

# **MAPPING POLICY LANDSCAPE FOR SME DEVELOPMENT FOR POLICY HARMONIZATION ACROSS GOVERNMENT ORGANIZATIONS**

A study conducted as a part of Daayitwa Nepal Public Policy Fellowship 2022, in collaboration with Ministry of Industry, Commerce and Supplies (MoICS)

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## ABBREVIATIONS

ADB	Asian Development Bank	NGO	Non-Governmental Organization
CBS	Central Bureau of Statistics	NPC	National Planning Commission
EEC	European Economic Chamber	NPR	Nepali Rupee
GDP	Gross Domestic Product	OECD	Organization for Economic Cooperation and Development
GVC	Global Value Chain	PPCP	Public-Private Cooperative Partnership
ICT	Information, Communication, and Technology	SME	Small and Medium Enterprise
ILO	International Labour Organization	UNCDF	United Nations Capital Development Fund
IMF	International Monetary Fund	UNCTAD	United Nations Conference on Trade and Development
MCSE	Micro, Cottage, and Small Enterprise	UNDP	United Nations Development Program
MEDEP	Micro Enterprise Development Program	UNECE	United Nations Economic Commission for Europe
MEDPA	Micro Enterprise Development Program for Poverty Alleviation	UNESCAP	United Nations Economic Commission for Asia-Pacific
MFI	Micro Financial Institutions	USD	United States Dollar
MOICS	Ministry of Industry, Commerce, and Supplies		
MSME	Micro, Small, and Medium Enterprise		

## ABSTRACT

This paper aims to discuss the potential challenges faced by SMEs in Nepal along with the gap existing between several governmental agencies. Despite several provisions made to boost the development of small and medium enterprises in Nepal, there has not been significant progress as it seems. The ground reality of the SMEs and those reflected in paper documents have huge differences. There is a massive gap between inter-governmental coherence to support the growth of SMEs. This paper highlights different SME-related provisions of governmental organizations and measures their effectiveness on the ground through field research. The gaps and challenges identified from the field have been considered as key references to design policy recommendations. The paper concludes with the policy recommendations for the federal government that was gathered through periodic consultations and discussions with the relevant stakeholders. The key stakeholders that were consulted throughout this research are SMEs, government organizations, MFIs, and the private sector.

**Key Words:** *SME, Ministry of Industry, Local Level, Entrepreneurship, Finance*

## 1. BACKGROUND

Small and Medium-sized enterprises (SMEs) are considered businesses that maintain revenues, assets, or a number of employees below a certain threshold while each country has its own definition of what constitutes a small and medium-sized enterprise (Liberto, 2022). The Organization for Economic Cooperation and Development (OECD) has defined Small and medium-sized enterprises (SMEs) as non-subsiary, independent firms which employ fewer than a given number of employees. The number differs according to the countries and their standards. The most frequent upper limit designating an SME is 250 employees, as in the European Union. However, some countries set the limit at 200 employees, while the United States considers SMEs to include firms with fewer than 500 employees (OECD, 2005, p. 17). IMF has further categorized enterprise type on the basis of the number of employees stating micro-enterprise with 1-9 employees, small with 10-49 employees, and medium with 50-249 employees (UNECE, 2018).

On the other hand, ILO indicates that in many countries; especially lower-income countries, more than 90% of all enterprises can be classed as SMEs, and a large share of those can be classed as micro firms, with fewer than ten employees (ILO, 2019)

Often referred to as MSME (Micro, small and medium enterprises), there are criteria like - assets, employment, and annual turnover which define its standard. But different countries have made different legal standards for the companies to claim themselves as MSME (UNCDF, 2020). In the case of Nepal, The Industrial Enterprises Act of 2020 defines micro-enterprises using four criteria (capital investment, employment, annual turnover, and energy consumption) while it uses the single criterion of capital investment to define SMEs (Department of Industry, Commerce, and Supplies, 2020).

The definitions of micro, cottage, small, medium, and large enterprises according to the Industrial Enterprises Act of 2020 are as follows:<sup>1</sup>

- i) Micro industries are enterprises that meet the following conditions: a) have a fixed capital not exceeding NPR 2 million (USD 18,000) apart from land and buildings, b)

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<sup>1</sup> Industrial Enterprise Act of Nepal - 2020:  
<https://moics.gov.np/uploads/shares/laws/Industrial%20Enterprises%20Act%20%202020.pdf>

- are run by the proprietor himself, c) work at the local level and utilize local raw materials, d) has an annual turnover of up to NPR 10 million (USD 89,000), e) employs not more than nine workers, and f) consume less than 20 kilowatts of electrical power when they run in full capacity.
- ii) Cottage industries are enterprises that use local workers and raw materials, are engaged in traditional labor-intensive industries that reflect the country's indigenous art and culture, and consume less than 50 kilowatts of electrical power when they run at full capacity.
  - iii) Small-scale industries (SSI) are enterprises other than micro and cottage industries with fixed capital not exceeding NPR 150 million (USD 1.3 million).
  - iv) Medium industries are enterprises with fixed capital between NPR 150 million and NPR 500 million (USD 4.4 million).
  - v) Large industries are enterprises that have over NPR 500 million in fixed capital

While the category of cottage industries is included under the category of SMEs, it is very essential to study the correlation between the growth of such cottage-related SMEs and the policy relevance in Nepal.

Small and Medium Enterprises (SMEs) play a significant role particularly in developing countries as they represent 90% of businesses and more than 50% of employment worldwide contributing to massive economic growth and support. While in the case of Nepal, Micro Cottage and Small Enterprises (MCSEs) contribute around 1.7 million employment generation (Rai, 2020). This shows that there is a massive influence of cottage industries in the Nepalese Economy.

The recent status of Fiscal Year (F.Y.) 2078/79 of the Department of Industry in Nepal shows that out of 309 industries registered in the F.Y., 110 belong to small enterprises that consist of cottage and micro industries. According to the Central Bureau of Statistics (2017), 908,000 of the total working-age population are unemployed. Micro, cottage, and small enterprises can be pivotal in making the labor force self-sustained and stimulating production that benefits the local and national economy.

Micro and small enterprises have played a major role in stimulating industrial growth in many developing countries, particularly in Asia as well (UNCTAD, 2001). Nepal has not been an exception in this case. The country has been acknowledged from very ancient times in terms of its

traditional arts, culture, and craftsmanship. From the fifth-century Chinese travelers Wanghunshe and Huansang to the present times of economic trade, Nepalese crafts and products are highly appreciated and recognized globally (Ghimire, 2011). The history of industrialization in Nepal dates back to 1936 during the time of then Prime Minister Juddha Sumsher Rana. This year Jute Mill established a joint venture with Indian industrialists in Biratnagar. In 1940 Thirty-Five new joint companies were established till 1951 but after that, for one decade no companies were established due to social and political unrest. In the Rana regime (1836 to 1951) Cottage Skill Awareness Office (Gharelu Ilam Prachar Adda) was established in 1940 (Ghimire, p. 3, 2011).

Furthermore, between 1970 to 1990, various cottage industry development programs were started to provide industrial and technical service programs, handicraft design programs, village industries programs, sales management programs, and training programs. Similarly, the Department of Cottage and Small Industries (DCSI) was established to promote various cottage and small industries (Ghimire, 2011).

Coming till date, the government has initiated multiple projects and programs to support the growth of SMEs in Nepal and create a suitable environment for their development. With the aim of catering to the needs of marginalized people living below the nationally defined poverty line by promoting off-farm employment, the government of Nepal along with the United Nations Development Programme started Micro Enterprise Development Program (MEDEP), now known as MEDPA, in 1998 (UNESCAP, 2018)<sup>2</sup>.

The program has specifically targeted the people below the nationally defined poverty line, with a special focus on women and socially excluded groups, such as Dalits, Indigenous Nationalities, Religious Minorities, Unemployed Youth, Ultra Poor, and Excluded Madheshis. MEDEP started as a pilot program in June 1998 in ten different districts. Until now, the program has covered all 75 districts of Nepal. Through MEDEP, a total number of 137,404 micro-entrepreneurs were created as of March 2018 (UNDP, 2018).

### **Table 1: Share of Industries type registered as of 2021**

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<sup>2</sup> MEDPA is a joint initiative between the Ministry of Industry, Commerce, and Supplies (MOICS) and UNDP started in 1998. Now the program is officially led by MOICS: <https://medpa.moics.gov.np/>

Scale	No. of Industries	Total Investment	Fixed Capital	Working Capital	Proposed Employment (Person)	Employment per Industry
Large Industry	1198	193857.6	181850.2	12007.4	165196	138
Medium Industry	1884	20425.7	14542.7	5883.1	169640	90
Small Industry	5302	10239.7	6580.9	3658.8	289825	55
<b>Total</b>	<b>8384</b>	<b>224523.0</b>	<b>202973.7</b>	<b>21549.3</b>	<b>624661</b>	<b>75</b>

*Source: Department of Industry, 2021*

Likewise, Nepal Economic Survey 2020/21<sup>3</sup> shows that during the mid-March of the fiscal year 2020/21, in terms of the number of industries, the share of large, medium, and small-scale industries was 14.0 percent, 22.5 percent, and 63.5 percent, respectively. Small Industries constitute a large number of industrial registrations until mid-march 2021.

