

FACTORS AFFECTING BUSINESS SUCCESS OF SMALL & MEDIUM ENTERPRISES (SMEs)

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Abstract

The objective of this study was to identify determinants of small and medium enterprises (SMEs) business success in an underdeveloped country like Bangladesh. The intention of this study is to provide the understanding of how people should start their business by looking at all the factors affecting business success hence help to reduce the risk of failure and increase chances of success in starting a business for SMEs. Findings of this study are useful for entrepreneurs and policy makers of the country. The study examined six factors that influence the SMEs business success. These factors are: characteristic of SMEs, management and know-how, products and services, the way of doing business and cooperation, resources and finance, and external environment. The theoretical framework has been drawn out and questionnaire was designed based on the factors chosen. The data collected were analyzed by using SPSS program which provides relevant analysis such as reliability analysis, frequency analysis, regression analysis, one-way ANOVA and T-test. Six hypotheses were developed to study the determinants of Business Success of SMEs in Bangladesh. The entire hypotheses were successfully tested with SPSS and four hypotheses were accepted. The regression analysis result shown that the most significant factors affecting business success of SMEs in Bangladesh were products and services, the way of doing business, management know-how and, external environment.

Key Words: Business Success, SMEs, Bangladesh

Introduction

Research into small and medium sized enterprises (SMEs) has grown strikingly during the last decade. This intense attention in the backdrop of the failure of various structural and trade policy reforms to stimulate any significant response from the private sector is remarkable, and seems to suggest that liberalisation measures must be supplemented by pro-active policies to attain the desired goal (Bhattacharya, 2002). A huge majority of firms worldwide are SMEs, and they play a significant role in the economy. There is a broad consensus that a vibrant SME sector is one of the principal driving forces in the development of a market economy. SMEs stimulate private ownership and entrepreneurial skills, are flexible and can adapt quickly to changing market demand and supply situations, generate employment, help diversify economic activity, and make

a significant contribution to exports and trade. Even in the developed market economies SMEs account for a large share in output and employment (UNECE, 2003). Bangladesh has thus far failed to maximize the benefits derived from the SME sector, which promises and needs to play a pivotal role in promoting and sustaining the industrial as well as overall economic growth (Ahmed M. U., 2003). The failure can be attributed to various reforms and trade liberalisation measures that have squeezed the sphere of Government's activity in business. Consequently, the private sector has to lead the economy in a dynamic growth path. Most of the previous studies dealing with the conditions of successful business have focused on large companies rather than SMEs (i.e., Ghosh and Kwan, 1996 ; Kauranen, 1996 and Pelham, 2000). However, changes in the environment cause more uncertainty in SMEs than in large companies. Their resources for acquiring information about the market and changing the course of the enterprise are more limited. The response to environmental changes is different in SMEs than in large companies. Large firms may even exit from one of its business areas, but this is not usually possible in a single-business firm. The options for responding are limited by the firms' resources and strategic choices as well as by the opportunities offered by the industry and location. Those ways may also differ between the development stages of the firm. SMEs have long been believed to be important in supporting economics development within a country (Mazzarol, Volery, Doss, & Thein, 1999). One of the important roles of SMEs in this context includes poverty alleviation through job creation. Thai SMEs are increasingly seen as creator of new jobs (Swierczek & Ha, 2003) and Vietnamese SMEs employ 64% of industrial workforce.

Literature Review

The word enterprise has been used in a range of contexts and meanings (Bridge, O'Neill & Cromie 2003). Salminen (2000) describes an enterprise as a controlled system consisting of a detector, a selector and an effector. The detector is the function by which a system acquires information about its environment, which is then used as the basis of the selection of a behavioral response by the selector. Finally, the behavior is executed by the effector. The measurement system of an enterprise gathers information about the changes in both the environment and the performance of the enterprise. This information is then used together with the values and the preferences of the enterprise and its management to produce decisions about the required actions. As a result, the outputs of the enterprise – the products, the services, the operational performance and the financial performance - are changed.

Firm performance refers to the firm's success in the market, which may have different outcomes. Firm performance is a focal phenomenon in business studies. However, it is also a complex and multidimensional phenomenon. Performance can be characterized as the firm's ability to create acceptable outcomes and actions.

