest proportion (33.6 per cent compared to an overall average of 4.7 per cent) of institutional loans for constructing factory buildings and for purchasing machinery and equipment (39.6 per cent compared to an overall average of 11.7 per cent). It is thus possible that expansion of fixed assets

was easier for the large enterprises as their need for loans for meeting working capital requirements was relatively less pressing.

This and similar evidence provided by others[1] for many developing countries tend to confirm that the small-scale entrepreneurs are able to start on a schoestring, but many of them may fail to grow and sustain because of lack of adequate flow of credit to meet short-term operating expenses.

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[1] See, for example, McCrory, J.T. Small Industry in a North Indian Town, Ministry of Commerce and Industry, Government of India, New Delhi, 1956; Haggblade, S. et. al. "Small Manufacturing and Repair Enterprises in Haiti; Survey Results" Michigan State University Rural Development Series, Working Paper No. 4, Department of Agricultural Economics, Michigan State University, 1979; Patel, V.G. "Innovations in Banking: The Gujrat Experiments", Domestic Finance Studies, No. 51, Development Economics Department, World Bank, Washington, D.C. 1978.

4.2 Sources of Funds Used by the SSCIS for Financing Initial and Expansion Capital

The analysis of the relative contribution of various sources of funds to the total initial and expansion capital of the sample enterprises reveals that self-financing through personal savings and ploughing back of profits has been the dominant source of funds for the majority of the enterprises.

As revealed by the data in Table 11, personal savings from agriculture, trade, business and other occupations provided slightly below 50 per cent of the funds needed for establishing rural industries in Bangladesh, followed by cash received through sales of land and other assets. In fact, the share of personal savings in the total initial capital was found to vary between 50 and 100 per cent in case of most of the industries[1] and the share of loans in the total initial capital very insignificant in most cases.

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[1] Similar proportions are reported by Liedholm and Chuta (1976) op. cit. for Sierra Leone; Child Frank, et. al. Proceedings of a conference on Small Scale Enterprise, Occassional Paper No. 6, Institute for Development Studies, University of Nairobi, 1973, for Kenya and by Harris, John R. "Nigerian Entrepreneurship in Industry", in Growth and Development of the Nigerial Economy, edited by C. Eicher and C. Liedholm, Michigan State University, 1970, for Nigeria.

TABLE 11

PROPORTION OF INITIAL CAPITAL CONTRIBUTED BY VARIOUS SOURCES OF FUNDS BY BROAD INDUSTRY CATEGORIES.

Industry sector	Personal savings from			Selling of assets		
	Agriculture	Other sources	Total (2+3)	Land	Other sources	Total (5+6)
1	2	3	4	5	6	7
Food and agriculture	(26.63)	(21.74)	(48.37)	(14.08)	(5.21)	(19.20)
Wood cane & bamboo products	(5.36)	(22.36)	(27.72)	(2.91)	(1.30)	(4.21)
Paper & paper products	(30.72)	(33.79)	(64.51)	-	-	-
Pharmacuetical & chemicals	(33.84)	(35.56)	(69.40)	-	(0.70)	(0.70)
Glass and ceramics	(23.81)	(43.15)	(66.96)	-	-	-
Rubber, leather & plastics	(4.65)	(21.54)	(26.19)	(12.13)	-	(12.13)
Textiles	(10.79)	(24.34)	(35.13)	(6.92)	(2.40)	(9.32)
Metal works	(3.76)	(49.89)	(53.45)	(3.14)	(6.51)	(9.65)
Repairing services	(14.00)	(48.34)	(62.34)	(14.35)	(9.83)	(24.18)
Column total (all sectors)	(21.46)	(27.71)	(49.17)	(10.52)	(4.53)	(15.05)

Note : '-' Indicates nil

TABLE 11 (Contd.)

Industry sector	Cash from inhare-tance and dowry	Partners contri-bution	Loans	Others	Row total
8	9	10	11	12	13
Food and agriculture	(1.14)	(0.37)	(3.22)	(27.61)	(100.0)
Wood cane & bamboo products	(22.97)	(1.30)	(4.83)	(38.96)	(100.0)
Paper & paper products	(30.72)	(2.27)	(2.52)	-	(100.0)
Pharmacuetical and chemicals	(25.84)	-	(0.30)	(3.72)	(100.0)
Glass and ceramics	(8.93)	(8.93)	(15.18)	-	(100.0)
Rubber, leather and plastics	(2.27)	-	(0.66)	(58.73)	(100.0)
Textiles	(12.92)	(0.30)	(5.49)	(36.84)	(100.0)
Metal works	(4.40)	(15.78)	(3.55)	(10.98)	(100.0)
Repairing services	(8.03)	(2.18)	(3.09)	(0.18)	(100.0)
Column total (all sectors)	(6.73)	(2.02)	(3.35)	(23.65)	(100.0)

Again, whatever amount was borrowed by the respondents in financing their initial capital requirements, most of it came from the non-institutional sources. The relative contribution of various sources of loans to total amount borrowed by the entrepreneurs in financing their initial capital requirements is presented in Table 12. It is be seen from the Table that of the total amount borrowed by the entrepreneous slightly less than 80 per cent was contributed by the non-institutional lenders and the rest came from the institutional lending agencies. Within the non-institutional sources, friends and relatives were the dominant contributors, followed by the local money lenders.

The relative high incidence of borrowing from friends and relatives may not be surprising given that it might have been relatively easier for the borrowers to approach such lenders and to obtain loans from them on more of flexible terms than those received from the other creditors.

The limited availability of funds from the institutional sources for financing initial capital requirements of the SSCIs is identified by many studies[1] to be a consequence of the existence of scale barriers to entry by such enterprises in the

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[1] Cf. Lee, S. Dennis, Financial Facilities for Small Firms, Committee of Enquiry on Small Firms, Research Report No.4, London, HMSO, 1971; M.C. Gupta, "The Effect of Size, Growth and Industry on the Financial Structure of Manufacturing Companies". June 1969, K.A. Yeomans, Company Finance and the Capital Market: A Study of the Effects of Firm Size, London Cambridge University Press, 1974.

TABLE 12

PROPORTION OF LOAN FOR FINANCING INITIAL CAPITAL (BY SOURCE OF LOAN)

Sources of loan	Amount of loan (in taka)	% of total	Average size* of loans in taka
Commercial Bank	24,000	15.1	8000.0
Other government agency	9,000	5.7	9000.0
Co-operative	350	0.2	150.0
Sub-total of institutional sources	33,350	20.9	4168.8
Local money lender	20,890	13.1	1044.8
Wealthy people other than the money lender	3,070	1.9	383.8
Friends and relatives	99,295	62.5	2309.2
Sub-total of non-institutional sources	123,255	77.6	1735.9
Other sources	2,300	1.5	575.0
Grand total	158,905	100.0	1914.5

* Calculated by dividing the total amount of loan received from various sources by the number of loans obtained from them.

organized capital market. It is argued that lack of knowledge of the institutional lending agencies about the affairs of the SSCIs and their characteristic deficiencies in offering adequate collateral confront them with greater difficulties compared to their large counterparts even in obtaining short-term loans from the institutional lenders.[2]

The limited use (availability) of external funds in general and that of institutional loans in particular by the SSCIs is also confirmed by the data presented in Tables 13 and 14, which show the relative contribution of various sources of funds towards expanding fixed assets by the sample enterprises in fifteen major rural industries of Bangladesh.

The data presented in Table 13 reveals that reinvestment of profits alone provided more than 70 per cent of the funds required for expansion of fixed assets by most rural industries

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[2] The validity of this argument in the case of the small and cottage enterprises in the rural areas of Bangladesh is varified in a later section of this study.

TABLE 13

CONTRIBUTION OF VARIOUS SOURCES OF FUNDS
TO FIXED CAPITAL EXPANSION BY MAJOR INDUSTIRES

	Reinvestment of profit	Personal savings from agriculture	Personal savings from other sources	Sale of land	Sale of other assets
Handloom product	70.48	6.94	5.20	3.29	3.95
Coir product	95.10	3.41	1.19	0.30	0.0
Gur making	100.0	0.0	0.0	0.0	0.0
Grain crushing	94.52	0.09	5.29	0.0	0.0
Cane & bamboo mat cover	71.01	28.99	0.0	0.0	0.0
Wooden transport and equipement and tools	100.0	0.0	0.0	0.0	0.0
Miscellaneous textile	66.67	0.0	0.0	20.0	0.0
Tobacco manufacturing	68.83	3.01	10.19	0.0	0.0
Basketary	85.42	0.0	14.58	0.0	0.0
Vegetable oil	59.38	5.29	1.19	0.0	0.0
Pottery products	100.0	0.0	0.0	0.0	0.0
Dairy products	60.37	0.52	0.0	0.0	0.0
Silk products	100.0	0.0	0.0	0.0	0.0
Blacksmithy	83.79	14.59	0.0	0.0	1.62
Column total (all major industries)	73.25	2.78	6.87	0.62	0.63

TABLE 13 (Contd.)