**Table 2: Breakdown of provincial-level MSME industrial registration**

Province	Number of Registered Micro, Cottage and Small Industries	Proposed Employment
Province 1	63290	406989
Province 2	66654	296949
Bagmati	159568	1010980

<sup>3</sup> Nepal Economic Survey 2020/21 was conducted by Ministry of Finance:  
[https://www.mof.gov.np/uploads/document/file/1633341980\\_Economic%20Survey%20\(English\)%202020-21.pdf](https://www.mof.gov.np/uploads/document/file/1633341980_Economic%20Survey%20(English)%202020-21.pdf)

Gandaki	49189	283898
Lumbini	81164	493686
Karnali	23254	128658
Sudurpashchim	32558	187579
<b>Total</b>	<b>475677</b>	<b>2908739</b>

*Source - Department of Industry, 2021*

In 2021, a total number of 475,677 micro, cottage, and small industries were registered and created 2,908,739 employments across 7 different provinces of Nepal. The estimated per industry average employment is 6 persons.

Bagmati province has the highest 33.0 percent of registered micro, cottage, and small industries followed by Lumbini province, Province 2, and Province 1, 17.0 percent, 14.0 percent, and 13.0 percent, respectively. Karnali province has the lowest, only 5.0 percent of the registered industries.

Considering the huge potential of SMEs to boost significant effects on the Nepalese economy, there is a need to substantially promote the presence of SMEs for Prosperous and Sustainable Development in Nepal.

## 2. LITERATURE REVIEW

### 2.1. General Status and challenges of SMEs in Nepal

Despite the continuous effort of the Government to boost the presence of MSMEs in Nepal, the progress has not been substantial. A working paper produced by Asian Development Bank (ADB) in 2020 suggested that Nepal lacks a concrete policy framework for SMEs followed by a lack of space for the participation of SMEs in the Global Value Chain (GVC). While several acts and policies have been designed that address the issues of SMEs, the Government has not yet designed a single policy solely for SMEs Development in Nepal.

For example - Nepalese handicrafts and crafted products have an abundance of opportunities to glow in the global market and boost the national economy. The Federation of Handicraft Associations of Nepal (FHAN), which was established as an NGO in 1972 has been working rigorously to promote SMEs working in the handicraft-related sector to the global market. However, their major concern is not getting adequate support from the government to promote these crafts in the global market (Online Khabar, 2021).

**Table 3: Number of Industries registered by type in F.Y 2020/21**

Scale	No. of Industry	Total Investment	Fixed Capital	Working Capital	Proposed Employment (Person)	Employment per Industry
Large Industry	1198	193857.6	181850.2	12007.4	165196	138
Medium Industry	1884	20425.7	14542.7	5883.1	169640	90
Small Industry	5302	10239.7	6580.9	3658.8	289825	55
<b>Total</b>	<b>8384</b>	<b>224523.0</b>	<b>202973.7</b>	<b>21549.3</b>	<b>624661</b>	<b>283</b>

*Source: Department of Industry, 2021*

Nepal Economic Survey 2020/21 shows that there is more than a 60% share of SMEs in Nepal. Whereas, the government has also planned for policy, legal and structural reform and to make investments in industries having competitive potential and comparative advantage for the development of the industrial sector. In addition, Micro Cottage and Small Industries (MCSEs) contribute around 22% of the GDP including 82% of export earnings, and 1.7 million employment generation in Nepal (Rai, 2020). This shows that there is a massive influence of cottage industries in the Nepalese Economy. But despite all of the efforts demonstrated by SMEs, the share of investments in SMEs is still low in the country.

Since, the industrial data on the contribution of SMEs to output, employment, and exports only addresses the manufacturing sector. The role of SMEs in their actual contribution to the manufacturing sector is missing (Asian Development Bank, 2020). This can be due to the lack of structural reforms in governmental policy frameworks for SMEs.

Furthermore, UNESCAP in Nepal has mentioned some specific challenges that SMEs in Nepal are facing which include - limited market linkages and export procedures, limited capital and technologies, domestic and international regulation, quality and standard issues, and vulnerability due to limited product range. ADB's working paper on SMEs in Nepal supports the statement reporting that financing, production, market access, and international linkages are major constraints to the growth and development of SMEs in Nepal.

The larger part of this facilitation can be linked with various governmental organizations that are responsible for facilitating the access of SMEs to these resources.

**Table 4: Micro and Cottage Enterprises Registration in F.Y 2020/21**

Province	Total	Female	Male	Youth
Province 1	6675	5213	1445	3217
Province 2	6609	5982	627	4297
Bagmati	4455	3731	724	3334
Gandaki	3510	2816	694	2627
Lumbini	4530	3965	565	3107
Karnali	5491	4564	927	4140
Sudurpaschim	5226	4307	919	4357
<b>Total</b>	<b>36479</b>	<b>30578</b>	<b>5901</b>	<b>25079</b>

*Source - Department of Industry, 2021*

The above data extracted from the Ministry of Industry, Commerce, and Supplies shows a very impressive fact about the huge number of female participations in micro and cottage enterprises. The total number of female-led micro-enterprises was recorded at 30578 out of the total number of 36479 enterprises. This shows how MSMEs are directly or indirectly linked with female-led entrepreneurship and have grown over a period of time.

Since federalism was incepted in Nepal in 2017, there are a plethora of opportunities for SMEs to boost their presence locally as well as nationally. There is a need for coherence between all three tiers of government to create appropriate space for SMEs, especially women-led enterprises to grow significantly. Local Governance Operations Act 2017 provides each local government a right to promote and encourage local-level small-scale entrepreneurs. Federal policies on SMEs are

already the gap however local level government can identify and formulate local-level SME policy.

The Industrial Policy and the associated Industrial Enterprise Act (IEA) categorize enterprises into micro-, cottage, small, medium-sized, and large enterprises. However, the specific provisions related to SMEs are lacking. The lack of SME policies has been a structural challenge to the growth of SMEs in Nepal (Kharel and Dahal, 2020).

The post-covid growth of SMEs has been hit hard. Although, Nepalese SMEs have survived through decade-long civil war, political uncertainties, earthquakes, and blockades. They have found their ways to survive those challenging years. But the covid made it hard for SMEs to grow. SMEs need support from the government and other agencies at the same time, they need to come up with strategies to find new market opportunities within Nepal and abroad (Dangol, et al, 2020).

In other words, globalization and economic liberalization have caused more challenges for SMEs in Nepal resulting in competition with imported products, an investment gap, and other factors due to which Nepalese SMEs have to lose with the global and regional players (EEC, n.d). The report from European Economic Chambers also reflects that among the SMEs in Nepal, handicraft-related enterprises have been the major player to boost foreign exchange and exports in Nepal. However, greater emphasis on specific policy measures aimed at competitive enterprises like such is lacking. India has set up its own Ministry for SMEs which makes it easier for SMEs to operate and grow which is contrary to Nepal.

An analytical report by CBS in 2018 reports that the share of small and micro businesses in Nepal is bigger in the case of Women. Whereas the Federation of Small and Medium Enterprises Nepal says despite women owning 60 percent of Nepal's small and medium-sized enterprises, their limited access to finance and financial literacy has caused a massive barrier to the growth of SMEs (NRB, 2018).

## **2.2. Constitution of Nepal 2015**

The Constitution of Nepal 2015, Part 51 has indicated the strengthening of the national economy through the participation and free development of the public sector, cooperative sector, and private sector. Following the article, the constitution has also stressed on promotion of domestic industries,

utilization of locally available resources, and creation of an environment for export of the domestic goods and services that are produced locally.<sup>4</sup>

### **2.3. Review of the 15th Periodic Plan and its provision for SMEs**

After the 5-year cycle of the 14th periodic plan ended in 2019, the National Planning Commission introduced the Fifteenth plan (2019/20 - 2023/24) with a Long-Term Vision of taking Nepal to the level of advanced countries by 2043 AD. The stability of the government structure in Nepal with the inception of federalism in Nepal was considered one of the significant achievements of the 14th plan of Nepal. (NPC, 2020).<sup>5</sup>

Furthermore, the 14th plan saw progress in terms of employment generation, women's participation, and cooperatives run by women, however, it has not been as significant as targeted.

Some long-term strategies for the ongoing 15th plan were designed during its formulation. Following are some key strategies that are in line with the development of SMEs in Nepal:

- a. Increase production and productivity
- b. Conservation and utilization of natural resources
- c. Creation of additional employment opportunities, promotion,
- d. Development of industries supported by local labor and skills.
- e. Increasing exports of micro-industrial sectors

The 15th plan of Nepal has identified the following challenges as a major gap in the development of SMEs and Entrepreneurship in Nepal:<sup>6</sup>

- a. Lack of entrepreneurial culture
- b. Inability to link training with industries

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<sup>4</sup> Constitution of Nepal 2015; [https://www.constituteproject.org/constitution/Nepal\\_2015.pdf](https://www.constituteproject.org/constitution/Nepal_2015.pdf)

<sup>5</sup> National 15th Periodic Plan of Nepal:  
[https://npc.gov.np/images/category/15th\\_plan\\_English\\_Version.pdf](https://npc.gov.np/images/category/15th_plan_English_Version.pdf)

<sup>6</sup> Points Extracted from Chapter 5 and Chapter 6 of 15th Periodic Plan of Nepal

- c. Inadequate access to finance
- d. Lack of mobilization and availability in productive sectors and industries
- e. Inability to link the issues of industry and investment with the one-window system;
- f. Lack of cost competition and quality in industrial products and lack of production and diversification of exportable goods
- g. The failure of the private sector to lead in connecting the capital, skills, raw materials, and technologies in the promotion of micro, cottage, and small industries;
- h. Inability to use new technologies and equipment in industrialization;
- i. Lack of research and development in industry and marketing, lack of adequately skilled technical human resources; and failure to bring together and coordinate industry
- j. Low utilization of domestically available resources

Despite the ongoing challenges faced by SMEs and local-level entrepreneurs in Nepal, some working policies and a strategic plan have been envisioned and designed by the National Planning Commission to help in the growth of SMEs and entrepreneurship in Nepal:

- a. Existing policies and laws are to be revised to support entrepreneurship development and the use of innovative technologies and traditional knowledge
- b. Business development centers are to be established to support potential entrepreneurs starting and developing their industries.
- c. Development of Social Entrepreneurship to be encouraged
- d. Micro, cottage, and small industries are to be promoted and developed based on locally available resources and skills, feasibility, and demand from the market
- e. Domestic production is to be encouraged by modernizing and upgrading traditional knowledge and skills
- f. Intergovernmental coordination is to be ensured for the establishment of industries and the marketing of industrial products

Furthermore, the 15th plan has highly stressed the import management system by mobilizing public-private-cooperative partnership (PPCP) in industries based on domestic raw materials and having a competitive capacity and comparative advantages.