Success, in general, relates to the achievement of goals and objectives in whatever sector of human life. In business life, success is a key term in the field of management, although it is not always explicitly stated. Success and failure can be interpreted as measures of good or indifferent management. In business studies, the concept of success is often used to refer to a firm's financial performance. However, there is no universally accepted definition of success, and business success has been interpreted in many ways (Foley & Green 1989). There are at least

two important dimensions of success: 1) financial vs. other success; and 2) short- vs. long-term success. Hence, success can have different forms, e.g. survival, profit; return on investment, sales growth, number of employed, happiness, reputation, and so on. In other words, success can be seen to have different meanings by different people. In spite of these differences, people generally seem to have a similar idea of the phenomenon, i.e. of what kind of business is successful.

Contribution of SMEs in the National Economy of Bangladesh

Any precise quantitative estimate of the importance of SMEs in Bangladesh economy is precluded by non-availability of comprehensive statistical information about these industries at the national level. BSCIC estimates suggest that there are currently 55,916 small industries and 511,612 cottage industries excluding handlooms. Including handlooms, the number of cottage units shoots up to 600,000 units indicating numerical abundance of small and cottage industries (SCIs) in Bangladesh. The most recent private sector survey estimates the contribution of the micro, small, and medium enterprises (MSMEs) is 20-25% of GDP. Quoting informal Planning Commission estimates, the SEDF puts the number of medium enterprises (undefined) to be around 20,000 and that of SCIs to be between 100,000 to 150,000. This wide variation in the BSCIC and Planning Commission estimates of the number of SMEs might be due to at least two reasons: (a) different definitions of SMEs and (b) different coverage of SME families. There is an urgent need for adopting and using a uniform set of definitions for SMEs by all government agencies to help formulation of pro-active SME promotion policies. Regardless of the correct magnitude, SMEs undoubtedly play a very important role in the economy of Bangladesh in terms of output, employment, and private sector activities (Ahmed, 2003). They are quite predominant in the industrial structure of Bangladesh comprising over 90% of all industrial units. Together, the various categories of SMEs are reported to contribute between 80-85% of industrial employment and 23% of total civilian employment (SEDF, 2003). However, serious controversies surround their relative contribution to Bangladesh's industrial output due to paucity of reliable information and different methods used to estimate the magnitude. The most commonly quoted figure by different sources (ADB, World Bank, Planning Commission and BIDS) relating to value added contributions of the SMEs is seen to vary between 45-50% of the total manufacturing value added.

A significant proportion of SME activities may be in the informal sector, for which there is no dependable information. Besides, the survey estimates SME contribution based on an approach that requires the use of data on profits earned by enterprises. However, it is very difficult to gather and measure profits of establishments. Therefore, the aforementioned contribution of SMEs may be underestimated. Further discussions on the role of SMEs in Bangladesh's economy can be found in (Ahmed, M.U., (2003). The robustness of SME contributions to employment generation is a common phenomenon in most developing countries in that the magnitude varies between 70% to 95% in Africa and 40% to 70% in the countries of the Asia-Pacific region (Ahmed, M.U., 1999). While SMEs are characteristically highly diverse and heterogeneous, their traditional dominance is in a few industrial sub-sectors such as food, textiles and light engineering and wood, cane and bamboo products. According to SEDF sources quoted from ADB (2003), food and textile units including garments account for over 60% of the registered SMEs. Various recent studies (Ahmed, M.U. 2001, ADB 2001, USAID 2001) show that SMEs have undergone significant structural changes in terms of product composition, degree of capitalization and market penetration in order to adjust to changes in technology, market demand and market access brought by globalization and market liberalization.

Growth of SMEs in Bangladesh

In terms of number of establishment, the SME sub-sector has exhibited notable dynamism. Table 1 presents the trend of SME sector growth. Available evidence (Ahmed M.U. et. al., 1992) suggests that 60% of new industrial enterprises during 1980s were SMEs.

Table 1:
Growth of SSIs sector (Excluding Handlooms) in Bangladesh

Year	No. of Units		Employment		Value Added (Tk.) Small and Cottage Combined
	Small	Cottage	Small	Cottage	
1981	24,590	321,743	322,110	855,200	17,987
1991	38,294	405,476	523,472	1,331,032	21,154
2001	55,916	511,621	808,959	1,166,724	29,323
Average Annual Growth Rate	6.4%	3.0%	7.6%	4.7%	3.2%

Source: Ahmad, M. U., 2001.

