

Micro, Cottage and Small Enterprises (MCSEs) for Local Economic Development in Nepal

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Abstract: *There is a structural change in Nepal since 2015. Local government has been given the legislative, executive, and judiciary rights. Agriculture, tourism, industry and commerce, cooperative and financial institutions have been mandated as components of local economic development (LED). Micro, cottage, and small industries (MCSEs) are the foundation of the local economy. It is believed that excess cash inflow over outflow develops the local economy. To do so, how every level of government of Nepal is working for the growth of MCSEs is an interesting subject of study in the current situation of Nepal. To know the actual scenario of MCSEs in the locality, this study was carried out. Both qualitative and quantitative methods were adopted. Primary and secondary data collection methods were applied. This study followed the deductive approach to explore the status of policies into practice.*

Keywords: Local Economic Development, Local Economy, Enterprises, Cash inflow and outflow

1. Introduction

Local economic development is the integration of the public sector, business, and civil society to work together [1]. Micro, cottage, and small industries (MCSEs) are the foundation of the local economy. The local economy is observed as the pillars of the national economic development because MCSEs have contributed 22% in GDP and about 1.7 million employment generation in Nepal [2]. MCSEs make social innovation possible for the sustainable development of the national economy [3]. [4] expresses that the MCSEs lead to cultural developments that lead to societal change through the involvement of women into equality with the man rather than the subordination role. Section 15 of [5] in Nepal has defined the MCSEs based on fixed capital. Furthermore, [5] categorizes that an enterprise of fixed assets equal to NPR 500 thousand except land and building is a micro-enterprise. [6] adds the data that 80% of industries have been registered in the Department of Cottage and Small Industries (DoCSI) with fixed capital ranging from NPR 300,000 to NPR 600,000 in the category of MCSEs.

Industries in Nepal are located in diversified geography. The largescale industries are located in urban areas whereas MCSEs are located in rural areas [7]. MCSEs which are small and labor-intensive, employ rural poor people. [8] noted that they are the source of earning money which goes from person to person, business to business, creating local employment and wealth. To multiply the money within the local economy, the flowing out of money should be stopped or lessened. [9] suggested that the local economy can be raised after stirring up the contents of the economy in motion. According to him, the speed of stirring up determines the level of the growth of the local economy.

The lack of funding, weak management, lack of updated technology, lacking support from an authority, and lack of

marketing ability result in MCSEs closing business in a short period [10]. The government announced various programs like educated youth self-employment, women entrepreneurship, and agriculture and livestock loan to support for starting MCSE through the budget of the fiscal year (FY) 2018/19 [11]. Under this program, Nepali youth not exceeded 25 years of age completed the secondary level education can apply for the loan up to NPR 500,000 at the interest rate not exceeding 2% against original academic certificates as collateral. Central Bank of Nepal (Nepal Rastra Bank) extended the loan limits from NPR 1 million to NPR 1.5 million to group members or individuals residing in rural municipalities for running MCSE against the acceptable collateral at the rate of 3% [12].

[13] suggests that a developing country has to pay greater attention to MCSEs to grow and develop the economy. But the development of economies is driven by the investment capital generated from external and internal capital [14]. Local government (LG) of Nepal has been made responsible for the allocation of the budget for local economic development (LED) in agriculture, tourism, industry and commerce, cooperatives, and the financial sector for the development of MCSEs in their region [15]. Government of Nepal (GoN) has come-up with many MCSEs friendly policies at accessing a subsidized loan, tax rebate, and subsidy in input, etc. to develop the local economy. Unfortunately, the owner of many MCSEs and the public are unaware of these provisions and facilities [2]. Because of a lack of collateral, inability to prepare a business plan, proper record management, and red-tapism, MCSEs are unable to raise the capital [16]. There are so many micro and cottage enterprises setup and being operated without registration. As a result, MCSEs are not fully accounted and their contribution to LED cannot be measured. Therefore, this study aims to explore the strategic support to MCSEs by LG in practice so that it can measure the present and future scenarios of MCSE in Nepal.

1.1. Objectives of the Study

The objective of this study is to explore the contribution of MCSEs LED in the local region concerning the. This study aims to find out how LG and MCSEs both can improve their actions to be better in Nepal.