The strategic plan for facilitating this process has been defined as:

- a. Collection and processing centers for Himalayan nettle, banana, cane, and bamboo are to be established and provided with technology supported for promoting entrepreneurship in products based on natural fiber.
- b. Priority is to be given to soft loans for micro, cottage, small and medium enterprises. Access to credit for other industries will also be prioritized.

#### **2.4. Industrial Policy 2011**

Nepal Industrial Policy 2011 was formulated with the objective of increasing the contribution of the industrial sector in balanced national and regional development by mobilizing local resources, raw materials, skills, and means with an emphasis on the environment-friendly production process and technology.<sup>7</sup> While this is very true that the majority of SMEs are indigenous-based and focus on the use of locally available resources that are natural and accessible. Some of the key SME-related highlights of Industrial Policy are as follows:

- a. Special emphasis to be given to promote the industries that use local resources, raw materials, skills, labor, and technology
- b. Technical and financial assistance to be made available to the industries that use environment-friendly and energy-saving technology at their own costs
- c. Micro, Cottage, and Small Industries Development Fund to be established in collaboration with private and cooperative sectors
- d. One Stop Centre to be implemented

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<sup>7</sup> Industrial Policy 2011: <https://www.climate-laws.org/geographies/nepal/policies/industrial-policy-2011>

- e. Most potential resources and means at the local level are to be identified according to the concept of one village one product and a Product Development Centre shall be established to promote the production of industrial goods
- f. Identification of the products of micro-enterprises, cottage, and small industries to be maintained through the use of collective marks and assistance shall be given for their promotion
- g. The market of the goods and services of micro-enterprises, cottage, and small industries to be promoted
- h. In order to use information technology for the promotion of micro-enterprises, cottage, and small industries, information technology hubs shall be brought into operation in collaboration with cooperative and private sector
- i. For promoting the sale of the products of micro-enterprises, cottage and small industries, governmental and nongovernmental agencies shall be encouraged to purchase such products

## **2.5. Monetary Policy 2022/23**

As per the Nepal Rastra Bank Act, 2002, the major objective of this bank is to formulate and then implement monetary and exchange rate policy to achieve price and balance payment stability for economic stability and sustainable economic development. Accordingly, the bank has been formulating and publicly announcing monetary policy since 2002/03. In addition, the bank has started a half-yearly review of the policy since 2003/04, and a quarterly review since 2016/17 to make necessary changes in policy measures after reviewing the economic and financial situation (NRB, p. 1, 2022)<sup>8</sup>

Understanding the need to increase access to finance for SMEs, the focus of existing monetary policy has been directed towards increasing access to credit for the small, cottage, micro, and medium enterprises and reducing the over-concentration of credit. Refinancing facilities are also promised to be continued for SMEs but priority is given to the productive sectors. NRB has also

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<sup>8</sup>NRB Monetary Policy Highlights:  
[https://pkf.trunco.com.np/uploads/publication/file/Monetary%20Policy%202022-23\\_20220726061811.pdf](https://pkf.trunco.com.np/uploads/publication/file/Monetary%20Policy%202022-23_20220726061811.pdf)

indicated the reduction of Refinance rate on small and medium enterprises (SMEs) against the collateral of 'Pass' loan up to Rs. 1 million to 3 percent from the existing 5 percent.

One of the very important aspects of SME financing and growth, Financial Literacy Framework 2022 will also be designed in coordination with the Ministry of Education, the Curriculum Development Centre, and the Government of Nepal (NRB, 2022). However, the Financial Access Report prepared by NRB in 2018 suggests that the Monitoring and Evaluation mechanism is missing to measure the success of the Financial Literacy Framework in Nepal. The Federation of Small and Medium Enterprises Nepal says women own 60 percent of Nepal's small and medium-sized enterprises, yet their limited access to finance and financial literacy has caused a massive barrier.

## **2.6. Nepal Annual, Plan and Budget 2022/23**

After the review of Nepal Budget 2021/22, the Government of Nepal (GoN) announced a budget of NPR 1.793 trillion (USD 14.7 billion) for the fiscal year 2022-23 (Gupta, 2022).<sup>9</sup> The objective of the budget has been set to achieve a self-reliant economy by prioritizing agriculture, industrial development, expansion of hydroelectricity and transmission lines, and promoting foreign investment and tourism.

Some provisions in terms of production and financial accessibility of the SMEs have been reflected to ensure the growth of SMEs as required. Given that a lot of SMEs have been focusing on locally-made products, the Prime Minister's Nepali Production and Promotion Program will be launched to increase domestic production by promoting an export-oriented industry and promoting domestic products. A budget of NPR 3.45 billion (USD 28.2 million) has been allocated for the program to promote 'Own Production, Own Consumption' and for other private sector initiatives which include, Make in Nepal and Made in Nepal. Furthermore, tax relief programs for SMEs have been highly prioritized by offering a tax rebate to small and medium enterprises in a bid to provide financial support for the post-pandemic growth of SMEs. In addition, at least 50% of the

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<sup>9</sup> Nepal Economic Forum: <https://nepaleconomicforum.org/key-highlights-of-budget-2022-23/>

cooperative funds are expected to invest in production activities. Under the initiative, GoN will provide a 5% grant to projects worth more than 200 million.<sup>10</sup>

## **2.7. Industrial Enterprise Act 2020**

Following the previous Industrial Act 2016, the Industrial Enterprise Act has been enacted for the efficient facilitation of industrial registration, operation, and regulation in Nepal along with the provided provisions for their support and growth. Like before, the Industrial Enterprise Act 2020 of Nepal has focused on different aspects of SME development including gender sensitization.

The act has promised the relief of MSMEs in various factors including zero fees for the registration of micro-industry under the same act, income tax exemption for micro-enterprise that is in operation upon registration at the time of commencement of this Act, 35% of fee exemption on registration for female entrepreneurs, and availability of export loan for female entrepreneurs based on their financial evaluation.<sup>11</sup>

## **2.8. Review of MEDPA**

Formally started in 1998 with a joint initiative between the Ministry of Industry and UNDP, MEDPA (formerly MEDEP) has helped increase the per capita income of micro-entrepreneurs by 343.8% from NRs. 17,605 to NRs 78,133 on average across the project's duration (UNDP, 2019).<sup>12</sup> As of 2016, out of the total micro-entrepreneurs created by MEDPA, 72% were women. This further shows that most of the SMEs in Nepal are led by women entrepreneurs. Furthermore, a report published by CBS in 2018 suggests that the share of female owners or owners in micro and small enterprises is high.<sup>13</sup>

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<sup>10</sup> Nepal Budget Speech of 2022/23:

[https://www.mof.gov.np/uploads/document/file/1656476715\\_Budget%20Translation%200031379%20cv.pdf](https://www.mof.gov.np/uploads/document/file/1656476715_Budget%20Translation%200031379%20cv.pdf)

<sup>11</sup> Industrial Enterprise Act 2020:

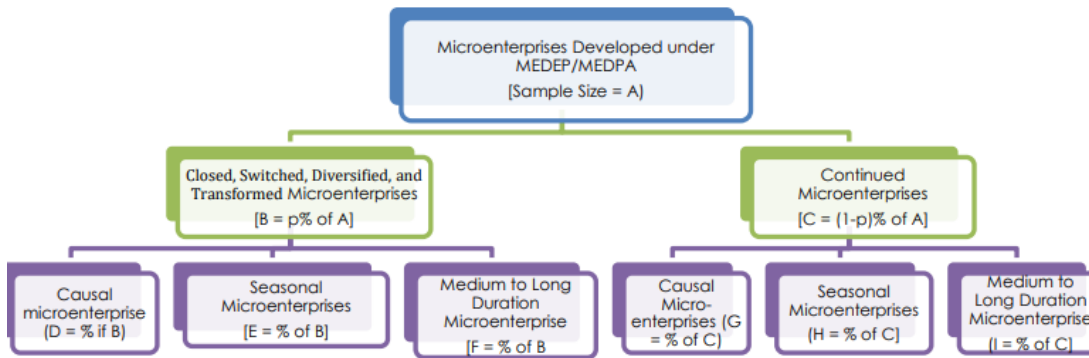
<https://moics.gov.np/uploads/shares/laws/Industrial%20Enterprises%20Act%20%202020.pdf>

<sup>12</sup> MEDEP Fact Sheet:

[https://medpa.moics.gov.np/Home/Download?fileLocation=/Content/Uploads/DownloadPublications/856f149a441742408639923c6c5d2c06\\_MEDEP%20Factsheet%202017.pdf](https://medpa.moics.gov.np/Home/Download?fileLocation=/Content/Uploads/DownloadPublications/856f149a441742408639923c6c5d2c06_MEDEP%20Factsheet%202017.pdf)

<sup>13</sup> Accessed from <https://nepalindata.com/resource/Analytical-Report-Women-in-Business/>

MEDPA classified SMEs or general enterprises largely into two categories: a. Closes, Switched, Diversified, and Transformed, and b. Continued. This classification was made to understand the ratio of successful entrepreneurs and unsuccessful entrepreneurs created by this program. The model focused on various phases that SMEs can come into after their operation. Therefore, to understand the overall mechanism and process of the survival of micro-enterprise, this model was developed.