	Partners contri-bution	Loans from banks and other govt. agencies	Loans from non-institu-tional sources	Row total
Handloom product	0.25	6.28	3.61	100.0
Coir product	0.0	0.0	0.0	100.0
Gur making	0.0	0.0	0.0	100.0
Grain crushing	0.0	0.0	0.0	100.0
Cane & bamboo mat cover	0.0	0.0	0.0	100.0
Wooden transport and equipment and tools	0.0	0.0	0.0	100.0
Miscellaneous textile	0.0	0.0	13.33	100.0
Tobacco manufacturing	0.0	17.98	0.0	100.0
Basketary	0.0	0.0	0.0	100.0
Vegetable oil	34.13	0.0	0.0	100.0
Pottery products	0.0	0.0	0.0	100.0
Dairy products	0.0	29.11	0.0	100.0
Sil products	0.0	0.0	0.0	100.0
Blacksmithy	0.0	0.0	0.0	100.0
Column total (all major industries)	2.61	10.86	2.39	100.0

TABLE 14

PROPORTION OF LOAN (FOR FINANCING FIXED CAPITAL EXPANSION) BY SOURCES OF LOAN

Sources of loan	Amount of loan in Tk.	% of total	Average size* of loans in Tk.
Commercial bank	289450	34.9	20675.0
Other govt. agencies	500	0.1	500.0
Co-operatives	1450	0.2	362.5
Sub-total of institutional sources	291400	35.1	15336.8
Local money lender	151585	18.3	1595.6
Rich persons	39250	4.7	1353.4
Friends and relatives	342584	41.3	1189.5
Sub-total of the non-institutional sources	533419	64.3	1229.1
Other sources	5180	0.6	235.5
Grand total	829999	100.0	1832.2

* Calculated by dividing the total amount of loans received from various sources by the number of loans obtained from them.

in Bangladesh[1]. On the contrary, flow of external funds either from formal or from informal credit markets has been found to be negligible. The funds received by the fifteen major rural industries as loans from institutional and non-institutional sources comprised only 10 per cent and 3 per cent respectively of the total expansion capital. This points to scarce dependence of the SSCIs on external funds in general and on formal sources of credit in particular not only at foundation (as shown earlier in Tables 11 and 12) but also during their subsequent expansion.

While the institutional sources appear to be relatively more important (Table 14) in terms of their share (35 per cent) in the total amount borrowed by the sample for financing fixed capital expansion compared to the share of such loans (40 per cent) in the total amount borrowed by fifteen major rural industries (Table 13), the non-institutional lenders still remain the dominant contributors (64 per cent) to the borrowed capital. And as in the case of loans for initial capital, friends and relatives appear to have contributed the largest proportion of the total expansion capital borrowed by the sample entrepreneurs, followed by the local money lenders within the non-institutional lenders.

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[1] The dependance of small-scale enterprises on self-financing for fixed capital expansion to a similar extent is also reported by Liedholm and Chuta, op. cit. for Sierra Leone, Davenport, op. cit. for India, E.W. Nafziger, "The Effect of Nigerian Extended Family on Entrepreneurial Activity" Economic Development and Cultural Change, Vol.18, NO.1, 1969, for Nigeria and Ahmed M.U., op. cit. for Ireland.

The heavy dependence of the rural industrial entipreneurs on internal financing as opposed to external borrowing particularly from the formal credit market both during foundation and subsequent expansion of their operations might reflect either reasonable rates of return accrued to them from the rural industries or a restructed flow of credit to them from the organized capital market. Of these, the last appears to be more plausible explanation in that the returns per hour of family labour in rural industry (Tk.1.86), though marginally higher than the wage rate (Tk.1.25) of agricultural labourer, appear to be substantially lower than that for owner cultivators producing either traditional variety (Tk. 2.90) or HYV rice (Tk.6.30). Further, the rate of profit in industries, though found to be positive for the sector as a whole it has been found to be negative in the case of a number of sample industries. This suggests that the limited use of external funds by the rural industrial intrepreneous in Bangladesh is not a matter of choice, but a consequence of their restricted access to such funds particularly from the formal credit market. And it is an explanation of the restricted access of the SSCIs to institutional sources of credit to which we turn next.

4.3 Factors Responsible for Limited Use Availability of Institutional Loans - the Entrepreneurs Views

One way of identifying the factors responsible for limited availability of institutional loans to the sample entrepreneurs may be to examine their own perceptions about the difficulties involved in obtaining them. This is done through analysing the replies of the respondents as to the reasons for not taking institutional loans as well as to the problems actually encountered by them in obtaining such loans respectively in Appendix Tables A.2 to A.6 and A.7 to A.11. The data in these tables are arranged by certain indicators of socio-economic status of the entrepreneurs assumed to exert considerable influence on the nature and intensity of the different obstacles affecting the respondents differently.

Appendix Tables A.2 to A. 6 reveal that of the various reasons given by the respondents for never taking institutional loans, lack of knowledge about availability of such loans was most dominant (38.4 per cent) followed by their inability to offer security (15 per cent) against the loans and the complicacies involved (11 per cent) in obtaining an institutional loan. While 5 per cent of the respondents gave no reason for never taking an institutional loan, 9 per cent of them indicated that they never felt the necessity for taking a loan from the institutional sources.

Another notable feature emerging from the data in most of the tables is that none of the difficulties perceived by the respondents appears to bear any clear pattern of association with their socio-economic status and business experience as indicated by social role of the entrepreneurs in the community, extent of land owned by them, level of per capita income, level of education and age of their enterprises. It is only in the Appendix Table A.5 that the proportion of respondents mentioning ignorance about the availability of institutional loans appears to decline consistently as we move towards more educated groups of the entrepreneurs. The other case in which an expected inverse relationship between the entrepreneurs economic status and the reason given by them for not taking institutional loans can be observed is that between lack of security and level of per capita income. As seen from the data in Appendix Table A.4, the proportion mentioning lack of security as a reason tends to decrease with increase in the level of per capita income of the entrepreneurs.

However, as mentioned earlier, the reasons given by the entrepreneurs for not borrowing from institutional sources are only their own perceptions and may, therefore, differ from the problems actually faced by them in obtaining loans from the institutional agencies. This is borne out by the data presented in Appendix Tables A.7 to A.11 as the ranking of relative importance of the problems encountered by the

entrepreneurs in obtaining loans from the institutional sources, lack of ability to offer security rather than ignorance topped the list followed by the official formalities involved in getting an institutional loan, ignorance of the borrowers about the sources of loans, payment of unofficial expenses in the form of bribes and the longer time required to get a loan. Again, payment of unofficial expenses, though perceived to be a minor problem appears to have posed considerable difficulties to the borrowers in getting a loan from the institutional sources.

Thus, to reiterate, the problems perceived by the entrepreneurs may not always represent those actually encountered by them in obtaining loans from the institutional sources, but may reflect partly an inertia not to approach them because of cumbersome official formalities[1].

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[1] Indeed, it is well documented in the literature (cf. P. Clarke, Small Business: How They Survive and Succeed, London David and Charles Publishers, 1972) that the typical small owner-managers are not only unable to find time to keep their books and accounts up-dated and go to a bank because of doing everything by themselves in running the "one-man show" but also highly skeptical at times to allow a bank manager to see their balance sheet position because of their mistrust of others.

Like in the Appendix Tables A.2 to A.6, the nature and degree of intensity of the problems cited by the entrepreneurs appear to have no consistent relationship with their socio-economic status, locational characteristics and business experience. It is only in Appendix Tables A.8 and A.10 that an expected inverse relationship between the entrepreneurs economic status and lack of ability to offer security against the loan and that between their ignorance about the sources of loans and level of education appears to hold good. As seen from these Tables, the proportion citing lack ofsecurity as a problem tends to decrease with increase in the extent of land owned by the entrepreneurs and that mentioning ignorance as a problem diminishes with a rise in the educational standard of the entrepreneurs. The implication is that the stronger the economic position of the borrowers, the less the problem faced by them in offering security against the loan. Similarly, the higher the level of education the borrower possesses, the lesser the information gap he faces about the sources of availability of a loan.

Given the stringent collateral requirement for institutional loans as indicated by the data in Table 15, it is hardly surprising that inability to offer security has emerged as the major barrier to taking a loan from an institutional lending agency. The value of security offered (usually in terms of items like land, buildings, other fixed assets of the enterprise and miscellaneous real assets) by the sample

TABLE 15

VALUE OF SECURITY AS % OF LOAN (FOR FINANCING INITIAL CAPITAL) BY SOURCE OF LOAN

Source of loan	Value of security as % of loan (average percentage)
Commercial bank	444.4
Other govt. agencies	122.2
Co-operatives	250.0
Sub-total	275.0
Local money lenders	189.8
Wealthy people	0.0
Friends and relatives	2.3
Other sources	0.0
Sub-total	54.86
Grand total	73.43

borrowers as percentage of loans from the institutional sources is, in general, quite high (275 per cent) rising upto 400 per cent and above for loans advanced by the commercial banks[1].

[1] In fact, the security requirement for loans taken by the sample borrowers from the institutional sources in expanding their fixed assets was also found to be more or less equally rigorous as in the case of loans taken from such sources in financing their initial capital. The value of security offered by them as percentage of loans from the institutional sources was found to constitute 252.8 per cent compared to 15.6 per cent for loans taken from the non-institutional sources.

In contrast, the collateral requirements for loans from non-institutional sources are comparatively less stringent (54.86 per cent) and this is specially so for loans obtained from friends and relatives. In fact, as seen from the data in the Table, the collateral requirements for loans obtained from the wealthy people and other miscellaneous sources apper to be nil. And this is the reason for which the value of security as percentage of loans from all sources together -- institutional and non-institutional, becomes on average less than 100 per cent of the total amount borrowed from them.

Next to lack of security, the requirement for completing too much official formalities in getting an institutional loan is identified as the other important constraint by the respondents. This is quite consistent with our findings in section 2.6 where it was found that the documentation requirements set by the institutional lending agencies is too elaborate and complicated to be met by the typical small entrepreneurs, majority of whom are illeterate and keep no records of their business[1].