1.2. Significance of the Study

This study is important to the local, regional, and central level government to formulate the strategy of LED knowing the role of MCSEs in the development process. As [17], expresses that MCSEs contribute positively to local capital formation i.e. they increase total investment by 66% and non-capital by 50%. They further add that growth MCSEs increases more employment than large industries. This study is significant to suggest the government to set up the mechanism to make MCSEs effective and profitable for LED.

1.3. Literature Review

1.3.1. Access to Finance

Financial support is indeed the most important factor for successful economic empowerment to carry out any activity in MCSEs [18]. Commercial banks don't show a willingness to lend MCSEs because lending to them is thought of as risky [19]. The survey report of [2], out of surveyed MCSEs, 33% use the fund from the ancestral property, 26% from own savings, 16% from the loan from the bank and financial institutions (BFIs), 8% from informal lending, 7% from remittances, 6% from the loan from cooperatives and 0.5% from venture capital for a business startup in Nepal. According to [20], out of all surveyed micro finances, 32.9% was financed through own savings, 58.7% through a loan from the formal sector, 6.5% from borrowing from the informal sector, and 1.9% from grant money have managed to finance. [21] identifies the constraint of access to finance as a key operational difficulty of 45-55% of MCSEs in developing economies.

1.3.2. Establishment and growth of MCSEs

It is difficult to assess the present status of MCSEs and to measure their contribution to the national economy. MEDEP/MEDPA run by GoN and UNDP has created 119,085 micro-entrepreneurs and employment opportunities to 187,358 directly and 172,425 indirectly as of June 2017 all over the country [22]. GoN and UNPD claimed that this program has moved out of poverty to 525,200 people and it has raised per capita income (PCI) from NPR 17,605 to NPR 78,133 as of June 2017 in Nepal. According to [2], the number of registered small industries in DoCSI and Cottage and Small Industries Development Committee is 268,934 in FY 2017/18. Except for this record, there are several micro and cottage industries that cannot be tracked in government statistics, have been run informally without registration [23]. [24] pointed out four major constraints which affect MCSEs (SMEs) growth in Nepal i.e. (a) macro-economic constraint such as interest rates, trade, and tariff, taxation, inflation, exchange rate; (b) legal, regulatory constraints

like registration and licensing, bankruptcy/exit policy, labor law, environmental law, patent protection; (c) infrastructure constraints such as land use and management, energy, water, transportation, cold storage; (d) business service constraints such as finance, research, innovation and development, capacity building, market access, etc.

[17] have concluded that monthly sale and enterprise life is positively related to employment level. Job creation at an average of 4.75 employees per micro-enterprise has been found in Timergara City. They have added that MCSEs are the most contributory to reducing unemployment and generating income.

1.3.3. Methodological Review

[25] studied the status of micro and small enterprises in Nepal based on discourse analysis. The study of access to formal sources of finance for MCSEs in Karnataka State of India by [26] has adopted a mixed research approach i.e. qualitative and quantitative method. Also, [27] has used a mixed research approach to study women entrepreneur perception towards BFIs in getting access to the bank loan.

2. Data and Methods

This research has been carried out on the interpretivism philosophical approach. The deductive approach has been adopted to test whether government policies and others have been supportive of MCSEs in practices or not. This study is based on the exploratory method. Both qualitative and quantitative method has been adopted in the research collecting the data using both primary and secondary sources. This study investigates the support from the LG and central government to MCSEs to run. A case study of the status of MCSEs in Chaudandigadhi Municipality has been carried out. Primary data were collected using a questionnaire and interviews. In Chaudandigadhi Municipality, 3 municipal authorities, 12 political activists, and 165 MCSEs owners, 180 persons in total were interviewed through mobile communication and direct contact. The data were collected from the snowball sampling method. Secondary data were collected from the analysis of the documents. The collected data were processed and analyzed using simple statistical tools.

2.1 Characteristics of respondents

RPEs in the study were as given in Table 1 below.