*Fig 1 - Microenterprise Survival Model of MEDPA*

The program was targeted at the people below the nationally defined poverty line, with a special focus on women and socially excluded groups, such as Dalits, Indigenous Nationalities, Religious Minorities, Unemployed Youth, Ultra Poor, and Excluded Madheshis. MEDEP started as a pilot program in June 1998 in ten different districts. Until now, the program has covered all 75 districts of Nepal. Through MEDEP, a total number of 137,404 micro-entrepreneurs were created as of March 2018 (United Nations Development Program, 2018).

### **3. RESEARCH OBJECTIVE**

This paper would focus on mapping, identifying, and analyzing various sector policies of the government that addresses the issues faced by SMEs. The ultimate goal of this paper is to identify the gaps in the harmonization process and coherence of various policies across the government organizations that exist in the SME development of Nepal.

In order to reach the desired goal, the following objectives have been considered vital and achievable for this research project:

- a. Understanding policy dynamics that have been supporting Small and Medium Enterprises (SMEs) Development in Nepal
- b. Understanding the harmonization between government sectoral policies related to SME development in Nepal
- c. Consulting and designing policy recommendations that is coherent for the inclusive growth of SMEs in Nepal

### **4. RESEARCH QUESTION**

Based on the nature of the research topic and the scope of the study, the following research questions have been defined which can be vital in exploring the research topic elements.

- a. What is the effectiveness of existing SME-related sectoral acts and policies in Nepal?
- b. What are the interlinkages between the Nepal government's sectoral policies for SMEs Development?
- c. What are the policy gaps existing between government organizations and the growth of SMEs in Nepal?
- d. What are the structural challenges faced by SMEs in terms of policy and regulations?

## 5. RESEARCH METHODOLOGY

The research topic is primarily designed to map the given policies and structural provisions for SME development in Nepal. Therefore, qualitative research methodology can be considered a vital approach to identifying the challenges and barriers faced by small-scale entrepreneurs on the ground level and contrasting the provision at the government level.

The following structural plan has been set and is practiced for this research topic:

- a. **Research Methodology:** Qualitative
- b. **Tools:** Recording, Reflection Notes, Observation Notes
- c. **Techniques:** In-depth Interview, Key Informant Interview, Focused Group Discussion, Observation, and Case study
- d. **Sample Size Determination for Qualitative:**

Research Techniques	Sample Size Factor	Sample Size
Key Informant Interview	Local Government Representative *2, Representatives from Ministry *1, Representatives from relevant association and federation *2	5
Focused Group Discussion	Group of 5 small and medium scale entrepreneurs from the field	5
In-depth Interview Interview	SMEs * 10 (from the research location proposed below)	10

### 5.1. Area of Study

Regarding the study areas, the following locations have been considered appropriate:

Kathmandu - (Ason, Thamel, Kirtipur)

Bhaktapur - (Durbar Square Area)

Lalitpur - (Sanepa, Kupondole, Nakkhu, Patan Area)

Pokhara - (Maalepatan, Lakeside)

### **5.1.1. Background about the study area**

Since ancient times, Kathmandu, Bhaktapur, and Lalitpur have become home to the Newar Community; an indigenous group of people. Newar Community has gained wide recognition as skilled craftsmen in several fields of handicraft and is considered the protector of traditional Nepalese material culture (Charpentier, 1973).

The Newar community in the Kathmandu Valley alone has reflected their living arts and crafts for centuries in metal crafts, wood carving, stone carving, silver and gold crafts, and much more (Shrestha, 2019). Handloom has been equally very essential in the Newar Community of Kathmandu, Bhaktapur, and Lalitpur districts of Nepal.

Weaving was a major industry in the Kathmandu Valley. Many people had handlooms in their homes, and in the old days, a spinning wheel and a seed separator were the required bridal gifts (Chattopadhyay, K.P, 1923)<sup>14</sup>. Many of those businesses fall under SMEs.

The Buddhist art and paintings are equally rich and prevail in many core areas of Patan Durbar Square situated in Lalitpur District. Woodwork has been part of the traditional architecture of Nepal and wood carvings have graced monasteries, temples, places, and residential homes since the 12th century. Bhaktapur is renowned for its wood carving and is one of the good examples in the Handicrafts centers.<sup>15</sup>

Pokhara itself has been crowned for its aesthetic attraction to the tourism industry. The flow of both domestic and international tourists along with the boom of the lakeside market around Pokhara has created entrepreneurship opportunities for hundreds of local people at Pokhara. Furthermore, Pokhara is also well known for its handicraft market and felt products that are owned by small-scale entrepreneurs.

Likewise, due to the presence of varieties of indigenous traditional businesses, handmade attractions, and authentic Nepalese arts, these four locations have been considered ideal locations for the proposed research study.

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<sup>14</sup> Extracted from 'An essay of the history of Newar Culture'

[https://archive.org/stream/mobot31753002183942/mobot31753002183942\\_djvu.txt](https://archive.org/stream/mobot31753002183942/mobot31753002183942_djvu.txt)

<sup>15</sup> Extracted from <http://dhandewata.blogspot.com/2008/07/products-of-bhaktapur.html>

## 6. FINDINGS AND ANALYSIS

The findings from the field have been well analyzed and constructed in this section after the interviews with the SMEs, MFIs, and government stakeholders including the local government from various places around Kathmandu and Pokhara. The finding analysis will elaborate on the key primary data that were identified from the field research. Whereas the discussion section would contrast the correlation between the findings and the SME-related policy framework of several governmental organizations and discuss their harmonization.

The findings section of the study has been largely analyzed into two different sub-sections: Challenges and Opportunities. This classification was needed to understand the problem that SMEs are facing whereas also the untapped opportunities that can leverage the growth of SMEs.

### 6.1. Challenges

#### 6.1.1. Human Resource Management

Among several challenges faced by SMEs, Human Resource Management has been considered a very concerning factor for a lot of SMEs. About 40% of the total SMEs interviewed for this study reported that a single person has to work in several departments which leads to slower growth of the organization. About 80% of the selected SMEs had a maximum of 5 employees in their organization. The factors behind the challenge in human resource management were reported as limited financial capital, high production cost to afford additional employees, the problem of human capital in SMEs, and the growing culture of an Informal Economy.

#### 6.1.2. Market Linkage

Majority of the SMEs have responded that despite the production capacity and availability of local resources, the market development and linkage factor has created huge frustration for SMEs regarding their growth in the economy. About 40% of the SMEs mentioned that despite some enterprise development programs run by the government and private organizations, many SMEs have failed to connect their products with the market. Some other interviewed SMEs support it by claiming that “Production Training is happening frequently but least attention has been paid towards training on market development and market creation”<sup>16</sup>.

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<sup>16</sup> Extracted from field interview - 5:45 PM; 09/26/2022

About 30% of the SMEs reported that due to the price competitiveness of the imported products, products made by SMEs are unable to compete in the mainstream market. In the case of SMEs producing exportable goods, the payment gateway has been another bothering factor. These SMEs reported that due to the unavailability of payment gateways like - PayPal, they have faced problems in marketing their products on global platforms like - Alibaba, Amazon, and Etsy.

### **6.1.3. Literacy and Training**

Digital Gap and Lack of Financial Literacy as important barriers, have been reported by 90% of the total interviewed SMEs. About 60% of the SMEs interviewed during the course of this study belonged to the age category of 40+. About 85% of them were female. Some of the identified challenges regarding digital and financial literacy were in business budgeting, unawareness of loan processing, lack of financing and digital skills, unable to navigate digital technology, and little or no knowledge about government provisions for SME financing.

Furthermore, because of the knowledge gap regarding financial and digital literacy, many such SMEs have faced problems with the economic growth of their business. About 15% of the SMEs also reported proper knowledge about business development and product development could help in the growth of SMEs.

In addition, one of the SMEs raised a very interesting point about the need for language development training for local small-scale entrepreneurs residing in tourist areas. In order to negotiate with foreign customers, their ability to speak a foreign language could increase the possibility of closing the deal for most SMEs.

### **6.1.4. Policy and Structural Support**

There are several indicators from the field findings that suggest the challenge in the Policy and Structural Support of the Nepal Government. Around 30% of the respondents reported that the government hasn't been taking enough effort to localize the use of local products made by SMEs. Some suggest that the government should focus on using local products made by SMEs inside government offices too.

About 60% of the SMEs complained that they still have to spend a lot of time going to government offices for business-related services. Adding to the same point, a few other respondents suggested the need for a one-window policy and its active implementation for all business-related services

and facilities. For most of the SMEs, there was a demand for a separate SME policy or supporting institution for the efficient growth of SMEs in Nepal.

The monitoring and Evaluation factor has also been placed as a very concerning factor for a lot of SMEs. The registration of the SMEs has been recorded every year at the government portal but the stability and current status of such SMEs haven't been recorded as it doesn't show the actual progress and success of SMEs operation in Nepal. The same applies in the case of SME Financing Support. A representative of the MFI mentioned that due to the lack of a proper monitoring mechanism for SME loans, such a loan has fallen into the wrong hands in Nepal. Whereas, loans allocated for the productive sector have been misused. While the same issue has been claimed by several SMEs stating that actual SMEs are not able to reap the benefits because of a lack of proper monitoring and evaluation mechanism.

#### **6.1.5. Awareness**

Public's criticism and doubt over the products made by SMEs is yet another challenge faced by SMEs in terms of their growth and development. Almost all the respondents mentioned that people are still hesitant to buy locally-made products because of the concern about price, design, and quality. About 60% of the SMEs claim that handmade products are high in quality and durable compared to imported ones but because of the manual process, the price is slightly higher than the mainstream products.