Growth in SME employment seems to have been even better during the same period. The dismal performance in value added growth is explained by the weak and faulty database used by the Bangladesh Bureau of Statistics (BBS) to estimate the parameters (Bakht 2001). Indeed, when revised estimates of value addition in the SMEs are made using the new system of national accounts⁸, the annual compound rate of growth of value added by the SME sector not only shoots up to 7.7% per annum during 1989/90 and 1994/95, it exceeds that of the large-scale industries during most of the 1990s.

Broadly four industry categories (food and allied products, textiles and apparels, and engineering and fabricated metal products) currently dominate the SME sector in Bangladesh. In recent years, other industries which have grown in importance in the SME sector are light engineering, readymade garments, printing and publishing, wood and wood products, plastic products, electrical goods, electronics, artificial jewelers, wooden and steel furniture, television and radio assembling and soaps and detergents. The growth in new sectors is reflective of a structural change taking place in the SME sector from traditional to relatively modern product categories, perhaps with higher capitalization and use of better production techniques. Summarizing the findings of various major studies the SEDF lists the following important positive changes taking place in the situation of the SMEs in Bangladesh: SMEs have diversified their activities, entry and exit into the sector has become easier, the RMG industry has contributed significantly to SME development by providing them with orders for accessories and packaging materials, the development of the footwear industry has increased subcontracts to SMEs, small-scale entrepreneurship has grown significantly in agro-processing in general and in poultry in particular.

Factors Affecting Business Success in SMEs

There is considerable variation in the criteria for success used in previous studies. Empirical studies of factors affecting SME success can be roughly divided into two groups according to whether they focus on a quite limited set of variables or try to capture more holistic profiles of successful SMEs. Previous empirical research has used both surveys and case studies. There are also some compilations of the results of previous studies of the factors contributing to firm success. For instance, Storey (2000) has compiled the results of previous studies focused on the birth, growth and death of small firms, on the basis of which he presents some normative “dos and don’ts” lessons for small firms.

The following recent studies based on surveys have dealt with the factors affecting SME success. Nurul Indarti and Marja Langenberg (2005) identified key components to be important in analyzing the business success of SMEs which includes the characteristics of the entrepreneurs; the characteristics of the SMEs; and the contextual elements of SME development. Westhead (1995) studied factors influencing the survival of 227 high-technology small firms. Ghosh and Kwan (1996) made a cross national intersectoral study of the key success factors of 152 SMEs in Singapore and 164 SMEs in Australia. Kauranen (1996) carried out a follow-up study of 37 new manufacturing firms in Finland and studied the determinants of the future success of the firm in the short term and in the long term. Yusuf (1995) explored critical success factors for small firms in several industry sectors based on the perceptions of 220 South Pacific entrepreneurs. Wijewardena and Cooray (1996) explored the importance of a set of success factors by studying a sample of 300 small manufacturing firms in Japan. Gadenne (1998) investigated the effect of various management practices on small firm performance by studying 369 small businesses in the retail, service, and manufacturing industry in Australia. Bracker and Pearson (1986) studied planning and financial performance of small mature firms in the dry cleaning business. Baker et al. (1993) studied planning in successful high-growth small firms. Pelham (2000) explored the relationship between market orientation and the performance of manufacturing SMEs in eight industry sectors.

Based on the findings of earlier research, the factors affecting SME business success were classified into the following categories: (1) an entrepreneur Characteristics (Kristiansen, Furuholt, & Wahid, 2003; and Rutherford & Oswald, 2000), (2) characteristic of SME (Kristiansen, Furuholt, & Wahid; 2003), (3) management and know-how (Swierczek & Ha, 2003), (4) products and services (Wiklund 1998; and Hitt & Ireland 2000). (5) customers and markets (William, James, & Susan; 2005), (6) the way of doing business and cooperation (Hitt & Ireland 2000; and Jarillo 1988). (7) resources and finance (Swierczek & Ha, 2003; and Kristiansen, Furuholt & Wahid, 2003). (8) strategy (McMahon, 2001), (9) external environment (Huggins, 2000; and Nurul Indarti & Marja Langenberg, 2005); and (10) internet (Henriette Hesselmann, Comcare, and Peter Bangs; 2002). However only 6 factors namely Characteristics of SMEs, Management and know-how, Products and Services, The Way of Doing Business and Cooperation, Resources and Finance and External Environment were considered for the theoretical framework of this study based on suitability with Bangladeshi context. Therefore, Business success is the dependent variable and independent variables are: characteristic of

entrepreneur and SMEs, management and know-how, products and services, the way of doing business and cooperation, resources and finance, and external environment.