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1. Indeed, it is the borrowers' inability to comply with such complicated documentation requirements that many of the small borrowers were reported to have failed to avail the credit facilities offered to them through the BSCIC-BSB joint lending programme introduced by the government in 1963. cf. BSCIC, proposal To Asian Development Bank For Financing Small Industries in East Pakistan, July 1969. pp. 17-19.

Besides the characteristic deficiencies of the small borrowers, further complications introduced to the lending procedures through certain deliberate actions of the institutional lenders make them even more reluctant to use formal credits.

First, the institutional lenders tend to avoid handling of small loans because of relatively high transaction costs and greater risks arising from the lack of adequate knowledge about the affairs of the small borrowers. Second, they also tend to complicate the lending procedures for such borrowers in order to assist governments policy of rationing the sacrace loan funds, especially when interest rates are set at concessional terms for the large-scale borrowers[1].

High interest rates charged on small loans from the institutional sources as penalties for covering higher service charges and greater risks involved in such loans, though sometimes believed to restrict access of the small borrowers to the institutional lending agencies[2], did not appear to have

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[1] See, for a survey of evidence, D.W. Adams and G.I. Nehman, "Borrowing Costs for Agricultural Loans in Low-Income Countries", The Journal of Development Studies, January, 1979.

[2] Evidence of higher interest charges paid on institutional loans by small firms vis-a-vis their large counterparts is provided by K. Miazawa, "The Dual Structure of Japanese Economy and its Growth Pattern", Development Economics, June, 1964.

posed difficulties to the small entrepreneurs in the rural industries sector of Bangladesh (Table 16). As seen from the data in the Table, the average percentage rate of interest paid by the sample borrowers against loans from commercial banks was quite consistent with the interest rate (11.5 to 12 per cent) paid by the industrial investors for such loans in the country as a whole during the financial year 1978[3].

However, the average interest charges (18.1 per cent) paid by the borrowers in the rural industries sector of Bangladesh for loans from the non-institutional sources is more than double the market rate paid for the institutional loans (Table 16)[4]. In fact, as indicated by the figures in parenthesis in the Table, the interest rate charged by the non-institutional lenders shoots upto more than 60 per cent on average if we exclude those borrowers from the sample who appear to have received interest-free floans from different non-institutional lenders.

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[3] World Bank, Bangladesh - Issues and Prospects for Industrial Development, Report No.2191, Volume I, December, 1978.

[4] The evidence of higher interest rates charged by the non-institutional lenders compared to those charged by the institutional agencies is also provided by J.C. Saha, "A Case of Differential Interest Rates for Rural Poor", Problems and Issues of Agricultural Credit and Rural Finance, Bangladesh Bank, Dacca, September 1979, pp. 72-79; for Bangladesh and by the IBRD, 1974, op. cit. for Korea and Colombia.

TABLE 16

RATE (AVERAGE PERCENTAGE) OF INTEREST ON LOANS FOR FINANCING INITIAL CAPITAL) BY SOURCES OF LOAN

Sources of loan	Rate of interest (weighted average of percentages) (a)
Commercial Bank	11.7
Other Government Agencies	9.0
Co-operatives	4.0
Sub-total	8.1
Local money lenders	38.5 (57.7)
Wealthy people other than money lenders	18.0 (48.0)
Friends and relatives	8.6 (97.0)
Sub-total	18.1 (63.8)
Others	0.0
Grand total	15.9

Note: (a) Average percentages of the rate of interest in the parenthesis represent the average rates paid by the borrowers excluding the cases of those who took loans from the non-institutional lenders without paying interests.

Turning to Table 17 it can be observed that the rate of interest paid on all loans -- institutional and non-institutional, appears to decrease with increase in the loan size except for the largest size group, suggesting a consistent inverse relationship between interest cost and loan size. Theoretically, such a relationship can be expected a priori given that a decline in the rate of interest is met by an increase in the demand for credit.

In case of our sample, the high interest rates for smaller loans may be explained by the fact that as most such loans (i.e. 93.2 per cent of all loan cases falling within the size range of Tk. 99 to 500) are obtained from high-cost, non-institutional sources, the borrowers have to pay more for them than for the loans obtained from the institutional sources[1]. In contrast, while the average size of institutional loans is much larger the rate of interest charged on them is both relatively low and by and large invarient with the loan size.

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[1] It is to be noted, however, that though the interest charges are relatively low for institutional than for the non-institutional loans the real cost of obtaining (when measured in terms of various formalities involved and miscellaneous official and unofficial expenses incurred) the former may be higher than that for the latter. This remains to be explored in a relevant part of the subsequent analysis.

TABLE 17

RATE OF INTEREST (AVERAGE PERCENTAGE) ON LOANS (FOR FINANCING INITIAL CAPITAL) BY SIZE OF LOAN

	Rate of interest - (average of percentage)
Upto Tk. 99	40.0
Tk. 100 to 500	23.5
Tk. 501 to 1,000	13.2
Tk. 1,001 to 5,000	5.4
Tk. 5,001 to 5,000	6.9
All sizes	15.9

While an inverse relationship between interest cost and loan size is also found to hold good (except for the loan size Tk. 1000 to 2500) in case of interest charges paid by the sample borrowers on loans taken by them for financing fixed capital expansion (Table 18), by far the most notable findings emerge from the data in Table 19 which examine the relationship between level of education of the sample borrowers and the interest rates paid by them on the loans raised for financing expansion of their business. As seen from the Table, the average rate of interest paid by the borrowers on all loans - institutional and non-institutional, decreases consistently with increase in the level of education of the borrowers, suggesting an inverse relationship between cost of loan and educational background of the sample borrowers.

TABLE 18

RATE OF INTEREST (AVERAGE PERCENTAGE) ON LOANS (FOR FINANCING FIXED CAPITAL EXPANSION) BY SIZE OF LOAN

Size of loan	Rate of interest (weighted average of percentages)
Upto Tk. 100	185.5
Tk. 100 to 500	128.4
Tk. 500 to 1,000	68.9
Tk. 1,000 to 2,500	78.2
Tk. 2,500 and above	57.2
All sizes	135.1

TABLE 19

RATE OF INTEREST (AVERAGE PERCENTAGE) ON LOANS (FOR FINANCING FIXED CAPITAL EXPANSION) BY LEVEL OF EDUCATION OF THE BORROWERS.

Level of Education	Rate of interest (weighted average of percentages)
No education	163.5
Upto primary level	146.8
Primary to secondary	90.8
Secondary and above	10.3
All borrowers	135.1

Among other things, ignorance of the illeterate and less educated borrowers about the terms and conditions of loans along with their consequent low bargaining capacity compared to their enlightened counterparts, might be responsible for higher costs of borrowing faced by them[1]. Indeed, as shown in a later section of our analysis, compared to more urbanized and wealthy borrowers, the relatively high official as well as unofficial expenses (in the form of bribes) incurred by the landless and near-landless borrowers, located in the villages in borrowing from the institutional sources, appeared to be an outcome of the illeteracy, lack of knowledge about the rules of borrowing and low bargaining capacity.

The findings emerged from the foregoing analysis have several important implications. First, lending by commercial banks compared to other institutional lending agencies is highly security oriented. Their lending operations appear to

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[1] Admittedly, part of the high interest charges paid on loans by the less educated borrowers may also be explained by the fact that they might be engaged in relatively low income-generating industrial pursuits where the investors would be less willing to invest. Funds for financing such activities may thus be available only at a higher cost covering the greater risks of defaults.

be geared primarily to secure and profitable pursuits such as larger industrial units at the neglect of small and cottage type enterprises, because of greater risks involved in lending to the latter[1]. Consequently, the small entrepreneurs in the rural industries sector of Bangladesh are forced to depend more on the financial intermediaries to raise the necessary investment funds, though the cost of borrowing from them is exhorbitantly high.

Second, the differential interest rates charged on loans by the institutional and non-institutional lenders is indicative of the existence of structural dualism in the markets for lonable funds. The structural dualism manifests itself in the form of existence of an organized capital market consisting of a fairly competitive banking system on one side and an unorganized market comprising the money lenders, wealthy people and other financial intermediaries on the other side. In the unorganized part of the capital market, credit policy of the government is often of little or no direct influence, interest rates are high, and borrowing terms are usually more stringent.

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[1] However, part of the reluctance of the institutional lending agencies in lending to the small enterprises may also be a reflection of their overcautions estimates of the risks of default involved in small lending and an understimation of the repayment and growth potential of such enterprises. Because evidence provided by Steel, op. cit., from Ghana and by the Economists Advisory Group, Problems of the Small Firms in Raising External Finance - the Results of a Sample Survey, Bolton Enquiry Committee, Research Report No.5, London 1971 and by J. Boswell. The Rise and Decline of Small Firms, London, Gorge Allen and Unurin, 1972, from U.K. show that small borrowers actually repay better than their large counterparts. Hence, repayment risks for small loans may not be as high as the institutional lenders usually apprehend.

Another important bottleneck affecting the borrowers and identified by them as a serious problem in taking loans from institutional sources is the payment of official expenses (i.e. legal fees) and unofficial fees in the form of bribes[1]. Indeed, as shown by the data in Table 20 the official fees, unofficial payments and miscellaneous expenses incurred by the borrowers in taking loans from various a considerable proportion (3.45 per cent) of the amount borrowed. Such expenses incurred in borrowing from other government agencies (i.e. Krishi Bank, Shilpa Bank, Handloom Board etc.) appear to be the highest followed by that incurred for loans .....

TABLE 20

COST (OFFICIAL: UNOFFICIAL AND MISCELLANEOUS EXPENSES AS % OF LOAN) OF INSTITUTIONAL LOAN AS PERCENTAGE OF LOAN BY SOURCES OF LOAN.