Furthermore, they reported that because of a lack of understanding in consumers about the story and importance of such products, they are always hesitant to buy them even if the price is not a very big differential. While about 30% of the SMEs expressed their concern about the lack of government initiative and interest in promoting SME products and services among consumers. One of the SMEs based in Pokhara mentioned that the local government itself hasn't shown significant interest in the promotion of local products as they participate in SME-related programs for the sake of formality or symbolic interest rather than actual ones.

#### **6.1.6. Access to Opportunities**

Opportunities are very important factors for the growth of any enterprise. SMEs are the least advantaged group when it comes to access to opportunities. Be it access to finance or access to networking opportunities; SMEs have been deprived of such access.

About 70% of the SME respondents expressed their frustration that financial institutions are very hesitant to provide loans to SMEs claiming several factors: SMEs are vulnerable to financing, slow return from SMEs, lack of financial skills among the SME owners, and the credit history of the SMEs. Some respondents also argued that the collateral systems for SMEs have restricted them to avail of credit facilities. While about 30% of the respondents have critical observations about access to loans. They believe that the majority of SME owners are women because of this reason financial institutions are very doubtful of women-led SMEs regarding repayment of loans. On the other hand, they also expressed that these women-led SMEs have a digital gap due to which they have to forgo a lot of opportunities that can be accessed digitally.

Besides access to financing opportunities, it is also found that SMEs have the least access to networking opportunities. One of the SME owners expressed his frustration saying “A lot of industrial fairs keep on happening time and often. But I feel bad to say that SMEs are least represented where much of the economy is supported by SMEs. Even if there are few representations of SMEs, they are only symbolic as they have no access to raise their voice on the forefront.”<sup>17</sup> In addition, a lot of SMEs claimed that SME benefits are disrupted by the practice of monopoly and favoritism in institutions; be it government, private or financial institutions.

#### **6.1.7. Information Gap**

While Digital literacy has already been a major challenge for a lot of SMEs, the information gap can be critically observed as a corresponding factor. But besides the digital gap, there are several factors that SMEs are concerned about. Many of the SMEs reflected that the Government is not doing public announcements about SME plans and programs. A help desk about SMEs at each local office could help a lot of household-based SMEs but due to the lack of such availability, there is a huge gap between what the government has stated on the policy papers and what actually is happening on the ground.

About 80% of SMEs are still unaware of the provisions available to them. While others argue that there is still confusion between the acts and local government plans. The case has been the same for some of the MFIs too. One of the respondents representing MFI expressed that due to the lack of proper guidelines and information about SME policy framework for the financial institutions, credit facilities and other financial access for SMEs have been bothered.

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<sup>17</sup> Extracted from field interview, 1:35 pm; 09/21

Besides this, SMEs have been found to be left out regarding information about business development programs and opportunities. Many have complained about not getting adequate information even from the local government about such opportunities.

## **6.2. Opportunities**

Despite the challenges that Small and Medium Enterprises in Nepal are facing in terms of growth, the field study has also helped in identifying potential opportunities that can lead to the growth and development of SMEs in Nepal.

### **6.2.1. Market Promotion**

After the inception of federalism, a lot of SMEs had hope for their growth and development. However, no longer after federalism was introduced, COVID-19 took the upper hand which dismantled the whole hopes and motivation of SMEs. As we move out of the pandemic, SMEs have expected that the local government could start promoting the products locally whereas the Federal Government could apply strategies in promoting SME products in the international market through global branding and networking.

About 25% of the respondents mentioned that the Weekly market can be organized by the local government at their respective local level to identify and promote their local products and to increase awareness among the people. Furthermore, some have also expressed that understanding and localizing the market strategies through private-sector engagement could be very promising for the government to boost the growth of SMEs.

### **6.2.2. Promotion of Technological Innovation**

The Technological Revolution has been demanded by several SMEs who have faced problems of scalability. Despite their competitiveness and viability, due to the least production capacity and labor exploitation issues among SMEs, they have been looking for support from the government in terms of technological subsidies and innovation grants. About 45% of the respondents believe that technological innovation can help in boosting the growth of SMEs while balancing the traditional use of raw materials. Adding to that, some also believe that such technological changes can help in reducing the cost of production and bring relief to many other factors of SME development.

The scalability of SMEs can help in the promotion of such products in the mainstream market too. Furthermore, many such SMEs led by young people are hopeful about government support in encouraging the need for technological changes by dismantling the traditional approaches of production which are time-consuming and costly. Some have also suggested the possibility to open up small-scale Foreign Direct Investment for technological growth through the diaspora living abroad.

### **6.2.3. Cooperative Policies**

Only a few SMEs discussed the need for changes in cooperative policy and support. However, some important discussions were analyzed and have been duly reflected in this paper. Micro-Finance Institutions can play a vital role as a catalyst for SMEs. Small Business owners believe that they have more faith in cooperatives because of their proximity to residential areas and close connection with the people. However, they are demanding the need for structural changes even in MFIs to facilitate the loan facilities and services for SMEs. A couple of SMEs have suggested the need for developing policy committees within the financial institutions that look after the SMEs and entrepreneurship programs.

### **6.2.4. Resource Mapping**

Mapping resources can be another important opportunity for the government to realize the capacity of local-level SMEs and the prospects of their growth in the economy. About 25% of the interviewee expressed that the government is still lacking in identifying potential products and resources needed to promote the SMEs of Nepal at the global level. Nepal is a resource-rich country with untapped resources and opportunities. About 40% of the respondents reported the need for proper research and development from all three levels of government but they reported it in general without focusing on the area of research and development. About 65% of the respondents believe that an inter-governmental coalition is very important to focus on the resource mapping process and develop a framework that can help in promoting the growth of SMEs in Nepal.

### **6.2.5. Blended Financing**

OECD has defined Blended Financing as the strategic use of development finance for the mobilization of additional finance towards sustainable development in developing countries. A representative from a financial institution during the progress of this study mentioned the

possibility of Blended Financing in terms of SME Development (OECD, 2018). The hybrid financing model between the private sector and philanthropic institutions can help in mobilizing finance toward the development of SMEs in Nepal. Blended finance can enable agri-SMEs to access more capital and targeted financial products to grow their businesses and their contribution to the 2030 Agenda.<sup>18</sup> Furthermore, it can help in fostering financial inclusion through a focus on target-specific financing.

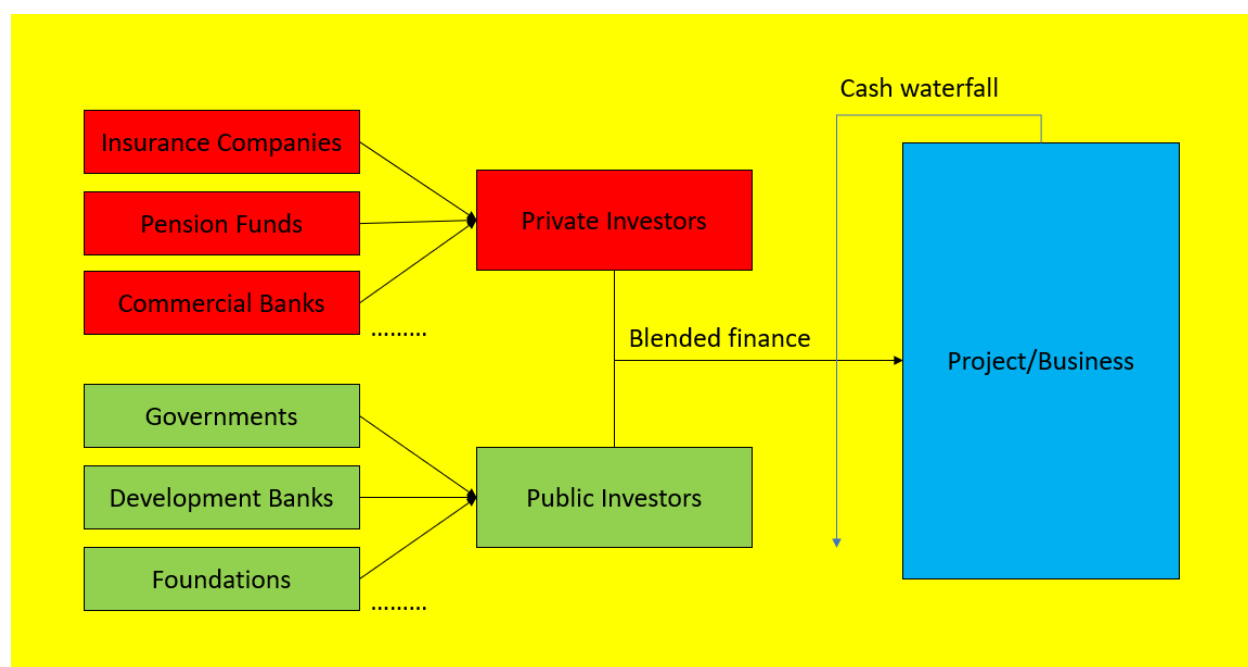


Fig 2 - Blended Finance Model (Source: Eco Intelligent)<sup>19</sup>

Blended Finance can be instrumental to mitigate the risk and failure of enterprises in financing by providing grants at the first phase and following up with the capital investment where the investor seeks a return on low risk. (Brodsky, 2019). This practice hasn't been well started in Nepal but some MFIs and financial institutions believe that this can be very helpful especially to support the development of SMEs in Nepal.

<sup>18</sup> Extracted from the report by OECD: <https://www.oecd.org/dac/financing-sustainable-development/blended-finance-principles/documents/Blended-Finance-in-Agriculture.pdf>

<sup>19</sup> Figure extracted from: <https://eco-intelligent.com/2019/11/20/understanding-blended-finance/>

### **6.3. Good Practices**

Since the inception of Federalism in Nepal, there have been remarkable changes and improvements observed at various local levels. Along with attention brought at the federal level, many local levels are now realizing the need to support enterprise development programs.