Table 1: Characteristics of respondents

Characteristic	Category	Frequency	Percentage
Age	15-24	6	4%
	25-34	44	27%
	35-44	43	26%
	45-54	61	37%
	above 55	11	7%
	Total	165	100%
Income Per Month (In thousand)	Below 100	66	40%
	100-250	39	24%
	250-400	23	14%

	400-550	26	16%
	550 above	11	7%
	Total	165	100%
Employees	Male	528	79%
	Female	141	21%
	Total	669	100%
Pay range (In thousand)	Below 5	302	45%
	5-15	192	29%
	15-30	111	17%
	Above 30	64	10%
	Total	669	100%
Source of capital for setup and operation	Own fund	103	62%
	Family finance	13	8%
	Informal lending	39	24%
	Loan from BFLs	3	2%
	Loan from financial cooperative	2	1%
	Both self & bank loan	5	3%
	Loan from other institution	0	0%
	Total	165	100%
Enterprise	Medical stores	15	9%
	Sweets stores	8	5%
	Electrical appliances stores	11	7%
	Books and stationery stores	7	4%
	Agriculture	34	21%
	Fancy shop	24	15%
	General stores	57	35%
	Meat shop	9	5%
	Total	165	100%

Source: Field Survey

3. Results and Discussions

3.1. Brief Description of Chaudandigadhi Municipality

Chaudandigadhi Municipality, located in the mid-eastern region of Nepal, constituency number 1 of Udayapur District of Province No. 1 was formed after the merger of Beltar Basaha Municipality, Chaudandi, Siddhipur, Hadiya and Sundarpur Village Development Committees on 10 March 2017. There are 10 wards in the municipality. The population of the municipality is 48,574 and 10,519 households according to [28]. The population growth rate is 7.89%. The gender ratio (male/female) is 83%. The population density per square kilometer is 171 persons. The total area of Chaudandigadhi Municipality is 283.78 sq km, plain land surrounded from latitude 26° 41' 26" N- 26° 54' 27" and longitude 86° 46' 07" E- 86° 59' 32". The altitude of this municipality from sea level is 78m lowest elevation to 1051m highest elevation.

3.2. Local Economic Development (LED)

According to [15], agriculture, tourism, industry and commerce, and cooperative and financial institutions are components of the local economic development sector. LED in the municipality is given in

Annex 1 and

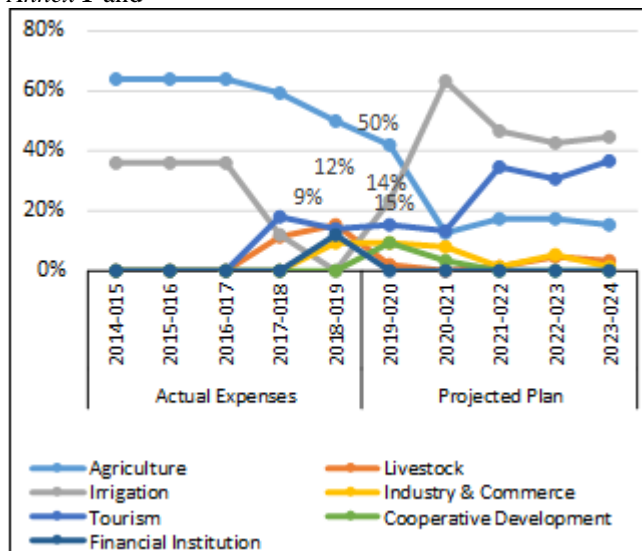


Figure 1. [29] has explained the status of the municipality as follows. The maximum proportion of budget allocation for LED is 11% by the municipality. The maximum amount allocated is NPR 29,761 thousand. In FY 2014, the priority was given to the agriculture sector and this sector was gradually declined and irrigation was emphasized. Then, the tourism sector was emphasized.