Source of loan	Cost of loan (average %)
Commercial bank	2.39
Co-operative	4.17
BSCIC	2.08
Other government agencies	5.81
All sources	3.45

[1] For evidence in support of the fact that the payment of bribes has been an outcome of the rampant frauds and forgeries existing particularly in the rural branches of the nationalized commercial banks in the country, see, L.R. Sarkar, "Need For A change in the Organizational Structure of the Commercial Banks", Finance and Development Vol. 1, June 1979. pp. 76-85.

from the co-operatives. In this context, an important finding emerges from the data in Table 21 which exhibits a systematic inverse relationship between size of loan and cost of loan. Except for the smallest size group of loan (against which no loans were found to have been taken by the borrowers) the cost of borrowing is found to decrease steadily with increase in the loan size.

TABLE 21

COST (OFFICIAL FEES, UNOFFICIAL FEES AND MISCELLANEOUS EXPENSES AS % OF LOAN) OF INSTITUTIONAL LOAN AS % OF LOAN BY SIZE OF LOAN

Size of loan	Cost of loan (average %)
Upto Tk. 99	0.0
Tk. 100 to 500	6.26
Tk. 501 to 1000	4.0
Tk. 1001 to 5000	3.20
Tk. 5001 to 50,000	2.71
All sizes	3.45

Two plaussible reasons may be offered to explain these differentials in the cost of borrowing. First, as institutional loans have certain elements of fixed costs (i.e. legal fees, book-keeping expenses and so on) lending larger amount permits scale economies reducing thereby the per unit cost of loans. On the contrary, as the small borrowers

take, by assumption, smaller loans, the fixed administrative costs become higher and give rise to dis-economies of scale. Thus, the relatively high cost involved in small loans may partly reflect higher transaction costs.

Second, given the characteristic weaknesses of the small borrowers (i.e. illeteracy, lack of knowledge about the rules of borrowing etc.) it might be easier for the corrupt officials to charge more from them in the form of bribes than from the elitist large borrowers. Indeed, the data presented in Table 22 and 23 tend to confirm this indirectly. The observations made from these tables may hold good under two assuptions.

If it is assumed that the relatively more urbanized borrowers are comparatively better informed about the rules and formalities of institutional lending than their less knowledgeable counterparts in the villages, the higher cost facing the borrowers located in the village areas (Table 22) may reflect the penalites paid (in terms of high unofficial expenses) by them for their ignorange and weak bargaining capacity.

Similarly, if it is assumed that the bigger landlords (having by assumption a stronger socio-economic power base in a country where land is the principal source of wealth) are more able than their landless and near lardless counterparts to bend the terms of loan to their favour, then the above argument as to the inverse relationship between loan size and cost of loan is also proved to be valid by the data in Table 23. Except for the 1-5 acre land-owning group of borrowers

TABLE 22

COST OF INSTITUTIONAL LOAN AS % OF LOAN BY LOCATION OF THE ENTREPRENEURS

Location	Cost of loan (average %)
Village	4.30
Market place	3.41
Town	2.44
All locations	3.42

TABLE 23

COST OF LOAN AS % OF LOAN BY LAND OWNERSHIP PATTERN

Land ownership pattern	Cost of loan (average %)
Landless	6.79
Upto 1 acre	2.71
1 to 5 acres	4.79
5 to 10 acres	2.70
All land owing classess	3.78

the cost of loan appears to vary inversely with the land-ownership pattern in that it decreases with increase in the amount of land owned by the borrowers. The relatively high cost incurred for loans by the landless and by the smaller land-owning groups may result from their lower bargaining strength. All these suggest that the cost of borrowing from the institutional sources is, in practice, much higher than revealed by the interest rates paid.

Another important element of cost facing the borrowers is is the longer time required in obtaining an institutional loan. As noted earlier though non-monetary in nature, longer waiting time as well as the working days lost in trying to get an institutional loan are also identified by the sample borrowers as important barriers. That these are genuine difficulties reported by the borrowers, are supported by the data in Tables 24 and 25. While the length of time involved in getting a loan from various agencies is found to vary from 20 days to 157 days, the average time required by all agencies in processing the applications appears to be slightly below three months. This indicates bureaucratic handling of the loan applications by the institutional agencies having the borrowers to face the adverse consequences[1].

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[1] Such longer time required in processing the loan applications is also partly an outcome of the difficulties prohibiting quick decision-making, particularly in the rural branches of the nationalized commercial banks. Though the branch net-works of the commercial banks have been extended to the rural areas, the decision-making authority still lies with the top officials concentrated in their head offices at Dacca. Lack of proper decentralization of decision-making authority, particularly among the financing banks appeared, in practice, to be the most important obstacle to effective functioning of most small industry lending programmes including the special credit programmes.

TABLE 24

AVERAGE NUMBER OF DAYS REQUIRED BY EACH BORROWER IN GETTING AN INSTITUTIONAL LOAN BY SOURCES OF LOAN

Source of loan	Average no. of days lapsed between making the application and getting the loan
Commercial bank	72.4
Co-operative	31.8
BSCIC	20.0
Other government agencies	157.4
All sources	85.6

TABLE 25

AVERAGE NUMBER OF WORKING DAYS LOST BY EACH BORROWER IN GETTING AN INSTITUTIONAL LOAN BY SOURCE OF LOAN

Source of loan	Average no. of working days
Commercial bank	10.5
Co-operative	2.7
BSCIC	10.0
Other government agencies	19.3
All sources	11.5

Indeed, as revealed by the data in Table 25, each borrower had to waste nearly 12 working days on an average in trying to get a loan from the institutional lending agencies. This loss of working days may be explained partly by the number of visits each borrower had to make in pursuing his loan application. It was found that each borrower had to pay a minimum of six visits on average to the concerned lending agency in between making the application and getting the loan.

Finally, ignorance of the small borrowers about the institutional sources of loans was also found to comprise an important barrier to receiving formal credits by the sample entrepreneurs. This may result, in part, from inadequate dissemination of the relevant information by the concerned agencies and in part from a lack of initiative on the part of some of the borrowers to look for the relevant sources of loan.

Our discussion of the SCP in section 3.2 indicated that lack of concerted efforts on the part of the banks to disseminate information regarding the availability of loans under the Programme considerably handicapped its effective operation.

Further, though nearly sixty per cent (58.13 per cent) of the branches of the NCBs operate at present in the rural areas of the country, the overall volume of their operations there is still far behind the urban branches in that they accounted for only 6 per cent of the total bank advances to the

farm and non-farm activities in the entire country during 1978 (A.S.M. Fakhrul Ahsan, 1979). This and similar evidence presented earlier in section 3.2 of the study suggests that lending policies of the commercial banks are geared primarily to financing large industrial undertakings[1]. Except a few special credit programmes, as discussed earlier, there seems to be no credit policies operated by the commercial banks for the SSCIs as such.

Again, whatever adhoc credit provisions are made occassionally for these industries, they do not seem to be administered properly. Lack of trained personnel and the absence of special cells in the banks to deal with the credit needs of the small industrialists pose important barriers to making such programmes adequately effective. In fact, the two other specialized development banks (i.e. BSB and BSRS), though function as the leading agencies for industrial loans in the country, do not appear to have any special credit programme for financing the SSCIs.

Finally, the limited promotional assistance rendered by other government agencies (i.e. DI, BSB and BHB and so on) to the SSCIs is only peripheral to their promotional programmes

[1] While lack of information about availability of credit and procedural difficulties in obtaining it prohibit small industries from entering the credit market, cottage industries do not appear to have access to institutional credit even in principle. The latter usually requiring small amounts do not qualify for submitting loan applications as the minimum loan floor practiced by most agencies (i.e. BSB, BSRS) is too high to make any credit provision for such industries. Indeed, the findings emerged from our analysis in sections 2.2 to 2.6 appear to have substantiated this clearly.

which are geared primarily to servicing the needs of medium to larger industries

The consequence of all these is that small entrepreneurs in the rural industries sector of Bangladesh are left with no choice but to fall back upon the non-institutional lenders even though loans obtained from them are inadequate and bear exhorbitantly high interest rates.

However, the real cost of borrowing from the non-institutional sources rises even further if other elements of exploitation of the small borrowers by their creditors are considered. It is observed, for example, from the data in Table 26 that those borrowers (2.6 per cent of the sample enterprises) who purchased material inputs from their creditors besides taking cash loans, had to pay a price for such inputs which was higher than that prevailing in the market by nearly 2 per cent on average. Such exploitation of the borrowers by their creditors might have resulted from the captivity of the former to the latter because of serious cash-flow problems pertaining to their working capital needs. The problem aggravates even further as the borrowers are also required to sell part (0.35 per cent) of the output to their creditors at a price lower than that prevailing in the market. As shown by the data in Table 27, the borrowers have to pay a rebate of 0.14 per cent on average to their creditors in the form of lower price for their output.

TABLE 26

PAYMENT OF PREMIUM ON INPUT PRICES PAID TO THE CREDITOR BY SIZE OF ENTERPRISES.

Enterprise size (no. of workers)	Premium in %
1	0.33
2	0.47
3	1.65
4 - 5	1.71
6 - 9	1.53
10 - 19	2.47
20 + above	3.14
All sizes	1.50

TABLE 27

REBATE ON OUTPUT PRICE PAID TO THE CREDITOR BY SIZE OF ENTERPRISES.