#### **6.3.1. Localization of resources**

One of the best practices that can be cited in this paper is the local-level adaptive approach adopted by Tilotamma Municipality of Lumbini Province in Nepal. The local government of Tilotamma Municipality has started using only locally available resources such as bamboo and natural fibers to completely eliminate the use of plastic materials at the Municipal level.<sup>20</sup> This has encouraged people to opt for locally available resources and support local small entrepreneurs.

There are several other examples at the local level that shows how the role of government can trigger the growth and development of SMEs. Formation of a tole development committee to support entrepreneurship and development at the local level is another good practice observed at many local level governments of Nepal. For instance, the formation of women's committees and similar local-level thematic committees has been significant in promoting the local level resource with the utilization of traditional knowledge and technology.

#### **6.3.2. Policy Interventions**

The federal government has also been supporting the growth and development of SMEs through various provisional and policy-level interventions. Nepal Annual Plan and Budget 2022/23 has prioritized SMEs in terms of budget allocation. NPR 3.45 billion (USD 28.2 million) has been allocated to promote the 'Own Production, Own Consumption' campaign and for other private sector initiatives which include, Make in Nepal and Made in Nepal. This will likely enhance the visibility of SMEs in Nepal. Similarly, Industrial Act 2020 has highlighted and effectively facilitated the relief of MSMEs in various factors including zero fees for the registration of micro-industry under the same act, income tax exemption for micro-enterprise that is in operation upon registration at the time of commencement of this Act, 35% of fee exemption on registration for

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<sup>20</sup> Noted from the conversation with the representative of Tilotamma Municipality extracted during the policy discussion series happened in Kathmandu, 2022

female entrepreneurs, and availability of export loan for female entrepreneurs based on their financial evaluation.<sup>21</sup>

In addition, to keeping MSMEs at the center, Financial Literacy Framework 2022 has been developed by Nepal Rastra Bank.<sup>22</sup> The framework has been designed to help increase financial access as well as to facilitate attaining financial system stability in a systematic manner for audiences who lack basic financial skills and knowledge. This will also help in facilitating access to finance for the disadvantaged group such as women-led SMEs.

### **6.3.3. Public-Private Partnership Model**

Through participation in various governance-related discussions and conversations with government stakeholders, it has also been observed that Government organizations are focusing on the public-private partnership model to strengthen to develop small and medium enterprises. Discussions about prioritizing foreign direct investment for SMEs have been growing at the government level. While there is an urgency to increase the implementation of this model, the positive factor of the government's attention towards this model can be observed as a very good approach.

The practice has already been implemented in several local-level governments in terms of infrastructural development and entrepreneurship programs. Various local government at the municipal level has started incubation program and production training in partnership with the private sector.

### **6.3.4. Institutionalization of Support Program**

Finally, enterprise development program such as MEDPA has been formally institutionalized by the Government of Nepal to support the development and promotion of SMEs in Nepal. With the end of the fourth cycle of MEDPA, the government is planning to continue the implementation of such a program to increase the participation of SMEs and support their growth in the economy. Despite the sluggish pace of growth of SMEs in Nepal, the role of the government cannot be ignored in its continued intervention and approaches towards its effort on SME development. The potential steps and collaborative interventions have been discussed in the following section.

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<sup>21</sup> Industrial Enterprise Act 2020:

<https://moics.gov.np/uploads/shares/laws/Industrial%20Enterprises%20Act%20%202020.pdf>

<sup>22</sup> Financial Literacy Framework 2022 by NRB:

<https://www.nrb.org.np/contents/uploads/2022/11/Financial-Literacy-Framework-2022.pdf>

## 7. DISCUSSION

The Industrial Act 2020 has categorized types of industries on the basis of different indicators. However, many SME owners have their own understanding of SMEs and it is found that there is a huge confusion about the government's definition and actual status of micro, cottage, and small enterprises in Nepal. Even the reports by government organizations and bilateral organizations have not been able to desegregate the data on the type of lower-level enterprises, instead many of the data have been represented in the form of three levels of industries; small, medium, and large. This has created a problem in identifying the actual data for the study of MSMEs in Nepal.

Industrial Policy 2011 of Nepal has indicated several provisions to facilitate the growth of SMEs in Nepal however 90% of the responses from the field claim that prioritization towards SMEs is still very knee-high. From the promotion of the SME market at the local level to the one-window practice for the business regulation process, the challenges are yet still the same for SMEs. Furthermore, despite the past 10 years of its formulation, Industrial Policy 2011 hasn't brought any significant changes with digitalization and incorporation of ICT in the SME sector. The policy has mentioned using information technology for the promotion of micro-enterprises, cottage, and small industries through IT Hub. The inter-governmental coordination between the Ministry of Industry and the Ministry of Communication and Technology is yet to be strengthened here.

There is still an abundance of flaws when it comes to governmental organizations looking after the financial structure. An analytical report by CBS in 2018 reports that the share of small and micro businesses in Nepal is bigger in the case of Women. Whereas the Federation of Small and Medium Enterprises Nepal says despite women owning 60 percent of Nepal's small and medium-sized enterprises, their limited access to finance and financial literacy has caused a massive barrier to the growth of SMEs (NRB, 2018). While Industrial Enterprise Act 2020 of Nepal has focused on different aspects of SME development including gender sensitization. Still proper regulation and guidelines regarding gender-lens investment are missing from the financial institutions.

Despite priority for credit facilities given towards the productive sector (about 50%), lack of regulation and proper monitoring from the financial institutions has avoided the actual SMEs to reap the benefits. A lot of SMEs have reported that a lack of financial literacy and skills has also created obstruction for them to understanding the utilization process of credit facilities. Monetary Policy 2022 has mentioned the preparation of the Financial Literacy Framework 2022 in coordination with the Ministry of Education, the Curriculum Development Centre, and the

Government of Nepal (NRB, 2022). However, the Financial Access Report prepared by NRB in 2018 suggests that the Monitoring and Evaluation mechanism is missing to measure the success of the Financial Literacy Framework in Nepal, which must be included in the framework.

Similarly, the 14th plan saw progress in terms of employment generation, women's participation, cooperatives run by women, operation of small and medium cooperative enterprises, and co-operative farming scheme, however, it has not been as significant as targeted. The financial accessibility of women and SMEs have mostly been symbolic. The inclusion of SMEs and MFIs-related stakeholders in the local government planning process for SME development is still lacking. A directive from the National Planning Commission can be very significant in this regard. However, the challenges of SMEs mentioned in the review of the 15th periodic plan are very evident and true when it comes to contrasting with the ground reality.

The Constitution of Nepal 2015 in part 51 has also stressed on promotion of domestic industries, utilization of locally available resources, and creation of an environment for export of the for domestic goods and services that are produced locally. However, challenges like payment gateway, unregulated export guidelines, and insufficient support from government institutions have still created barriers for SMEs to grow in the global economy.

While the Industrial Act of Nepal 2020 has provisioned for several waivers including zero fees for the registration of micro-industry under the same act, income tax exemption for micro-enterprise that is in operation upon registration at the time of commencement of this Act, 35% of fee exemption on registration for female entrepreneurs, and availability of export loan for female entrepreneurs based on their financial evaluation, yet a lot of SMEs are unknown and uninformed about these provisions because of their access to this information. Furthermore, some SMEs have claimed that despite the provisions, they are not able to get those waivers as indicated in the policy papers.

One of the very important programs of the government, MEDPA which has been directly linked with MSME development, has lasted for the past two decades. MEDPA has made significant progress in terms of producing a large number of local entrepreneurs across all seven provinces and 77 districts of Nepal. However, a few of the former participants of MEDPA informed that market linkage and development-related training is still in the infant phase for most of the government-led programs. Despite extending product and business incubation for a long, they have

desired for inclusion of market linkage and development workshops to increase the possibility of their success in the market. Additionally, some of the SMEs who wanted to build collaboration with other relevant SMEs find it difficult to reach out to such enterprises because of the unavailability of data and their current status.

## **8. KEY POLICY RECOMMENDATIONS**

The purpose of this research was to map the SME-related policy landscape across government organizations and their harmonization. Based on these reflections, the paper also intended to design some policy recommendations for government organizations. These recommendations are highlighted based on close consultations with the relevant stakeholders including; SMEs, MFIs, government stakeholders, and other private institutions.

