

Economic Freedom Matters

Does Economic Freedom Affect Kirana Pasals in Nepal?

Samriddhi, The Prosperity Foundation

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SEP, 2013

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Published by

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First edition: November 2013

PREFACE

With a belief that political, civic and economic freedom paves way to prosperity, Samriddhi, The Prosperity Foundation has been working on entrepreneurship development, improving business environment, economic policy reform and promoting democratic values for over five years now. It has also been releasing the Fraser Institute's Economic Freedom of the World Report in Nepal for the past four years.

The Fraser Institute in Canada and The Heritage Foundation in Washington, DC bring economic freedom to the world's attention every year through their Economic Freedom Indexes. With few differences on the parameters, in both indexes countries that promote trade (both internal and external), free competition and strong legal protection for private property score well. The reports offer governments around the world a chance to analyze their economic policies and directions they have been taking for growth. Nepal has remained on the bottom half of both the indexes since the beginning of its rankings and has also faced the challenges of slow economic growth, poverty and poor quality of life for a big majority of its history.

To find out what economic freedom means to average small entrepreneurs in Nepal and how it impacts their survival and growth, Samriddhi foundation picked one sector of the Nepalese economy which is quite typical to Nepal and a few other South Asian economies. The sector also encompassed some key issues developing economies usually face - slow growth, informality, economies of scale, etc. The sector was *Kirana Pasals* - small mom and pop shops selling groceries and fast moving consumer goods. People who have lived in Nepal long enough have often noticed that these *Kirana Pasals* rarely grow to become medium or large-sized operations, like department stores or supermarkets and that called for this quest to find out what prevented the growth of these independent businesses run by entrepreneurial and hardworking people. In the process, the focus was on finding if economic freedom had a role to play in their growth.

Samriddhi conducted a research, which studied the day-to-day realities of Kirana Pasal owners in a methodical way to find out the barriers preventing growth for these entrepreneurs and the communities they support. This research report offers an insight into a sector, which has hardly been studied before despite its ubiquity and prevalence in the region. It helps us have a better idea on how economic freedom is important, not only to big businesses or international trade but also to people who are involved in rather local and small businesses in a unique economic setting.

Robin Sitoula

Executive Director

Samriddhi, The Prosperity Foundation

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ACKNOWLEDGEMENT

This research report is an outcome of support and solidarity shown by individuals who believe in prosperity for people all around the world. We would like to thank Atlas Economic Research Foundation in Washington, DC and 84 very generous supporters who showed their support for the growth of small entrepreneurs in different corners of Nepal by making a contribution in the crowdfunding campaign. We also deeply appreciate the time and willingness of all the Kirana Pasal owners in the valley who took time to share information about their businesses and their valuable experience and reflections. We are very grateful to the different associations, government bodies and other members who took time to attend the consultation meetings on the topic of the research. Finally, our sincere thank you to all the researchers, enumerators and writers who were very important in making this research possible.

Samriddhi, The Prosperity Foundation

September 2013

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ABBREVIATIONS AND ACRONYMS

ADB	Asian Development Bank
CSID	Cottage and Small Industries Development Board
EU	European Union
FY	Fiscal Year
FIAS	Foreign Investment Advisory Service (of the World Bank and International Finance Corporation)
GDP	Gross Domestic Product
GoN	Government of Nepal
IFC	International Finance Corporation
ILO	International Labour Organization
MoF	Ministry of Finance
MSE	Micro and Small Enterprises
MSME	Micro, Small and Medium Enterprises
NRs.	Nepalese Rupees
OECD	Organisation for Economic Co-operation and Development
PAN	Permanent Account Number
SEDF	South Asia Enterprise Development Facility
UNCTAD	United Nations Conference on Trade and Development
UNIDO	United Nations Industrial Development Organization
UNODC	United Nations Office on Drugs and Crime
VAT	Value Added Tax
IRD	Inland Revenue Department

The Nepali year is based on the Bikram Sambat Calendar and is approximately 57 years ahead of the Gregorian calendar (2062/1/1=2005/4/14)

1 USD = 99.7 NRs. (September 30, 2013)

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PART I

INTRODUCTION

What Are *Kirana Pasals* - The Subject Of Our Study?

*Kirana Pasals*¹ are mom-and-pop stores that sell groceries and other necessary daily goods. Scattered around commercial hubs, serving the locals and the visitors alike with wide variety of goods, they are an integral part of the daily Nepali life. In the urban areas, almost every house facing the street design spaces to rent it out to shops and most of those one or two room spaces in the ground floor turn into *Kirana Pasals*. Even in the rural parts of Nepal, *Kirana Pasals* are important as people rely on them to obtain goods for their families' daily use.