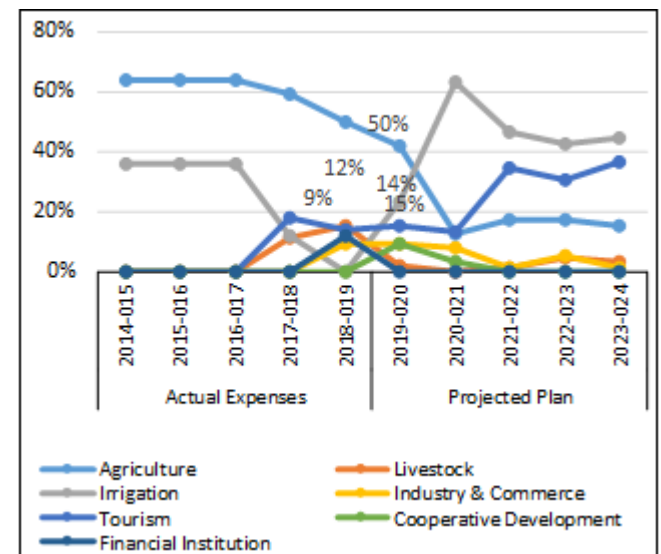


Figure 1: Weightage of the budget in different components of LED

Source: Chaudandigadhi Municipality Record 2019

3.2.1. Agriculture. 3,324 (16.28%) hector land is cultivatable, 14,010 (68.84%) hector is covered by forest and 3,078 (15.08%) hector is covered by cliff and rivers. Agriculture Service Center has been established to facilitate the farmer. According to [30], the different areas can be developed as a pocket area of different products such as food grain, oil, seed, vegetables, fruits, coffee, ginger, turmeric, and fish. There are 199 farmers' groups in the municipality. The existing fund of the group ranges from minimum NPR 0 to maximum NPR 198,000. The people in the municipality depend on agriculture for their livelihoods.

Soil is full of clay and sand. Paddy, maize, millet, wheat, and barley in the southern part and orange, cardamom, ginger, and other fruits can be produced in the northern part of the municipality. But agriculture has not been industrialized. The private sector is making livestock farming business-oriented. According to the municipality record, livestock businessmen have earned about 507 million rupees in FY 2017/18. According to the Udayapur Agriculture Development Office, in FY 2017/18, the income from agricultural products like paddy, wheat, vegetables, oil, ginger, turmeric, and potato, etc. was 585.6 million rupees. 40% to 50% of total households earned NPR 72.2 million [29]. The municipality has lessened the budget in this sector.

3.2.2. Livestock. People in the municipality have been attracted to the major source of income from livestock. The Local Level Detailed Report (2017) of Udayapur district describes that every household owns 5-7 four-footed big animals and 20 small animals and birds on average [30]. Most of the households have local animals and birds. The cow 56,511 local and 3,098 hybrids, buffalo 13,302 local and 5,835 hybrids, goat 65,392 local and 30,175 hybrids, pig 10,049 local and 3,468 hybrids, and chicken 21,946 local and 79,092 hybrids have been domesticated for business in the municipality.

3.2.3. Irrigation. There are 20 rivers which are the source of irrigation and drinking water. Except for these rivers, there are many small rivers too. There 8 evergreen ponds in the municipality. The municipality is running 12 projects to improve the canal and irrigation. There are 16 major sources of irrigation. The 495.5 hector land is irrigable according to the agriculture statistics update in 2015.

3.2.4. Industry and commerce. There are production-oriented and service-oriented industries in the municipality. Production oriented industries involve in the production of furniture, grill, tobacco, agriculture, ice-cream, boutique, and noodles. Service-oriented industries involve grinding grains, computer teaching, stitching, hotel, beauty parlor, communication, mobile repairing, motorcycle repairing, and construction, etc. There are 5 cottages, 18 small, and 1 medium industry. The main trade centers of the municipality are Beltar Bazaar, Ranitar, Chhuila, Birendra Bazar, Hadiya, Shivai Chowk, Sundarpur, and Belha. There are not any star hotels but 49 ordinary hotels.

3.2.5. Tourism. The tourism sector is not good in the municipality. The municipality lacks drinking water, hotel and lodges, transportation, marketing, and means of entertainment. However, cultural, religious, natural, and historical places in the municipality can be developed as tourism places. The municipality has planned to develop 8 highly potential tourism places.

3.2.6. Cooperative Development. There are 10 cooperative organizations. These cooperative organizations serve people as support to people to advance loans.

3.2.7. Financial Institution. There are 2 commercial banks, 1 agriculture development bank, 3 development banks and 1 finance company to support people for financial services.

3.2.8. Foreign employment. According to [31], 3521 individuals have received the passport. As per [30], about 3,434 individuals have gone abroad for foreign employment from the municipality from 2014 to 2016.