Research Hypotheses

The study intended to see the relationship between entrepreneur characteristics, characteristic of SMEs, management and know-how, products and services, the way of doing business and cooperation, resources and finance, strategy, and external environment towards business success.

From the above theoretical framework, the following hypotheses were derived:

H1 There is a relationship between SMEs characteristics and business success in SMEs.

H2 There is a relationship between management & know-how and business success in SMEs.

H3 There is a relationship between products & services and business success in SMEs.

H4 There is a relationship between the way of doing business & Cooperation and business success in SMEs.

H5 There is a relationship between resources & finance and business success in SMEs.

H6 There is a relationship between external environment and business success in SMEs.

Research Approach

A sample of 300 employees from SMEs located in the Dhaka, Narayanganj, Khulna and Chittagong were chosen for the purpose of this study. This geographical area has been chosen as they represent a large number of SMEs in Bangladesh. The population frame was drawn from the list obtained from the Bangladesh Small and Cottage Industries Corporation (BSCIC). Data collection was accomplished by mail and personal delivery. The sampled companies were contacted in advance by telephone. The population of the study consisted of front-line employees and middle management levels of SMEs in those areas mentioned earlier. A self-designed questionnaire was used to gather the research data. The questionnaire consisted of three parts. The first part comprised of demographic, characteristic, and profile information of the respondents. The respondents were asked to rank statements on contextual condition related to each success factor faced by the respondents in the second part. This part consisted of 45 questions which were intended to measure factors of business success, using 5-point likert scale anchored by strongly agree to strongly disagree. The factors were characteristic of SMEs, management and know-how, products and services, the way of doing business and cooperation, resources and finance, strategy, management know how; and external environment. In the third part, the respondents were asked to score the importance of perceived of business success. Five-point likert scale anchored by strongly agree and strongly disagree were applied to measure the perceived success. A total 300 sets of questionnaires were distributed among managers of SMEs, only 92 participants were responded.

Survey Results

A total 300 sets of questionnaires were distributed to selected respondents, only 92 questionnaires were collected back; the response rate is 30.46% (i.e. 92/302). However only 89 questionnaires were used for analysis, three questionnaires was rejected due to the respondents were not from the management level.

Descriptive analysis shows that out of 89 respondents, there were more male than female respondents. The results show that 82% of the respondents are male and the remaining 18% are female. The majority of respondents, a total of 44 (49.4%) were aged between 31 to 40 years old, 23.6% each (21 each) were aged between 21 to 30 and 41 to 50 years old, 3.4% (3) were above 50 years old, and 0% of respondents were from age less than 20 years old. There are zero respondent from Primary School, 5 (5.6%) were from Secondary School, 20 (22.5%) were from Certificate/Diploma, 40 (44.9%) were from Bachelor's Degree, 24 (27%) were from Master's Degree, and no respondent from PhD/DBA. Two respondents having working experience less than 2 years (2.2%), 10 (11.2%) respondents between 2 to 5 years, 29 (32.6%) respondents were between 6 to 10 years, 33 (37.1%) respondents were between 10 to 20 years, and 15 (16.9%) respondents were more than 20 years. On the other hand for the Duration of Organization Operated, 18 (20.2%) were less than 5 years, 21 (23.6%) were between 5 to 10 years, 17 (19.1%) were between 10 to 15 years, 7 (7.9%) were between 15 to 20 years, and 26 (29.2%) were more than 20 years.