### **Policy Support and Mechanism**

- Formulation of SME Policy is needed and urgent to further enhance the growth of SMEs
- Separate SME unit at each local unit to monitor the approval of SME loans and SME selection is required
- Monitoring and Evaluation mechanism for registered SMEs and their status update
- Public Announcement regarding SME programs must be made by local government
- Enabling export environment for SME through payment gateway integration and market facilitation
- SME or Entrepreneurs help desk at each local level is needed
- Localization of locally made products in government offices and community is must
- Facilitation by all forms of government to certify the local products with International Market Standard
- Coherence between three levels of government to design SME standard policies or framework that aligns with each level of government and their need
- SME or entrepreneurial related governmental unit is highly recommended at all the 753 municipalities across Nepal under the direction of Federal government

### **Public-Private Partnership Model**

- Government stakeholders must strengthen tie-up with private sectors such as: incubation centre, corporate and manufacturers to introduce inclusive incubation programs for SMEs
- Developing digital literacy training for SMEs along with Information Technology related offices
- Designing market development related handbook and training for SMEs
- Digitalization of registered SMEs through the help of private sector engagement
- Organize weekly or bi-weekly market in collaboration with restaurants or hospitality businesses to promote locally made products and create general public awareness

### **Literacy and Training**

- Nation-wide focus on digital and financial literacy campaign for all the SMEs especially women-led SMEs is required; this could include localization of the literacy campaigns with the local context and challenges
- Language and soft skill development programs for disadvantaged SMEs
- Political Literacy must be localized to ensure that MFIs and SMEs are included in local level planning process for SME

### **Restructuring Financial Provision**

- Inclusion of Monitoring and Evaluation on Financial Literacy Framework is must
- Monitoring Committee for SME loan is required at every local level
- Financial Literacy Training for SMEs must be made compulsory
- MFIs must be mobilized to support women entrepreneurs in Loan Utilization Process
- Gender-lens Investment Plan must be designed and implemented to ensure women SMEs have access to finance
- Financial accessibility should be promoted even without collateral in case of SME
- Entrepreneurship Council must be formed in every MFIs to support SMEs

- Women empowerment committee should be reformed in every local unit to increase women's access to a loan

### **Inter-governmental agency Coherence**

- Enterprise related coalition between women's committee like: Aama Samuha and local government organization should be strengthened at the local level
- SME development related periodic review and progress meeting between three levels of government should be conducted
- Networking and best practice sharing event should be prioritized among all the 753 municipalities of Nepal, an example of Tilotamma Municipality promoting local products by eliminating plastic uses could be a great learning example for other municipalities
- Monthly review and reflection are needed between sectoral organizations of Government to identify the gaps between government organizations
- Policy gap between the Ministry of Industry and the Ministry of Finance are huge, therefore proper coherence and harmonization between these two governmental agencies is a must
- Coordination between three levels of government in terms of SME related policy and provision
- Joint initiative between sectoral organization could be best to enhance the growth of SMEs; an example could be forming an SME council at federal government with the inclusion of different governmental agency

## 9. CONCLUSION

The status of SMEs in Nepal has not significantly changed as various acts and policies have intended. There are still gaps between inter-governmental harmonization. The field findings have suggested that despite some improvements in the development of SMEs, there is still a long way ahead for the intended growth of SMEs. Factors like - access to financing, digital gap, access to opportunities, information gap, and market linkage are still major challenges to be resolved. Having a large number of female entrepreneurs leading SMEs on the ground, financial institutions must be driven towards business development financing along with gender-lens investment to support these small-scale entrepreneurs through an inclusive model. In addition, the Blended Financing model can be a better option for financial institutions to collaborate with private and public partners to ensure the financial gain of the SMEs and possible return on investment for the investors. The model can also assist SMEs in market linkage and development through the support of investors. Along with this, the need for SME policy is urgent and utmost, therefore, the Ministry of Industry could proceed ahead for inclusive consultations with sectoral ministries and relevant organizations for the formulation of SME policy. To further support the growth of SMEs, a separate SME governing body could be formed given that more than 60% share of industrial registration is occupied by small-scale industries. With these structural changes and sectoral interventions from respective governmental bodies, the status of SMEs can be enhanced and developed.

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## **Annex**

### **ANNEX I**

#### Interview Questionnaire

##### **SMEs**

1. What is your understanding of SMEs?
2. What are the products and services offered by your organization?
3. How many people are working in your enterprise now?
4. What are the major market areas of your enterprise?
5. How do you see the growth of your enterprise in recent times?
6. What are the challenges faced by your enterprise?
7. How is your experience of going to government offices for your enterprise-related services?
8. What is your opinion on starting a small business enterprise in a country like Nepal?
9. What is your reflection about programs and policies for SME development in Nepal?
10. Do you think that the Government has structural support in developing small businesses in Nepal? Explain briefly
11. Do you see any potential for the export of your products to the International Market? If yes, how do you see the support from the Government?
12. Are you aware of the local government provision for businesses like yours?
13. What kind of Government plans and programs would you prefer for businesses like yours?
14. Do you think there is a need for a separate SME policy in Nepal? What are your expectations?
15. What is your reflection on the government's paper framework for SME development and the ground reality?

##### **Government Organizations**

1. What is your understanding of SMEs in Nepal?
2. How do you differentiate Micro Enterprise and Small Enterprise in terms of the working model?
3. What are your sectoral plans and programs for the development of SMEs in Nepal?
4. Are there any challenges for the government in addressing the issues of SMEs in Nepal? What are they?

5. Is there any coordination mechanism between government organizations for SME development in Nepal?
6. Do you see the larger prospect of boosting SME development in Nepal?
7. What are the possible reasons that the government doesn't have an SME Policy?
8. Do you think SME policy would work for a country like Nepal?
9. Are there any frequent inter-governmental discussions or meetings often related to SMEs?
10. What are the technical challenges of the government to support and develop the SME sectors of Nepal?

### **Financial Institutions**

1. Does your institution work for SME development in Nepal?
2. What challenges do you see in uplifting the growth of SMEs?
3. How often do you support SMEs in terms of financial literacy?
4. What are the provisions available in your institution for SMEs?
5. What are the gaps that you have felt between government plans and the ground reality of SMEs?
6. Are there any trust issues between financial institutions and SMEs? Please explain
7. What are your institutional criteria for supporting SMEs financially?
8. Do you see the prospect of SME growth in Nepal?
9. Do you need any technical support from the government to boost SME development?

### **Membership Organization for SMEs**

1. How many SMEs are part of your membership organization?
2. Is there any coordination between your organization and Government Organization?
3. What are the existing challenges faced by SMEs in Nepal?
4. Are there any institutional support provided to the SMEs of your network?
5. What are your observations about the policy dynamics for SME development in Nepal?
6. Does Government provide enough support for your organization?
7. Have you ever got a chance to participate in any of the policy-level dialogues or discussions with the government?
8. Do you think there are any bureaucratic hurdles for SME growth in Government organizations?
9. Do you think there is a harmonization between government organizations to support SME-related policies?

## ANNEX II

### Consent Form

#### Consent to take part in research

- I..... voluntarily agree to participate in this Daayitwa Nepal's Fellowship Research Study
- I understand that even if I agree to participate now, I can withdraw at any time or refuse to answer any question without any consequences of any kind.
- I understand that I can withdraw permission to use data from my interview within two weeks after the interview, in which case the sensitive material will be deleted.
- I have had the purpose and nature of the study explained to and I have had the opportunity to ask questions about the study.
- I understand that participation involves in-person interview which also includes audio recording for future references and backup materials for information gathering related to research topic or particular field of research
- I agree to my interview being audio-recorded.
- I understand that all information I provide for this study will be treated confidentially and solely for the purpose of Daayitwa Nepal's Strategy Public Policy Fellowship Research.
- I understand that in any report on the results of this research my identity will remain anonymous unless required by the law of work or testimonial.
- I understand that if I inform the researcher that I or someone else is at risk of harm they may have to report this to the relevant authorities - they will discuss this with me first but may be required to report with or without my permission.
- I understand that signed consent forms and original audio recordings will be only valid throughout the Daayitwa Nepal Fellowship period.

· I understand that under freedom of information legalization I am entitled to access the information I have provided at any time while it is in storage as specified above.

· I understand that I am free to contact any of the people involved in the research to seek further clarification and information.

Signature of research participant

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Signature of participant

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Date

I believe the participant is giving informed consent to participate in this study  
Signature of researcher

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**Signature of researcher**

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**Date**

## ANNEX III

### Data Coding and Analysis

Data Number	Key Extractions	Codes	Themes
1	<p>SMEs are considered in terms of their Scale of work, less investment, small physical store or no store, Human resource Management cost is very high, low investment margin for SMEs, high production cost, logistic cost, then transaction cost, and also limited market linkage, lack of government monitoring and supervision on business stability, Government is missing the point for the need for promoting social and environment-friendly businesses, One-window system is still missing, proper information is missing especially people with least digital knowledge, Digital gap for 40+ women, weekly local market events featuring SMEs by the government could be very vital, International Branding Support from government can be vital, Need for SME Policy, Strengthening tie-up with private partners is a must, SME Help Desk in each local government can be best</p>	<p><b>Challenges:</b> Human Resource Management, Financing, Market Linkage, M&amp;E from Government, One-window system, and Digital Gap  <b>Opportunities:</b> Weekly Local Market by Government for SMEs, International Branding of local SMEs  <b>Suggestions:</b> SME Policy, Private-Public Partnership, SME Help Desk in each local government</p>	<p><b>Challenges:</b> Human Resource Management, Market Linkage, Literacy, Government Structure  <b>Opportunities:</b> Market Promotion  <b>Suggestions:</b> SME Policy Support, Public-Private Partnership</p>
2	<p>Limited capacity, capital, human capital, customer and product market fit, lack of customer's understanding, lack of understanding of customer about product story, Provision for locally made products a compulsory, There's a huge information gap between what government says and how SMEs receive, need for SME policy, creating criteria for supporting small business is required or example promoting paper products rather than</p>	<p><b>Challenges:</b> Limited Capacity, Human Capital, Customer's Understanding and Perception,  <b>Opportunities:</b> Governmental Structure for SME  <b>Suggestions:</b> Wide campaign, promotion of products in government offices, Financial Literacy for SMEs, Digital Literacy</p>	<p><b>Challenges:</b> Human Resource Management, Awareness  <b>Opportunities:</b> Government Structure  <b>Suggestions:</b> Awareness and localization, Literacy and Training</p>