Size of enterprises (no. of workers)	Remate on out price paid to the creditor (%)
1	0.89
2	0.09
3	0.04
4 - 5	0.06
6 - 9	0.35
10 - 19	0.19
20 + above	0.00
All sizes	0.14

Thus, exceptionally high interest charges, lower price for output and higher price for input together make borrowings from the non-institutional sources not only exceedingly costly but also socially undesirable for the enterpreneurs in the rural industries sector of Bangladesh. The unearned incomes appropriated by the financial intermediaries from the cative borrowers breeds inequalities and leads to further worsening of the already skewed income distribution pattern existing in the rural areas.

However, given the inadquate supply of institutional finance to the rural industries sector, financing by the money lenders, though usurious, might not perhaps be avoided or eliminated altogether at the present state of affairs for many reasons. As demonstrated in relevant parts of the analysis, all categories of the non-institutional lenders are not equally exploitative. Additionally, they are also much more prompt and informal compared to the institutional lenders. What is more important, they sometimes provide funds assuming much greater risks (i.e. without any collateral) which is extremely important for increasing the supply of loanable funds to the typical small borrowers. Viewed in this sense, their terms of financing appear to be less rigid compared to that of the institutional lenders.

It is thus imperative that appropriate steps need to be taken to improve the mode of operation of the financial intermediaries so that they can be made a more constructive element of development financing. An effective approach in this direction may be to increase competition through increasing the flow of institutional finance to the rural industries sector so that both interest rates and other costs associated with non-institutional lending get reduced.

Summary, Conclusions and Policy Recommendations

The purpose of this study has been to assess the contributions of the existing financial institutions of Bangladesh towards meeting the credit needs of small-scale and cottage industries (SSCIS) in the rural areas of the country.

An important feature of the study is that unlike most other studies in the field -- based either on the views of the lending agencies or on those of the borrowers only, the present study has been based on the contiguous views of the parties on either side of the credit market. Such an approach may enable us to identify correctly the forces underlying any disequilibrium (and the reasons thereof) that may exist between the demand for and supply of institutional credit and find appropriate solutions to tackle them.

Consistent with this two - pronged approach, attempts have been made to ascertain the type of credit needed by the SSCIs, the sources used and the terms and conditions faced by them in raising the needed funds from alternative sources of credit. Analysis of these issues is expected to shed light on the intensity of demand of the SSCIs for institutional credit as well as on the degree of their accessibility to the existing credit giving agencies.

CHAPTER 5

SUMMARY CONCLUSIONS AND POLICY RECOMMENDATIONS

5.1 Summary of Findings:

The major findings emerged from the study are as follows:

The majority of the sample entrepreneurs in the rural industries sector of Bangladesh identify finance to be one of their key bottlenecks. Of the various problems encountered by them in starting their business, lack of adequate funds meeting fixed and working capital needs has been identified as the over riding constraint by an overwhelming majority of the entrepreneurs irrespective of their locational characteristics.

The financial problem confronting the sample entrepreneurs relates more to working capital needs than to fixed assets. The entrepreneurs' perception about their need for various types of assistance from the concerned government agencies tends to confirm that lack of working capital is their primary concern. This is further substantiated by the fact that the lion's share of the institutional loans obtained by them is used for meeting the working capital needs irrespective of their location and scale of operations. This, along with the inadequate provision for working capital loans made by most of the existing lending programmes for the SSCIs, further aggravates their cash - flow problems.

Thus, the SSCIs may be able to make a modest start on their own because of generally low requirement for initial capital but many of them may fail to grow and sustain through time due to lack of adequate flow of credit to meet their short-term operating expenses.

The analysis of the sources of initial and expansion capital of the rural industrial enterprises reveals that funding of such enterprises both at foundation and during subsequent expansion is done, in most cases from internal sources. Personal savings from agriculture, trade, business, and other occupations of the entrepreneurs appear to have been the dominant contributors to the initial capital funds required by them in setting up their industries, followed by cash received through sales of land and other assets. In contrast, the share of loans in the total initial capital was found to be insignificant for most rural industries. Again, whatever amount was borrowed by the respondents in financing their initial capital requirements, most of it (slightly less than 80 per cent) came from the non-institutional lenders

The infrequent use of loans as a source of initial capital funds by the sample entrepreneurs seems to be a function of general paucity of loanable funds in the rural areas of the country resulting from the lack of an appropriate credit programme, an underdeveloped capital market, high cost involved in obtaining such funds, and an information gap facing the borrowers about the availability of whatever funds there may exist.

The limited flow of external funds from the capital market in general and from the institutional sources of credit in particular to the rural industries sector of Bangladesh also becomes evident from the analysis of the sources of funds used by the entrepreneurs in financing expansion of their businesses.

The analysis of the relative contribution of various sources of funds to the total expansion capital exhibits that internal financing through re-investment of profits has been the dominant source, providing more than 70 per cent of the funds required for expanding fixed assets by most SSCIs in the rural areas of the country. On the contrary, external financing through institutional and non-institutional borrowing is found to have contributed only 10 and 3 per cent of the total expansion capital respectively. Further, as in the case of initial capital, the predominance of the non-institutional lenders as suppliers of expansion funds also becomes evident from the fact that the non-institutional sources provided nearly two - thirds of the total amount borrowed by the sample entrepreneurs in expanding their fixed assets.

The heavy reliance of the sample entrepreneurs in the rural industries sector of Bangladesh on internal financing (through personal savings and re-investment of profits) as opposed to external borrowing both during foundation and subsequent expansion of their operations has been found to be a consequence of their restricted access to external funds flowing particularly from the organized segment of the

capital market. Indeed, this is strongly supported by the findings emerged from the analysis of the nature and magnitude of involvement of the existing lending agencies in SSCIs financing and the degree of contributions made by them towards meeting the credit needs of such enterprises, particularly in the rural areas of the country.

From mid 1950s to mid 1970s, BSCIC was the principal source of institutional credit for the SSCIs in Bangladesh. Over this twenty year period, the corporation continued to provide financial assistance to the small industrialists in the private sector either separately or jointly, in collaboration with the BSB and the NCBs. It is to be noted in this context that the financial operations of the BSCIC constituted only one aspect of the wide ranging promotional services offered by the corporation ot the SSCIs. While the corporation had thus too much to do as the sole agency directly involved in SSCIs promotion in the country, the operative efficiency of its promotional programmes including that of financial assistance appeared to have been adversely affected by frequent changes in it's organizational structure from time to time.

Under the three loan programmes (i.e. BSCIC loan programme, BSCIC - BSB and BSCIC - Consortium of Commercial Banks Loan Programmes), BSCIC provided a total amount of Tk.131.80 million as loans to roughly 1500 units in the small-scale sector during the period between 1957 - 1977 and generated an estimated private investment of Tk. 56.6 million in the form of equity.

However, given a vast number of small-scale and cottage industries operating in the country, the lending operations of BSCIC were barely enough to meet financial requirements of these industries in any effective manner. A complex of factors were found to be responsible for this.

First, as BSCIC has always been dependent on grants from the government and from various international donor agencies, the magnitude and direction of its lending operations have been influenced by the availability of such grants. Irregular and inadequate availability of loanable funds had thus drastically curtailed it's ability to meet the credit requirements of the SSCIs.

Second, except the BSCIC Loan Programme, whatever funds were available under the BSCIC - BSB and BSCIC - Consortium of Commercial Banks Loan Programmes, major proportion went to the public sector enterprises falling within the upper range of the small industry definition. The bias against lending to the smaller enterprises particularly under the joint BSCIC - BSB Loan Programme seems to have been caused by the fact that BSB is geared primarily to financing larger industrial enterprises and lacks in the kind of organizational set-up needed for assisting the small entrepreneurs of modest means.

Third, an indirect bias against lending to the relatively small enterprises in general and to the cottage enterprises in particular has also been caused by both the BSCIC - BSB and the BSCIC -- Consortium joint programmes because of adopting a rigid approach to lending. Their lending operations appeared to have exhibited urban - orientation, stringent collateral requirements, extensive documentations and cumbersome official formalities.

Fourth, the limited success achieved by the two joint loan programmes seems to have been an outcome of inefficient administration of such programmes. This latter has, in turn, resulted from the split of responsibilities in areas that are and should ideally be interrelated (i.e. apprasial and disbursement of loans, follow-up and collections). But different institutional agencies making decisions on different aspects of a project during appraisal and sanctioning resulted in the institutions blaming each other for mistakes without taking responsibilities for failures. Sometimes, lack of a clearcut demarcation of responsibilities as to different aspects of loan administration in general and to the recovery of loans in particular under the joint loan programmes led to inadequate supervision, leaving bulk of the loans in arrears.

Finally, BSCIC, being essentially a promotional agency, appeared to have lacked in the kind of expertise and dynamism required to meet the credit needs of the SSCIs. In fact, till 1969-70, there was no separate division/department in the corporation for handling the financial operations.

Next to BSCIC, BSB is the other important specialized financial institution involved in financing private sector industries in the country. However, it has no specific programme to extend credit facilities to the SSCIs as such. On the contrary, it could be gathered through information collected from the bank that it generally discourages small loans because of administrative difficulties. Consistent with this restrictive lending policy, only 9.23 per cent and 10.73 per cent of BSBs total financial assistance to the private sector industries went to the small industrialists over the six year period between 1971 to 1977 and during 1978/79 respectively.

Further, the bank's policy to discourage loans below Tk.0.10 million (Tk.10,000) implies that it has no provision at all for financing the cottage industries. In addition to the minimum loan floor, high debt - equity ratio, strict collateral requirements and extensive documentation requirements set by the bank make it exceedingly difficult for the SSCIs to approach it for financial assistance.

BSRS, though the most leading specialized bank for supplying medium and long-term capital for industrial concerns in the country, has no provision at all for financing the SSCIs. While the bank generally discourages lending to the small industrialists, it's minimum (operational) loan floor of Tk.2.5 million excludes both small scale and cottage enterprises from the perview of its credit facilities.