Reliability analysis was used to measure both consistency and internal stability of data. The Cronbach's Alpha measuring the inter-item consistency and reliability measure the coefficient that reflects how well items in a set are positively correlated to one another. Cronbach's Alpha that are less than 0.6 are generally considered to be poor, those in the 0.7 range to be acceptable, and those over 0.8 to be good; the closer the reliability coefficient gets to 1.0, the better. Cronbach's Alpha for six independent variables and the dependent variable were above .70. Therefore data that were collected for this research were considered to be internally stable and consistent.

4.1 Factors Affecting Business Success of SMEs

Multiple Regression Analysis was used to determine whether the six independent variables, which are SMEs characteristic, management and know-how, products and services, the way of doing business and cooperation, resources and finance, management know how; and external environment, have any significant effect toward Business Success of SMEs in Bangladesh. The results are shown in Table 2.

The findings of the study revealed that products and Services, management know-how, the way of doing Business & Cooperation, and External Environment have significant positive effect on the Business Success of SMEs in Bangladesh. Characteristics of SMEs, and, resources and finance were found to have no significant effect on the Business Success of SMEs in Bangladesh.

Factors	Beta	T-Ratio	Sig. t
SMEs Characteristic	0.046	0.312	0.756
Management and Know-How	0.218	1.561	0.048
Products and Services	0.265	1.955	0.033
The Way of doing Business & Cooperation	0.227	1.630	0.039
Resources and Finance	0.051	0.559	0.578

External Environment	0.288	2.265	0.019
R square = 0.523 Durbin-Watson = 1.545 F = 15.561 Sig. F = 0.000 Condition Index = 41.042			

Table 2: Results of Regression Analysis on the Business Success of SMEs

The overall results of the regression analysis shows that this model is well constructed and it is well represented as reflected in the variables selected. Table 2, the summary table on regression analysis indicated that the R-square is 52.3 percent. This means that the seven variables which include SMEs characteristic, management and know-how, products and services, the way of doing business and cooperation, resources and finance, and external environment can explain 52.3 percent variations in the business success of SMEs in Bangladesh.

The Durbin-Watson statistic shows that the serial correlation of residuals is 1.545, the value falls within the acceptance range (1.5 to 2.5). This means that there is no auto correlation problem in the data. The Condition Index, Variance Inflation Factors (VIF) and tolerance all fall within the acceptance range (Condition index = 30.083, VIF = 1 - 10, tolerance = 0.1 – 1.0). This means that there is no multi-collinearity problem in the regression model used for this study. The histogram indicates that data used in this study is normally distributed and F-value is found to be significant at 1% significance level (sig. F = .000). This concludes that the regression model used in this study is adequate or in other words, the model was fit.

Effect of Demographic Factors toward Business Success of SMEs

One-Way ANOVA was used to find out whether age, education level, working experience and duration of organization operated have any significant effect on business success in SMEs. This technique examined the variability of the observation within each group as well as the availability between the group means. Therefore, it was conducted to find out whether the various groups are different in respect of business success. The results of the analysis show that only one of the demographic factors which is duration of organization operated has significant effect toward business success of SMEs. Duncan statistics shows that SMEs that are operated longer period have been more successful in compare to those have been in operation in a shorter period. In addition to this independent sample t-test was used find out whether gender plays any significant role in business success and found out that gender does play any role in Business Success of SMEs in Bangladesh.

Discussion

The purpose of this study was to identify the factors affecting the business success in small and medium sized enterprises in Bangladesh. A major implication for the findings is that these findings will able to give better understanding for entrepreneurs and business owners in addressing the factors which will significantly affect the business success in SME. The study of the factors affecting business success of SMEs is critical in understanding the business continuity

and growth hence help supporting economics development within a country. The results of this study can also be used as reference for anyone who is interested to start their own business which will provide insights into decision making in starting a business and also for any companies which are interested to continue to sustain and grow.

To achieve business success, many factors should be optimal simultaneously, since SMEs success is a multidimensional phenomenon. Both firm-internal and firm-external factors affect firm success. Entrepreneurs in successful SMEs and those in failed SMEs thought that pretty much the same factors are the most important for business success, and held the same views on the factors to be avoided in business. The research has looked into characteristic of SMEs, management and know-how, products and services, the way of doing business and cooperation, resources and finance, and external environment.