3.2.9. Women development. Till July 2017, municipality traced 314 groups, 47 committees, 2022 members [29]. 197 Dalits, 1,180 Janajatis (Indigenous), and the remaining other people have membered among total members of the groups. The total saving of all groups is NPR 4,118,415 and share capital is NPR 1,752,974. Women and children's office has provided NPR 260,000 to 80 members for pig, goat, and vegetable farming. Movement of women against poverty program has provided skill development training to 360 women of Siddipur and provided NPR 1,462,000 as an aid through Uchcha Jyoti Women Saving and Credit Cooperative Society.

3.3. Selected Micro, Cottage, Small Enterprises (MCSEs) in the Municipality

3.3.1. Registration status of MCSEs

The legal registration status of respondent MCSEs was reviewed as follows in Table 2.

Table 2: Registration status of respondent MCSEs

Category	Frequency	Percentage
Registered	23	14%
Unregistered	142	86%
Under registration process	0	0%
Total	165	100%

Source: Interview, 2020

Out of all respondent MCSEs, 86% are not registered and 14% have been registered in tax office and office of the municipality or DoCSI.

3.3.2. Social and Cultural Benefits

Out of all research participant enterprises (RPEs), 89% was found the family member not involved in the business. The response of all RPEs for question-related to give the reason how their business is beneficial to society was as follows in Figure 2.

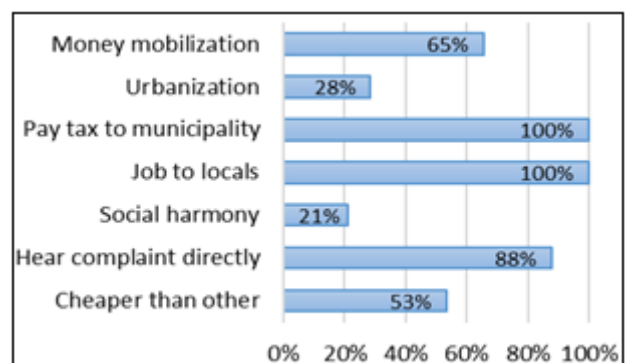


Figure 2: How does the enterprise support to society?
Source: Interview, 2020

All RPEs expressed the above-mentioned benefits to society. All mentioned that business in the municipality is the source of income and employment to the locals. 88% of RPEs mentioned that local enterprises can address the complaint of the client directly. 53% of the RPEs claimed that local product is cheaper than the imported product. 65% of RPEs pointed out the cash flow support to the market. 28% and 21% of total RPEs told that local enterprises are beneficial for developing urbanization and social harmony respectively.

3.4. Use of Profit

Out of all RPEs, 90% uses the profit in the productive channel. It means they use it in another business or adds investment in the existing business.

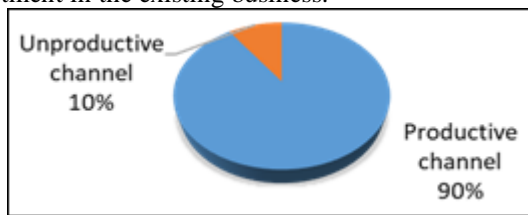


Figure 3: Use of profit
Source: Interview, 2020

3.5. Policy/Regulatory Environment

3.5.1. Clarity about the rules and regulations related to RPEs business

Section 3.2 of [32] group members of the guarantors' group can receive the loan against group guarantee or acceptable collateral from Microfinance Financial Institutions (MFIs). Agriculture and livestock business loan, educated youth self-employment loan, loan to the youth returned from foreign employment, women entrepreneurship loan, deprived community business development loan, high technology, and business education loan, private building construction loan to earthquake affected people are soft loan categorized according to clause 10 of [33]. Loan holder's business, loan document, and group guarantee document are loan security for women entrepreneurship development loan, agriculture, and livestock loan, and deprived sector loan according to the soft loan procedure. This soft loan procedure has provisioned the subsidy of 5% on the interest in the loan interest rate of BFIs to all loan holders except women entrepreneurs. Subsidy of 6% in the interest rate of the loan to women entrepreneurs should be provided. [34] provisioned special facility to women entrepreneur loan for the promotion, development, and diversification of women entrepreneurship. According to sub-section 9.6 of [35], the concept of one village one product will be explored identifying the most potential resources and means at the local level. In sub-section 11.4, the policy further adds that financial access will be provided to MCSEs through funding arrangements by creating different funds. Regarding the rules and regulations of GoN, 59% of RPEs are aware and clear, 33% have no clarity and 8% are

somehow clear. However, 86% of RPEs are the unregistered and informal economy.