In addition to loan finance, availability of equity finance poses another critical obstacle to the SSCIs. The two important institutional agencies -- ICB and DI, providing equity support (along with other promotional incentives) to both private and public sector industries in the country, are found to have done very little for the SSCIs in this direction. Resource constraints appeared to have led to limited participation by the ICB in providing equity support to all private sector industries in general. DI's preoccupation with too much of control functions in areas other than the promotion of private sector industries and the lack of a special cell to deal exclusively with the SSCIs, seems to have prohibited it from paying adequate attention to the SSCIs.

Like in the case of BSB, BSRS, ICB and DI, the participation of the commercial banks in SSCIs lending is also incidental. The NCBs do not have any separate programme for providing credit facilities to the SSCIs except under the joint BSCIC - Consortium Loan Programme and that operated under the two special credit programmes -- Small Loans Scheme (SLS) and and Special Credit Programme (SCP) of Tk.6 crore, introduced by the Bangladesh Bank in 1978 with a view to intensifying institutional credit facilities to the SSCIs.

However, despite considerable efforts made by the government towards providing the SSCIs with increased credit facilities through participation of the NCBs in small industry financing, very little could be done so far in the direction. For example, loans to SSCIs (including small businesses) comprised only 2 to 4 per cent of the total commercial bank advances during 1975 and 1977.

The contributions of the NCBs towards small industry financing when assessed in terms of their involvement in various special credit programmes, (i.e. SLS and SCP) do not also appear to be noteworthy. So far as the SLS is concerned, the actual disbursement of the loan funds made available by the Bangladesh bank for distribution among SSCIs, was found to have fallen substantially below the planned target. While lack of creditworthiness of the borrowers and shortage of trained staff to handle small loans made the banks reluctant to implement the scheme, complicated disbursement procedures appeared to have prohibited many of the eligible SSCIs from approaching them for loans.

However, compared to the SLS, the operation of the SCP by the NCBs appeared to have achieved relatively better results. Till June 1981, a total amount of Tk. 10.28 crore as found to have been sanctioned as small loans under the SCP, of which Tk. 8.41 crore (81 per cent) has been disbursed. However, while the overall sanction and disbursement of loans under the SCP appears satisfactory, there exists an enormous

gap between the amount demanded by the borrowers and that actually made available to them.

While there exists both inter-bank and inter-regional differences in the sanction and disbursement of loans under the SCP, the overall recovery position of loans advanced under the Programme is found highly unsatisfactory. Only about 30 per cent of the loans due for repayment is found to have been recovered. Lack of knowledge and experience in dealing with industrial credits, lack of trained staff to make proper appraisal of the loan cases and that of extension officers to carryout close supervision of end-use of the loans by the concerned banks appear to be the important reasons for high rate of overdues. These problems are found to have been aggravated by the absence of a clearcut demarcation of responsibilities between the BSCIC and the financing Banks with respect to recovery of the loans sanctioned and the SCP.

Finally, like in the case of other programmes of institutional financing for the SSCIs, the SCP also failed to make adequate credit provision for the cottage enterprises. A number of factors appeared to have been responsible for this.

First, processing of the loan applications under the SCP also has, as usual, been too complicated. The three - tier processing mechanism (i.e. BSCIC and Bank Representative → District Committee → Financing Bank) adopted by the Programme seems to have made the decision - making process unnecessarily lengthy. Additionally, the clash of interests between the

representatives of the concerned agencies involved in the processing mechanism made it even more complicated with the consequence that some of the loans sanctioned could not be disbursed until after long delay.

Second, the documentation requirements set by most of the financing banks in support of the loan application were, in general, too cumbersome taxing too heavily on the time and ability of the small borrowers to procure and submit them all. Not surprisingly, this appeared to have acted as a relatively more serious deterrant to receiving formal credits by the cottage than by the small enterprises leading thereby to the differential access of the two groups to the credit facilities offered under the SCP.

Third, the adoption of a high minimum loan floor by most of the financial banks appeared to have caused another indirect bias against the smaller enterprises in the disbursement of funds under the SCP. Though unitended, the bias has been further strengthened through discontinuation of the practice of giving working capital loans under the SCP to all existing SSCIs except the Handicrafts.

Finally, the banks might have been partly correct in blaming at least some of the small entrepreneurs for not receiving institutional loans because of their reluctance to borrow from the formal credit market and their failure to submit viable proposals. It might also be true that incidence of borrowing for ill-conceived projects, ignorance about the

banking principles and use of the borrowed funds for unproductive purposes by some of the small borrowers render the lending institutions practicing utmost caution in extending credits to the SSCIs.

In the ultimate analysis, however, the fault seems to lie more with the banks. While the banks appear, in general, to be alergic to extend credit facilities to the small borrowers because of high risks and low profits involved in small lending, none of the NCBs nor any other lending agencies were found to have specific credit policies for the SSCIs. Moreover, in giving reasons for bad recovery position of the loans under the SCP, most banks also mentioned that lack of trained manpower acted as an important barrier to efficient handling and administration of the small loans programmes. The problem was reported to have been further aggravated by the lack of autonomy of the financing banks in decision - making. Most banks dealing with the small loan programmes felt that they needed more freedom and independence than granted to them at present for ensuring effective operation of such programmes.

5.2 Conclusions and Policy Recommendations

Both the specialized financial institutions and the NCBs lack in the kind of organizational set-up, expertise and orientation that are required for financing the SSCIs. Their services are geared more towards the larger and secure undertakings. Besides the absence of a comprehensive credit policy for small scale and cottage industries, lack of a

clear-cut development strategy for the small-scale sector at the national level creates further operational constraints for various agencies concerned with SSCIs promotion in determining the promotional needs of such industries and in providing them with promotional services.

Though BSCIC holds the key responsibility to promote the SSCIs in the country through providing these industries with an wide array of promotional incentives including finance, the Corporation does not seem to have the appropriate structural orientation and adequate extertise for the purpose. While frequent changes in the organizational set-up, lack of operational autonomy, and shortage of qualified staff appeared to have adversely affected its overall efficiency, the financial operations of the Corporation appear to be handicapped by the fact that its basic functional orientation is not towards financing activities. It might thus be desirable for BSCIC to concentrate more on promotion and extension work leaving the banking operations to be effectively handled by other appropriate agencies.

Thus, the institutional arrangements now existing in Bangladesh appear inadequate as well as inappropriate for meeting the credit needs of the SSCIs, particularly in the rural areas of the country. While this, along with the ambivalence of the government towards promoting the SSCIs sector explains the absence of a comprehensive credit policy for such industries in the country, the adhoc credit provisions made

for them also fail to create any appreciable impact because of lack of motivation and inefficient administration of the programmes by the concerned agencies.

Thus, if the decision is to intensify institutional credit facilities to the SSCIs for enhancing their growth and expansion through formulating and implementing comprehensive credit policies under the existing institutional arrangements, then an important step in this direction would be to simplify the lending procedures of the relevant agencies as well as to relax the existing rules and regulations so that the typical small borrowers, deficient in collateral and unable to fulfill the intricate official formalities, find it lot easier than now to enter the formal credit market.

Along with greater flexibility in the mode of operation of the existing financial institutions as to their present lending policies, necessary steps need also to be taken to decentralize their operations more effectively with a view to covering more wider geographical areas in order to bring the large majority of the SSCIs under the cover of the financial assistance programmes. This seems particularly important for the commercial banks as the financial operations of their rural branches were found to be seriously handicapped by the lack of sufficient autonomy in decision-making.

The extent of loan safety now provided by the Bangladesh Bank to the commercial banks through its "Credit Guarantee Scheme" need to be enhanced from the present 30 and 50 per cent to cover at least 80 per cent of the genuine losses incurred through bad debts. This may prove an important step towards increasing the rate of participation of the commercial banks in rural industries financing.

While the bank officials involved in operating the SSCIs Loan Programmes should be given short-term in-service training on the operation of various credit programmes right from the receipt of loan applications, upto appraisal, disbursement and recovery of loans, the concerned banks should also have separate cells, staffed by adequate number of officers and extension workers, whose sole function will be to look after the administration and operation of the SSCIs Credit Programmes This will ensure efficient operation of the SSCIs Credit Programmes by those who are experienced in the job and can appreciate the special needs and problems of the SSCIs.

Since a wide range of institutional arrangements (and combinations thereof) may be suitable under varying circumstances for channeling credit to the SSCIs, depending on the particular pattern of socio-economic, cultural and geographical factors associated with a given country, other feasible alternatives to the institutional arrangements for the purpose may also be considered.

One of such alternative arrangements may be to establish a separate financial institution for providing credit facilities to the SSCIs in Bangladesh. The sole (or at least primary) function of this institution will be to meet financial requirements of the SSCIs. Such an institution as in operation in Japan, Korea and Israel, would have the advantage of a staff specially trained in and oriented towards the credit needs and problems of the SSCIs. There may not also be the risk of the SSCIs being overlooked or given lower priority than their large counterparts -- a risk in which the present non-specialized institutions are rather deeply involved. Given the couspicuous absence of any credit provision whatsoever for the cottage industries in Bangladesh, the vaibility of establishing a separate financial institution particularly for meeting the credit prequirements of such industries may deserve serious considerations.