The results show that product and services played an important role in ensuring the SMEs business success in Bangladesh. Innovative product, quality, cost, reliability, and services are the key strategic dimension in business success. Innovative product gives added value to the customer and it is important to achieve a suitable balance between product quality and costs. Small-business owners must have a missionary zeal about their products or services, be willing to be personally involved in it, be willing to stick with the business, be able to define the market clearly and pay attention to details and proactiveness. Beside that, companies must compete based on their strength and specialization which is classified as cost leadership, differentiation, and focused Michael Porter (1985). Cost leadership-based companies have tight controls on their operational costs, have efficient production, are volume producers or focused on tonnage. Differentiation described companies which offer differences in their product or services. They tend to put brands as a market capture, have high service levels, unique distribution and non-standard terms of business. Lastly, focused companies are companies concentrating on a particular buyer, group, geographic area or segment of the product line, continual improvement in quality, cost, delivery lead time, customer service and flexibility are part of the package to become world class. Innovators with continuous growth should pay special attention to their research and development, and the ability to maintain their innovativeness.

External environment factor play a very important role as well for firm success. Social network, government support, and legality, are the key strategic dimension in external environment in business success. Networks represent a means for entrepreneurs to reduce risks and transaction costs and also to improve access to business ideas, knowledge and capital. A social network consists of a series of formal and informal ties between the central actor and other actors in a circle of acquaintances and represents channels through which entrepreneurs get access to the necessary resources for business start-up, growth and success (Kristiansen, 2003). In developing areas, satisfactory government support has been shown to be important for small firm success (Yusuf 1995). In many cases, dealing with legal aspects has forced the SMEs to allocate significant amount of financial resources due to bribery practices. Legal aspect is often also used in selection operating decision in order to ensure future business success (Mazzarol & Choo, 2003).

Business success is usually the outcome of the way of doing business and cooperation. Interfirm cooperation, consultation, performance measurement, and flexibility may play an important role

in business success. Inter-firm cooperation contributes positively to gaining organizational legitimacy and to developing a desirable marketplace reputation. Cooperation also may enable the small firm to improve its strategic position, focus on its core business, enter international markets, reduce transaction costs, learn new skills, and cope positively with rapid technological changes. Successful firms were likely to spend more time communicating with partners, customers, suppliers, employees. Use of outside professionals and advisors, and the advice and information provided by customers and suppliers is also important for business success. Networking seems to be important both between and within firms. The proportion of SMEs led by an entrepreneurial team was high among successful SMEs and low among failed SMEs, so fostering the formation of entrepreneurial teams in starting up businesses is recommended

A huge proportion of successful SMEs are led by men. However, there seems to be no association between the gender of an entrepreneur and SME success. Also, SMEs led by woman are rarely growth seeking. From this point of view, it could be expected that women have underutilized growth potential. On one hand, women should be encouraged to become entrepreneurs, and on the other hand female entrepreneurs should be encouraged to expand their firms. However duration of organization operated has a significant effect on the business success in SMEs; the longer the organization operates the more successful they are.

Conclusion

We attempted to find out the most significant factors that affect the Business Success of SMEs in Bangladesh and found out that product and services, external environment, and management know-how are the most significant determinants of Business Success of SMEs in Bangladesh. Products and Services hypothesis accepted as innovative and high quality of product gives added value to SMEs customer in Bangladesh. Most of the Penang SMEs adopted Porter's Generic Strategies by Michael Porter; they are cost leadership, differentiation, and focused. To ensure Bangladeshi SMEs can continue successful they need to ensure good products and services deliver to customer continuously. External Environment hypothesis accepted as social network help entrepreneurs in Bangladesh to reduce risks and transaction costs, improve access to business ideas, knowledge and capital. Government support is vital to foster SMEs development and legal aspect is used in selection operating decision in order to ensure SMEs future business success. Hence, Bangladeshi SMEs should ensure they have built a strong social network and good government relationship in order to ensure their business success. The Way of doing Business & Cooperation hypothesis accepted as inter-firm cooperation contribute positively to gaining organizational legitimacy and to developing a desirable marketplace reputation, and enable the small firm to improve its strategic position, focus on its core business, enter international markets, reduce transaction costs, learn new skills, and cope positively with rapid technological changes. Besides that, use of outside professionals and advisors should continue to be practiced by Bangladeshi SMEs.

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