For the purpose of this research, *Kirana Pasals* are defined as micro or small enterprises that sell fast moving consumer goods, have basic infrastructure and use simple technology. The Industrial Enterprise Act (1992) of Nepal characterizes such retail shops under Small Service Industries. Enterprises with fixed asset of value less than or equal to 30 million rupees are designated under Small Industries in this act.

Why Economic Freedom And *Kirana Pasals*?

Large amount of work has been done to demonstrate positive correlations between economic freedom and other important components of wellbeing such as growth, poverty reduction, peace and cooperation, equality, and improvement in human welfare. Annual publications such as the Economic Freedom of the World Report by Fraser Institute and the Index of Economic Freedom by The Heritage Foundation have asserted this in the past years. As a country that has scored dismally in both the indexes ever since the publication of those reports and has remained a slow growth economy, discovering the relationship between these two aspects of Nepal seems indeed intriguing.

This research takes a small step towards that direction and attempts to examine the applicability of the explanation by viewing the growth (or lack of it thereof) of one of the most ubiquitous economic activities in Nepal from the lens of economic

¹ Kirana, a Nepali word means groceries and Pasals, another Nepali word means shops

freedom. It tries to see how the components of economic freedom impact micro or small enterprises in their growth.

The Fraser Institute's Economic Freedom Index looks into five broad areas, namely, Size of Government, Legal System and Property Rights, Sound Money, Freedom to Trade Internationally and Regulations. 24 components within these areas are placed on a scale of 0 to 10 to reflect the distribution of the underlying data for each country. The Heritage Foundation's Index also studies similar aspects under four broad categories, namely, Rule of Law (Property Rights, Freedom from Corruption), Limited Government (Fiscal Freedom, Government Spending), Regulatory Efficiency (Business Freedom, Labor Freedom and Monetary Freedom) and Open Markets (Trade Freedom, Investment Freedom, and Financial Freedom).

Based on the parameters set by these Economic Freedom indices, the purpose of this research is to identify impediments to growth for *Kirana Pasals* and understand what components of economic freedom play a role in the growth of such *Kirana Pasals*.

Methodology

The data used in this research are both primary data and secondary data. Primary data was collected through randomly selected structured questionnaire survey and interviews with stakeholders. Secondary data was collected from relevant published and unpublished sources.

The questionnaire survey was carried out on *Kirana Pasals* within the Kathmandu valley, which constitutes nearly 10 percent of the total population and less than one percent of the total area of the country but contributes almost one-third of the total economic activity (Nepal Rastriya Bank, 2012). *Kirana Pasals* were identified as micro or small enterprises that sold fast moving consumer goods, had basic infrastructure and used simple technology.

Sample

The survey was carried out in 13 different locations within the Kathmandu valley's three districts, which are three of the country's most urban and economically dynamic places. 7 of these areas are in the Kathmandu district, 3 are in Bhaktapur district and 3 are in Lalitpur district. These locations were chosen so as to create a mix of *Kirana Pasals* in commercial hubs, residential areas, agricultural, and industrial areas. The location and the mix were selected in a manner to be representative of all Kirana stores within the valley.

Table 1: Location of Sampled Kirana Pasals

Location	City	Type
Thimi	Bhaktapur	Agricultural
Nagarkot Road	Bhaktapur	Industrial
Siddha Pokhari	Bhaktapur	Agricultural
Chabahil to Bouddha Nath	Kathmandu	Commercial
Maitidevi	Kathmandu	Residential
Narangopal Chowk	Kathmandu	Commercial
Ason Chowk	Kathmandu	Commercial
Kalimati	Kathmandu	Commercial
Shantinagar	Kathmandu	Residential
Naya Bazaar	Kathmandu	Commercial
Pulchowk to Gwarko	Lalitpur	Commercial
Sunakothi	Lalitpur	Agricultural
Imadol	Lalitpur	Residential

Sampling Technique

A two-stage sampling technique was used to select sample respondents. In the first stage different locations were selected purposely to make the variability of samples and to make the sample more representative. Then within each location, list of Kirana stores was made. All Kirana stores in the selected locations were listed in a non-discriminatory manner. A list of 540 stores was created from the 13 locations. In the second stage, 268 stores were selected randomly from the list for the survey by using systematic sampling. Questionnaires were administered using five enumerators in the 13 locations. Data was collected within a week spanning from 14th August to 21st August 2013.

The questionnaire consisted mostly of close-ended multiple-choice questions and a few short answer open-ended questions. After completing questionnaire design, pre-testing was done to check the validity and errors in questionnaire. During the testing phase, 15 questionnaires were filled at random from the selected locations in an interview style.