Finally, whatever the particular institutional framework any effective programme for financing the SSCIs should incorporate the following essential elements: (a) provision for all types of loans ensuring adequate flow of short, medium and long-term funds for meeting fixed and working capital requirements; (b) a branch network having adeuate autonomy in independent and quick decision-making, to reach the SSCIs spread out over widely disperesed areas; and (c) provision for providing the SSCIs with basic support services and extension facilities. Such services and facilities may include ,

among others, training the entrepreneurs in such areas as proper maintenance of the books and accounts, conception of bankable propositions, correct estimation of credit requirements and so on, which will help quick and accurate appraisal of loan applications, better utilization of loans and better collection of the dues.

In the interest of better recovery of loans, particular attention is also needed to assist the small borrowers not only in procuring raw-materials and machinery but also in improving their technological standard, product quality and design through providing them with necessary pre and post-investment counselling and support services. While all such promotional assistance and support services are expected to enable the SSCIs to make better utilization of loans and generate enough income to repay the loans in time, arrangements should be made to supply the SSCIs with all facilities from the same place, such as the DICs of BSCIC.

Last but not of least significance is the fact that as the flow of institutional credit to the rural areas of the country is highly restricted and is also likely to continue to be so in the near future, financing by the financial intermediaries though usurious, may not perhaps be avoided altogether at the present state of affairs for many reasons. All categories of the non-institutional lenders have not been found to be equally exploitative. Additionally, they appear to be more prompt and less formal compared to the institutional

lending agencies. More important, they sometimes provide funds assuming much greater risks (i.e. without any collateral) which is extremely important for purposes of increasing the supply of loanable funds to the small borrowers.

It would thus appear imperative that appropriate steps be taken to improve the mode of operation of the financial intermediaries so that they are turned into a more constructive element of development financing. And an effective approach in this regard might be to increase competition through increasing the flow of institutional finance to the rural industries sector. This will help reducing both interest rates and other costs associated with non-institutional lending.

APPENDIX TABLE A.1

DISTRIBUTION OF ENTERPRISES FACING VARIOUS PROBLEMS BY LOCATION AT START

Problems at start	Location			
	Village	Market place	Town	Row total
Finance	597 (70.2)	97 (68.8)	152 (61.8)	846 (68.3)
Fixed assets	43 (5.0)	13 (9.2)	49 (19.9)	105 (8.5)
Sub-total of finance & fixed assets	640 (75.2)	110 (78.0)	201 (81.7)	951 (76.8)
Raw materials	106 (12.4)	13 (9.2)	17 (6.9)	136 (10.9)
Skilled worker	43 (5.1)	1 (0.7)	13 (5.3)	57 (4.6)
Fuel	4 (0.5)	2 (1.4)	-	6 (0.5)
Marketing	30 (3.5)	2 (1.4)	2 (0.8)	34 (2.8)
Transportation	1 (0.1)	-	-	1 (0.1)
High tax rate	7 (0.8)	6 (4.4)	-	13 (1.1)
Competitive import	1 (0.1)	-	-	1 (0.1)
Lack of demand	5 (0.6)	2 (1.4)	-	7 (0.6)
Technical knowledge	5 (0.6)	1 (0.7)	5 (2.0)	11 (0.9)
Others	9 (1.1)	4 (2.8)	8 (3.3)	21 (1.6)
Column total	851 (100.0)	141 (100.0)	246 (100.0)	1238 (100.0)

Note : Figures in parentheses are row percentages.
' - ' Indicates nil

APPENDIX TABLE A.2

DISTRIBUTION OF THE ENTREPRENEURS GIVING VARIOUS REASONS FOR NOT TAKING INSTITUTIONAL LOANS BY SOCIAL ROLE OF THE ENTREPRENEURS IN THE COMMUNITY

Nature of reasons	Role in the society					
	No role	Minor role	Matab-bar	Member UC	Chair-man UC	Total
Ignorance	461 (39.7)	4 (14.8)	11 (36.2)	1 (10.0)	-	477 (38.4)
How to apply	70 (6.0)	-	6 (14.3)	1 (10.0)	-	77 (6.2)
Lack of security	190 (16.4)	2 (7.4)	3 (7.1)	-	-	195 (15.7)
High interest rate	38 (3.3)	4 (14.8)	-	3 (30.0)	-	45 (3.6)
Takes long time	55 (4.7)	4 (14.8)	4 (9.5)	-	1 (50.0)	64 (5.2)
Unofficial payment	33 (2.8)	1 (3.7)	1 (2.4)	-	1 (50.0)	36 (2.9)
Too troublesome	126 (10.9)	(22.2)	7 (16.7)	-	-	139 (11.2)
Had no need	100 (8.6)	3 (11.1)	7 (16.7)	2 (20.0)	-	112 (9.0)
Others	31 (2.7)	-	-	1 (10.0)	-	32 (2.6)
Non-response	56 (4.8)	3 (11.1)	3 (7.1)	2 (20.0)	-	64 (5.2)
Column total	1160 (100.0)	27 (100.0)	42 (100.0)	10 (100.0)	2 (100.0)	1241 (100.0)

Note: Figures in bracket are row percentages.

'- ' Indicates nil

APPENDIX TABLE A.3

DISTRIBUTION OF THE ENTREPRENEURS GIVING VARIOUS REASONS FOR NOT TAKING INSTITUTIONAL LOANS BY THEIR LANDOWNERSHIP PATTERN

Nature of reasons	Recorded land owned					
	Land-less	Upto 1 acre	1 - 5 acre	5 - 10 acre	Above 10 acre	Row total
Non-resonse	14 (4.5)	29 (4.7)	15 (6.5)	3 (8.8)	2 (10.0)	63 (5.2)
Ignorance	110 (35.1)	253 (41.4)	88 (38.3)	6 (17.6)	5 (25.0)	462 (38.2)
How to apply	28 (8.9)	33 (5.4)	13 (5.7)	2 (5.9)	1 (5.0)	77 (8.4)
Lack of security	57 (18.2)	119 (19.5)	11 (4.8)	2 (5.9)	-	189 (15.6)
High interest rate	11 (3.5)	22 (3.6)	9 (3.9)	-	2 (10.0)	44 (3.6)
Takes long time	14 (4.5)	26 (4.3)	17 (7.4)	4 (11.8)	3 (15.0)	64 (5.3)
Unofficial payment	5 (1.6)	19 (3.1)	7 (3.0)	3 (8.8)	-	34 (2.8)
Too trouble some	31 (9.9)	55 (9.0)	36 (15.7)	9 (26.5)	1 (5.0)	132 (10.9)
Had no need	35 (11.2)	40 (6.5)	27 (11.7)	3 (8.8)	6 (30.0)	111 (9.2)
Others	8 (2.6)	15 (2.5)	7 (3.0)	2 (5.9)	-	32 (2.6)
Column total	313 (100.0)	611 (100.0)	230 (100.0)	34 (100.0)	20 (100.0)	1208 (100.0)

Note : Bottom figures in each cell are row percentage.
' - ' Indicates nil.

APPENDIX TABLE A.4

DISTRIBUTION OF THE ENTREPRENEURS GIVING VARIOUS REASONS FOR NOT TAKING INSTITUTIONAL LOANS BY LEVELS OF THEIR PER CAPITA INCOME

Reasons	Per capita income						
	Under 250	250 to 500	500 to 1000	1000 to 1500	1500 to 2500	2500 to 5000	Row total
Non-response	-	-	-	-	6 (2.3)	55 (6.3)	61 (5.0)
Ignorance	2 (66.7)	3 (25.0)	6 (66.7)	25 (46.3)	127 (48.7)	302 (34.6)	465 (38.4)
How to apply	-	-	-	5 (9.3)	9 (3.4)	58 (6.7)	72 (5.9)
Lack of security	1 (33.3)	2 (16.7)	2 (22.2)	14 (25.9)	71 (27.2)	105 (12.0)	195 (16.1)
High interest rate	-	-	-	-	2 (0.8)	42 (4.8)	44 (3.6)
Takes long time	-	1 (8.3)	-	-	4 (1.5)	58 (6.7)	63 (5.2)
Unofficial payment	-	-	-	-	1 (0.4)	35 (4.0)	36 (3.0)
Too troublesome	-	-	1 (11.1)	8 (14.8)	23 (8.8)	102 (11.7)	134 (11.1)
Had no need	-	5 (41.7)	-	2 (3.7)	13 (5.0)	89 (10.2)	109 (9.0)
Others	-	1 (8.3)	-	-	5 (1.9)	26 (3.0)	32 (2.7)
Column total	3 (100.)	12 (100.0)	9 (100.0)	54 (100.0)	261 (100.0)	872 (100.0).	1211 (100.0)

Note : Bottom figures are row percentage

' - ' Indicates nil

APPENDIX TABLE A.5

DISTRIBUTION OF THE ENTREPRENEURS GIVING VARIOUS REASONS FOR NOT TAKING INSTITUTIONAL LOANS BY THEIR LEVEL OF EDUCATION.

Level of education	Reasons				
	No-response	Ignorance	How to apply	Lack of security	High interest rate
No formal education	11 (2.2)	248 (49.6)	38 (7.6)	81 (16.2)	5 (1.0)
Passed grade 1-4	25 (5.9)	159 (37.5)	24 (5.7)	80 (18.9)	18 (4.2)
5 - 9	17 (7.6)	56 (25.0)	11 (4.9)	26 (11.6)	15 (6.7)
10 - 11	3 (7.5)	8 (20.0)	1 (2.5)	3 (7.5)	15 (7.5)
12 - 13	3 (12.0)	4 (16.0)	2 (8.0)	2 (8.0)	1 (4.0)
UD and over	5 (19.2)	2 (7.7)	1 (3.8)	3 (11.5)	3 (7.7)
Vocational training	-	-	-	-	-
Column total	64 (5.2)	477 (38.5)	77 (6.2)	195 (15.7)	45 (3.6)

Note : Bottom figures are row percentage.