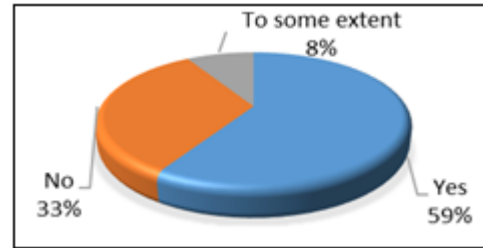


Figure 4: Clarity of rules and regulations of the government
Source: Interview2020

3.5.2. Perception of the RPEs regarding regulatory support from the government in running a business

Out of all RPEs, 87% of RPEs claim that the government has not supported to MCSEs. But 12% of them, agree for government support to some extent. Only 1% of RPEs agree that the government works for the support of MCSEs.

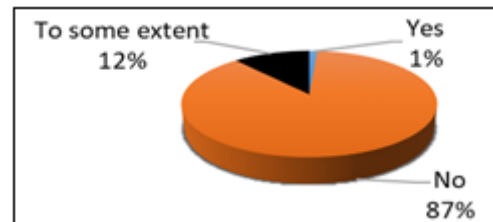


Figure 5: Perception of entrepreneurs regarding regulatory support from the government
Source: Interview, 2020

3.5.3. Expected support from the government to MCSEs

The expectation of the RPEs businessman from the municipality has been given in Figure 6. The research demonstrated that 100% of RPEs want price control for a healthy business environment. Out of all RPEs, 90% and 97% expected local tax minimization and improvement of social security respectively. 75% of RPEs expect support from financial institutions formally to fulfill the requirement for the growth. 62% of RPEs expect training and awareness and the role of LG to facilitate marketing linkages. The warehousing facility has been expected by 58% of RPEs. 39% of RPEs desire to monitor the quality of selling products. 21% of RPEs, agricultural entrepreneurs expect the availability of fertilizers and seeds easily and timely.

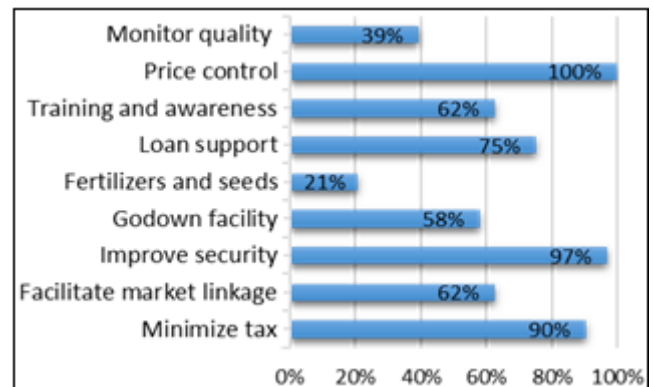
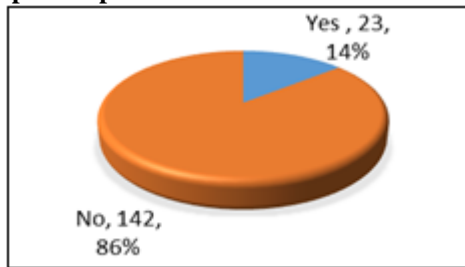
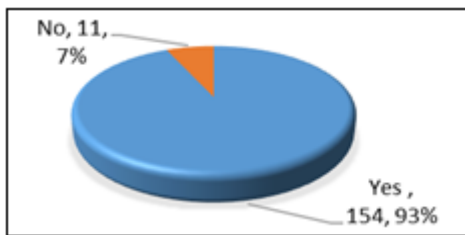


Figure 6: The expectation of support from LG

Source: Interview, 2020

3.5.4. Export-import related information**Figure 7:** Export of the goods

Source: Interview, 2020

**Figure 8:** Import of goods and materials

Source: Interview, 2020

Out of total RPEs, 14% of RPEs export the product to the outside of the municipality for sales, and the remaining 86% is consumed within the municipality. Similarly, 93% of RPEs import goods from outside, and 7% of RPEs produces the goods from the internal resources and sale in the market. The estimated average import per enterprise per year is NPR 1,750,000/- and estimated average export per enterprise per year in NPR 750,000/-. The estimated total import per year of total RPEs is NPR 17,250,000/- and total export is NPR 269,500,000/-. It means the estimated inflow is 15 times less than the outflow of the money in the municipality.