<p>plastic, push from government, promotion among consumer mass, advocacy programs are required, promoting products made by SME in government offices, Financial Literacy for actual SMEs are still a huge gap as these entrepreneurs are not able to digitally promote their products and have to depend on mediator</p>		
<p>People complain a lot about allo being handmade and a tedious process, very difficult to explain why people don't see the benefits of these resources, map out resources, know the sources, understand market and connect with the market Government should help SMEs to figure out the value chain and market linkage process, production training is happening several times but lacks market development training, government should support for technological innovation, huge gap between people's perception and SMEs' products, SME loans must be approved by those who belong to the SME category, actual SMEs are not getting the loans, Programs like MEDPA come and introduce so many entrepreneurs, but still so many entrepreneurs have faced problem with marketing, government organize frequent industrial fair but I am very surprised that there is no representation of SMEs, small scale entrepreneurs don't have access to networking opportunities, concrete and systematic policy that defines value chain, focus on research and development, and create a market development mechanism</p>	<p><b>Challenges:</b> Consumer Perception, Market Linkage and Training, Representation in Industrial Fair, Networking Opportunities <b>Opportunities:</b> Technological Innovation, Localization of Nepal-made products, Entrepreneurial Mindset <b>Suggestions:</b> SMEs loan approval institution, Monitoring and Supervision by Government</p>	<p><b>Challenges:</b> Awareness, Market Linkage, Access to Opportunities <b>Opportunities:</b> Promotion of Innovation, Awareness and localization <b>Suggestions:</b> Government Structure</p>

3

	<p>is required, No preparation yet from the government side to focus on localizing nepali made products, monitoring and supervision</p> <p>by Government is very important in marketing of the products, Focus on hybrid-production mechanism is also important as</p> <p>government should check about the availability of such machines and resources, Entrepreneurial Mindset' among general public</p> <p>along with capacity building program and market linkage</p>		
<p>4</p>	<p>Coalition between women's committee through different toles (neighborhood) of ward, production capacity is huge but market development is lacking</p> <p>Price competitiveness of imported products has created difficult for SMEs, local government has started 5 year entrepreneurship program,</p> <p>Access to networking and resource opportunities is lacking for SMEs,</p> <p>There is a need for linking every cooperative with SME programs,</p> <p>Cooperative policy focusing on SME can be formulated by institutionalizing service system, Cooperative system can be very effective</p> <p>because of close connection and proximity with the local communities,</p> <p>Lack of concrete framework and process for MFIs to support SMEs,</p> <p>Women empowerment committee should be reformed to increase women's access to loan, SME loan for productive sector has been allocated but due to lack of monitoring these loans have been misplaced,</p> <p>Entrepreneurship Council in every MFIs should be established, focus on market linkage is must, Many SMEs focus on informal economy because SME cannot afford for regular salary-based worker,</p> <p>Digital Marketing should</p>	<p><b>Challenges:</b> Market Development, Price Competitiveness, Networking Opportunities, Clarity on MFIs, Loan Process Monitoring</p> <p><b>Opportunities:</b> Cooperative policy for SMEs, Entrepreneurship Council setup</p> <p><b>Suggestions:</b> Digital Marketing, Market linkage and Development, reformation of women's committee</p>	<p><b>Challenges:</b> Market Linkage, Access to Opportunities, Government Structure</p> <p><b>Opportunities:</b> Cooperative Policy</p> <p><b>Suggestions:</b> Literacy and Training, Government Structure</p>

	be promoted		
5	<p>Market linkage is a very significant issue despite of long SME journey, Financial Institution has doubt over SMEs regarding the repayment plan of SMEs,</p> <p>Entrepreneurial Support hasn't been changed despite after federalism, handicrafts and SMEs are high market potential if government focuses on the same level of advocacy campaign and promotion from their level, English Speaking is a must for all the SMEs working in tourism sector of Nepal that's why government and private sector can come up with the plan for Language Skill Development along with business incubation program, Government can support in running the workshops for aspiring entrepreneurs who wish to start small businesses in Nepal</p>	<p><b>Challenges:</b> Market Linkage, Trust issues for Financing,</p> <p><b>Opportunities:</b> English Language Skill Development Training</p> <p><b>Suggestions:</b> Workshop Facilitation for SMEs</p>	<p><b>Challenges:</b> Market Linkage, Access to Opportunities</p> <p><b>Opportunities:</b> Literacy and Training</p> <p><b>Suggestions:</b> Literacy and Training, Participant Selection</p>
6	<p>Criticism from general public for SME products still exist, Policy framework is still missing in terms of SME development and promotion, Government has failed in identifying actual SMEs for SME benefit plan as networking and favoritism is still prevailed among government organizations and private sectors, local government needs to do public announcement related to SME development time and often as digital gap still exists for SMEs, focus on connecting resources to small-scale entrepreneurs is necessary, even if government does SME related training and programs, problems like wrong audience selection persists</p>	<p><b>Challenges:</b> Public Criticism, Policy Framework, Identification of actual SMEs, favoritism, digital gap, wrong audience selection</p> <p><b>Opportunities:</b> -</p> <p><b>Suggestions:</b> Public Announcement related to SME development, digital literacy</p>	<p><b>Challenges:</b> Awareness, Government Structure, Access to Opportunities</p> <p><b>Opportunities:</b></p> <p><b>Suggestions:</b> Literacy and Training, Government Structure</p>

	because the trainee are not sure about continuation of business, appreciation model from the government organization still lacking.		
7	<p>SMEs are financially least but valuable with resources, financial burden is very high, Raw materials unavailability, import tax exist, time-consuming process,</p> <p>and government structural challenges, human resource management is a big issue for SMEs, still time consuming process at government offices and has lot of transaction cost, information gap related to SME exist, need for subsidies and small grants for actual SMEs, tax-liability must be actually waived for eco-friendly businesses, access to finance and information about financial accessibility is needed to every SMEs</p>	<p><b>Challenges:</b> Raw materials unavailability, import tax exist, time-consuming process, and government structural challenges, human resource management, information gap</p> <p><b>Opportunities:</b> SMEs are valuable enterprise</p> <p><b>Suggestions:</b> Subsidies and small grants, tax-liability waived, access to finance and small business information</p>	<p><b>Challenges:</b> Government Structure, Human Resource Management, Information Gap</p> <p><b>Opportunities:</b> Resource Mapping</p> <p><b>Suggestions:</b> SME Policy Support, Literacy and Training</p>
8	<p>One window-policy about SMEs is still lacking, bureaucratic hurdles is high, small grant program for SMEs could be very valuable, not enough support from government in localizing local products and services, international facilitation by government for exporting the products is needed in terms of payment gateway, digital gap is high among female SMEs as majority of the SMEs accounts for female owners, there is no proper monitoring and track about the status of registered SMEs in Nepal, digitalization of SMEs and their products is still missing as lot of SMEs have to be dependent on medicator, private sector engagement must be prioritized by all forms of government</p>	<p><b>Challenges:</b> One-window policy, localization of products, Digital Gap, M&amp;E Mechanism, Digitalization of SMEs</p> <p><b>Opportunities:</b> International Facilitation for export</p> <p><b>Suggestions:</b> Small grant program for SMEs, Private Sector Engagement</p>	<p><b>Challenges:</b> Government Structure, awareness, Literacy</p> <p><b>Opportunities:</b> Market Linkage</p> <p><b>Suggestions:</b> SME Policy Support, Public-Private Partnership</p>

<p>9</p>	<p>Lot of women entrepreneurs belong to SMEs category, problem is that these women entrepreneurs lack financial literacy as they are unaware about the process of loan securement and repayment plan, women-friendly desk is lacking to see the entrepreneurship benefits from gender-lens too, Focus on digital and financial literacy is very important, loss of indigenous, natural and cost-effective practice in SMEs because of lack of support and resources, Change in women participation compared to before but still participation may be symbolic rather than actual, subsidy plan by government must be well targeted as actual SMEs are deprived of such facilities, Blended Financing Model can be adopted for SMEs development in Nepal, Women Entrepreneurs need more support for 'Loan Utilization Process', Financial Institutions are yet hesitant to provide loan for Women SMEs, Gender Lens Investing is needed for promoting women-led SMEs, Digital Footprint of SMEs is very important to access loan, Digital and Financial literacy should be incorporated in mainstream education</p>	<p><b>Challenges:</b> Financial Literacy, Women-friendly desk, loss of indigenous practise, Trust issues for loan to women, <b>Opportunities:</b> More women entrepreneurs, Blended Financing Model, <b>Suggestions:</b> Financial Literacy along with digital, Well targeted subsidies, loan utilization training for women, Digital Footprint for SMEs, Gender lens investing,</p>	<p><b>Challenges:</b> Access to opportunities, Awareness, Literacy <b>Opportunities:</b> Blended Financing <b>Suggestions:</b> Literacy and Training, Participant Selection</p>
<p>10</p>	<p>Training on women entrepreneurship from women's committee under each local ward, Business Development and Market Linkage is still missing, only provision for collateral has caused problem in accessibility of loan for SMEs or else financial institutions are looking for credit history of SMEs to see their viability, Various sub-committees under MFIs can be formed to support SME sector development, still has trust issues towards SMEs, monopoly in access to finance, slow return from SMEs has forced MFIs to treat SMEs differently, actual SMEs are not getting the benefits</p>	<p><b>Challenges:</b> Business Development and Market Linkage, Collateral Loan, Credit History, Trust issues from MFIs, <b>Opportunities:</b> Women's Committee on Entrepreneurship Training, MFIs as a catalyst for SME <b>Suggestions:</b> Critical acceptance of business plan by MFIs, Political inclusion of MFIs and SMEs, Digital and Financial Literacy</p>	<p><b>Challenges:</b> Literacy, access to opportunities <b>Opportunities:</b> Government Structuring <b>Suggestions:</b> SME Policy Support, Political Inclusion</p>

<p>as promised, MFIs should critically accept business plan with proper market feasibility study, MFIs can work as a catalyst for growth of SMEs in Nepal, There is high prospect for small scale</p> <p>FDIs, Financial accessibility should be promoted even without collateral, digital transaction should be promoted to enable digital footprint of SMEs, digital</p> <p>gap should be reduced specially for women-led SMEs, focus on product-market fit is important by SMEs and government too, government only encouraging</p> <p>SMEs for the sake of formality, MFIs and SMEs should be included in local level planning process for entrepreneurship and enterprise related policy</p>		
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