' - ' Indicates nil

APPENDIX TABLE A.5 (CONTD.)

Level of education	Reasons					
	Takes long time	Unofficial payment	Too rouble some	Had no need	Others	Row total
No formal education	16 (3.2)	6 (1.2)	51 (10.2)	33 (6.6)	11 (2.2)	500 (100.0)
Passed grade 1-4	13 (3.1)	12 (2.8)	45 (10.6)	37 (8.7)	11 (2.6)	424 (100.0)
5 - 9	25 (11.2)	12 (5.4)	30 (13.4)	24 (10.7)	8 (3.6)	224 (100.0)
10 - 11	5 (12.5)	1 (2.5)	6 (15.0)	9 (22.9)	1 (2.5)	40 (100.0)
12 - 13	2 (8.0)	3 (12.0)	2 (8.0)	5 (20.0)	1 (4.0)	25 (100.0)
UD and over	2 (7.7)	1 (3.8)	5 (19.2)	4 (15.4)	-	26 (100.0)
Vocational training	1 (100.0)	-	-	-	-	1 (100.0)
Column total	64 (5.2)	35 (2.8)	139 (11.2)	112 (9.0)	32 (2.6)	1240 (100.0)

APPENDIX TABLE A.6

DISTRIBUTION OF THE ENTERPRISES GIVING VARIOUS REASONS FOR NOT TAKING INSTITUTIONAL LOANS BY AGE OF THE ENTERPRISES

Reasons	Record age of enterprise						
	Under 5	5 - 9	10-14	15-19	20-32	33 and over	Row total
Non-response	14 (6.5)	10 (4.6)	10 (6.1)	9 (7.3)	9 (3.9)	12 (4.2)	64 (5.2)
Ignorance	59 (27.3)	76 (34.9)	71 (43.3)	50 (40.3)	96 (41.4)	125 (43.6)	477 (38.4)
How to apply	17 (7.9)	16 (7.3)	5 (3.0)	11 (8.9)	12 (5.2)	16 (5.6)	77 (6.2)
Lack of security	34 (15.7)	36 (16.5)	16 (9.8)	23 (18.5)	47 (20.3)	39 (13.6)	195 (15.7)
High interest rate	12 (5.6)	9 (4.1)	9 (5.5)	5 (4.0)	3 (1.3)	7 (2.4)	45 (3.6)
Takes long time	17 (7.9)	8 (3.7)	14 (8.5)	6 (4.8)	5 (2.2)	14 (4.9)	64 (5.2)
Unofficial payment	13 (6.0)	5 (2.3)	5 (3.0)	3 (2.4)	7 (3.0)	3 (1.0)	36 (2.9)
Too troublesome	17 (7.9)	27 (12.4)	17 (10.4)	8 (6.5)	28 (12.1)	42 (14.6)	139 (11.2)
Had no need	28 (13.0)	20 (9.2)	14 (8.5)	6 (4.8)	19 (8.2)	25 (8.7)	112 (9.1)
Others	5 (2.3)	11 (5.0)	3 (1.8)	3 (2.4)	6 (2.6)	4 (1.4)	32 (2.5)
Column total	216 (100.0)	218 (100.0)	164 (100.0)	124 (100.0)	232 (100.0)	287 (100.0)	1241 (100.0)

Note: Bottom figures are row percentage.

' - ' Indicates nil.

APPENDIX TABLE A.7

DISTRIBUTION OF THE ENTREPRENEURS MENTIONING VARIOUS PROBLEMS FACED IN TAKING INSTITUTIONAL LOANS BY THEIR SOCIAL ROLE IN THE COMMUNITY

Problems	Role in the society				
	No role	Minor role	Matabbar	Chairman U.C.	Row total
Lack of security	33 (34.7)	2 (40.0)	-	-	35 (33.7)
High interest rate	1 (1.1)	-	-	-	1 (1.0)
Takes long time	11 (11.6)	2 (40.0)	1 (33.3)	-	14 (13.5)
Unofficial payment	14 (14.7)	1 (20.0)	-	-	15 (14.4)
Official formalities	18 (18.9)	-	-	1 (100.0)	19 (18.3)
Others	4 (4.2)	-	-	-	4 (3.8)
Ignorance	14 (14.7)	-	2 (66.7)	-	16 (15.4)
Column total	95 (100.0)	5 (100.0)	3 (100.0)	1 (100.0)	104 (100.0)

Note: Bottom figures are row percentages.

' - ' Indicates nil.

APPENDIX TABLE A.8

DISTRIBUTION OF THE ENTERPRENEURS MENTIONING VARIOUS PROBLEMS FACED BY THEM IN TAKING INSTITUTIONAL LOANS BY THEIR LANDOWNERSHIP PATTERN.

Problems	Recorded land owned					
	Land	Upto 1	1- 5	5 - 10	Above 10 acre	Row total
Lack of security	6 (37.5)	19 (34.5)	8 (33.3)	1 (25.0)	1 (33.3)	35 (34.3)
High interest rate	-	1 (1.8)	-	-	-	1 (1.0)
Takes long time	3 (18.8)	7 (12.7)	2 (8.3)	-	2 (66.7)	14 (13.7)
Unofficial payment	2 (12.5)	7 (12.7)	4 (16.7)	1 (25.0)	-	14 (13.7)
Others	-	4 (7.3)	-	-	-	4 (3.9)
Ignorance	3 (18.8)	8 (14.5)	5 (20.8)	-	-	16 (15.7)
Column total	16 (100.0)	55 (100.0)	24 (100.0)	4 (100.0)	3 (100.0)	102 (100.0)

Note : Bottom figures are row percentage

' - ' Indicates nil

APPENDIX TABLE A.9

DISTRIBUTION OF ENTERPRISES MENTIONING VARIOUS PROBLEMS IN TAKING INSTITUTIONAL LOANS BY LOCATION

Problems	Location			
	Village	Market place	Town	Total
Ignorance	16 (15.8)	-	-	16 (11.1)
Lack of security	27 (26.7)	-	8 (24.3)	35 (24.3)
High interest rate	2 (2.0)	1 (10.0)	-	3 (2.1)
Takes long time	10 (9.9)	3 (30.0)	7 (21.2)	20 (13.9)
Unofficial payment	17 (16.8)	1 (10.0)	11 (33.3)	29 (20.1)
Official formalities	26 (25.8)	4 (40.0)	5 (15.1)	35 (24.3)
Others	3 (3.0)	1 (10.0)	2 (6.1)	6 (4.2)
Column total	101 (100.0)	10 (100.0)	33 (100.0)	144 (100.0)

Note: Bottom figures are row percentage

' - ' Indicates nil

APPENDIX TABLE A.10

DISTRIBUTION OF THE ENTREPRENEURS MENTIONING VARIOUS PROBLEMS FACED BY THEM IN TAKING INSTITUTIONAL LOAN BY THEIR LEVEL OF EDUCATION.

Level of education	Problems							
	Lack of security	High interest rate	Takes long time	Unofficial payment	Official formalities	Others	Ignorance	Total
No formal education	14 (46.7)	-	1 (3.3)	2 (6.7)	4 (13.3)	2 (6.7)	7 (23.3)	30 (100.0)
Passed grade 1 - 4	11 (30.6)	-	6 (16.7)	5 (13.9)	6 (16.7)	2 (5.6)	6 (16.7)	36 (100.0)
5 - 9	7 (26.9)	-	5 (19.2)	4 (15.4)	7 (26.9)	-	3 (11.5)	26 (100.0)
10 - 11	-	-	-	1 (50.0)	1 (50.0)	-	-	2 (100.0)
12.- 13	2 (33.3)	1 (16.7)	1 (16.7)	2 (33.3)	-	-	-	6 (100.0)
UD and over	1 (25.0)	-	1 (25.0)	1 (25.0)	1 (25.0)	-	-	4 (100.0)
Column total	35 (33.7)	1 (1.0)	14 (13.5)	15 (14.4)	19 (18.3)	4 (3.8)	16 (15.4)	104 (100.0)

Note : Bottom figures are row percentage

'- ' Indicates nil

APPENDIX TABLE A.11

DISTRIBUTION OF ENTERPRISES FACING VARIOUS PROBLEMS IN TAKING INSTITUTIONAL LOANS BY AGE OF THE ENTERPRISE

Recorded age of enterprise	Problems							
	Lack of security	High interest rate	Takes long time	Unofficial payment	Official formalities	Others	Ignorance	Total
Under 5	7 (35.0)	-	1 (5.0)	5 (25.0)	5 (25.0)	-	2 (10.0)	20 (100.0)
5 - 9	5 (27.8)	-	3 (16.7)	2 (11.1)	3 (16.7)	1 (5.6)	4 (22.2)	18 (100.0)
10 - 14	4 (26.7)	-	2 (13.3)	5 (33.3)	2 (13.3)	-	2 (13.3)	15 (100.0)
15 - 19	5 (50.0)	-	3 (30.0)	-	2 (20.0)	-	-	10 (100.0)
20 - 32	8 (44.4)	1 (5.6)	2 (11.1)	2 (11.1)	1 (5.6)	3 (16.7)	1 (5.6)	18 (100.0)
33 and over	6 (26.1)	-	3 (13.0)	1 (4.3)	6 (26.1)	-	7 (30.4)	23 (100.0)
Column total	35 (33.7)	1 (1.0)	14 (13.5)	15 (15.4)	19 (18.3)	4 (3.8)	16 (15.4)	104 (100.0)

Note: Bottom figures are row percentage

' - ' Indicates nil.

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