3.6. Strengths/weaknesses of MCSEs in carrying out the business activities

Experts, municipal authorities, political leaders, and academicians opine that cheap labor, cheap local material, production of the locally preferable product, and direct relationship with the client are strengths of MCSEs in the municipality. Furthermore, they opine that unavailability of resources (skilled labor and material), old technology, support from the government, lack of know-how, lack of market, and high competition with the global production are weaknesses of MCSEs of the municipality. Their opinion demonstrates that MCSIs have greater challenges to existing sustainably.

3.7. Strategies/interventions required to overcome the weaknesses

The municipality has not been able to update the statistics of enterprises in the municipality. Many producers and traders have not been registered in the municipality.

However, the municipality has begun updating the status of all enterprises in the municipality. After the up-to-date statistics of the enterprises, a strategic plan for the development of MCSEs will be developed. Although the government has not been able to support to MCSEs adequately, experts, municipal authorities, and political leaders have suggested some strategies to be adopted by LGs such as setting vision, mission, and objective to develop MCSEs; motivate to entrepreneur to improve as per vision; searching for the competitive advantage of the municipal area; teaching, training and supporting to entrepreneur; developing network, market mechanism and core values of the locality.

4. Conclusion

LED is a less prioritized sector in Chaudandigadhi Municipality. LED processes make the local economy more inclusive and LG can reach the poor and marginalized people by setting up enterprises and stakeholders collectively [36]. The locally established enterprises are beneficial to society for the cheaper product than an imported one, hearing complaints directly, creating social harmony, providing jobs to locals, increasing municipality revenue, growing urbanization, and money mobilization. When local enterprises carry out businesses, they have to increase the inflow of money more than the outflow of money to develop the economy. The research concluded that a large number of enterprises have been excluded from the formal economy in local level government. This exclusion proves that LG has loosened the formal employment and income opportunities. The local, provincial, and central government are suggested to set mechanism for the formalization of unregistered and informally operated enterprises which are unregulated. The government has to develop a support system to address their expectations like minimizing tax, facilitating market linkage, improving security, warehousing facility, providing fertilizers and seeds, loan support, training, and awareness, controlling price, monitoring quality, etc. Due to informal status and lacking exact statistics of enterprises, the LG is hindered to support local enterprises by policy management, legal framework, value addition, technology development, capital formation, market management, and product development. The study found out that MCSEs have more weaknesses than strengths. The municipality has to carefully develop the strategic plan to strengthen all components of local economic development to overcome weaknesses. The strategy has to search for the competitive advantage of the municipality.

Since this study has been carried out only in the case of Chaudandigadhi Municipality, the findings and suggestions may not be suitable for all local governments in Nepal. But I believe that this study may be fruitful to the provincial and central government for the formulation of local economic development strategy.

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Author Profile

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Annex 1: Expenditure and projected plan of the municipality in LED

(In thousand)

Components of Local Economic Development	Actual Expenses					Projected Plan				
	2014-015	2015-016	2016-017	2017-018	2018-019	2019-020	2020-021	2021-022	2022-023	2023-024
Agriculture	1,657	1,996	2,496	17,537	10,630	12,058	1,150	1,640	1,350	1,650
Livestock	-	-	-	3,402	3,280	500	-	100	350	350
Irrigation	935	1,127	1,409	3,455		6,665	5,961	4,430	3,380	4,795
Industry & Commerce	-	-	-	-	2,000	2,700	750	100	415	100
Tourism	-	-	-	5,367	3,000	4,500	1,250	3,270	2,400	3,920
Cooperative Development	-	-	-	-		2,600	300	-	-	-
Financial Institution	-	-	-	-	2,500	-	-	-	-	-
Total LED Expenses	2,592	3,123	3,904	29,761	21,410	29,023	9,411	9,540	7,895	10,815
Increase/Decrease Percentage		20%	25%	662%	-28%	36%	-68%	1%	-17%	37%
Percentage of LED out of total budget	3%	3%	3%	10%	11%	10%	10%	9%	8%	11%

Source: Chaudandigadhi Municipality Record 2019