The questionnaire was divided into five sections to draw out information based on major impediments to growth identified during the literature review. These sections were 'Nature of the Shop', 'Enterprise Operation and Growth', 'Registration', 'Finance', and 'Profit Generation and Distribution'. The questions were aimed at understanding issues of distribution of income and cost between household and enterprise, labour

standards, extortion, bribery and corruption, bandhs (general shutdowns and strikes), competition, support services, regulatory environment, perception of government policies, supply chain constraints, economies of scale, business environment, entrepreneurship, registration and the process of formalization, tax, and access to finance.

On responses regarding questions like tax payment, bribery, income and expenses, the accuracy of the data is questionable due to the reluctance to divulge such information. Furthermore, most of these stores did not practice bookkeeping. We were only able to collect these data in estimated ranges. To minimize the recall error, responses on income and expenses were requested in a monthly format. The data was then extrapolated to calculate annual values.

After completing the data collection, each questionnaire was edited to maintain high quality of data. IBM SPSS 20.0 was used for data entry and analysis.

Simple descriptive analysis is used on the data. The types of analysis predominantly used were frequency/ percentage tables, cross-tabulation, correlations and chi square tests.

Limitations

Some limitations of this research are:

- Sample size restricted to Kathmandu Valley. Other urban areas like Pokhara and Biratnagar not included in the research.
- Our purpose was to identify and explore the impediments to growth for *Kirana Pasals*. There is much room for more detailed analysis in each of the factors and the use of more complex statistical analysis will be able to draw out much richer findings.
- The research has not looked at the demand side constraints to growth for *Kirana Pasals*. This research is primarily focused on the supply side constraints to growth.
- The research has not included all factors of economic freedom. Impact of factors like inflation, political instability, poor rule of law and such have not been explored in this research.

PART II

LITERATURE REVIEW

Definitions

The factors most often taken into consideration when classifying enterprises are labour, turnover, initial investment and the net value of assets. Based on a certain limits set on these factors, enterprises are separated into micro, small, medium and large sized enterprises. There are many ways of defining these enterprises and it is difficult to strictly universalise the definition. Various countries choose to define their MSMEs using one or more criteria. For example, the European Union defines micro, small and medium-sized enterprises based on their employment and turnover or net asset (EU, 2003). Japan classifies its enterprises based on initial investment and employment criteria's (The Government of Japan, 2013). In Nepal, the Industrial Enterprise Act 1992 (amended in 1997) categorizes Micro enterprises as those with fixed asset up to 200,000 rupees, small enterprises as those with fixed asset up to 30 million rupees, and medium enterprises as those with fixed asset between 30-100 million rupees. *Kirana Pasals*, which are studied in this paper, mostly fall under micro and small enterprises definition in Nepali legislation.

Historical Context On Importance Of MSMEs

The importance of MSMEs to sustainable economic growth and social development went largely unnoticed till the later half of the 20th century. They have always existed in large numbers, employing large proportion of the labour force and providing considerable additions to the national GDP. They play an important role in income distribution and social inclusion. Recently, their importance to the development of knowledge economy has also come to the forefront of SMEs (small and Medium Enterprises) literature. For much of the 20th century, these enterprises were thought of as merely a Segway into building larger firms. They were understood as some sort of a by-product of an economy that could not build and sustain enough large-scale production. The leading idea was that, it was large firms and big corporations that really drove economic growth. These small enterprises, particularly micro and small enterprises, were thought to exist largely due to lack of employment opportunities in

large enterprises. Needless to say, due to their perception as an adverse and unwanted aftereffect of insufficient economic development, they were paid very little attention by the authorities and were largely relegated to the shadow economy or informal economy. Once the economies developed, it was thought that these MSMEs would fizzle away as labour and capital got absorbed into larger more productive firms (Mc Pherson 1996, Enderle 2004, Spence and Painter-Morland 2010). MSMEs were the lesser-preferred enterprise that existed until something better came along, namely large modern and formal enterprises.

Of course, the way we view these enterprises now have changed. We understand that they are no longer just a temporary transitional phase institutions but rather a solid fixture of a strong economy. We understand the important role they play in developing community economies, creating a healthy labour market, reducing income inequalities, reducing social inequalities (e.g. gender inequalities and exclusiveness), in developing knowledge economy, generating innovations and creativity, to curbing monopolies and other such non-competitive behaviour, and in providing vital goods and services to local communities and markets (Dalberg 2011, Ayyagari, Demirguc-Kunt and Maksimovic 2012). This begs some explanation, but first let's look way in which micro, small and medium enterprises are classified.

Characteristics Of MSMEs

MSMEs in Nepal share similar characteristics to that found in MSMEs in other developing countries and Least Developed Countries. Researches done on the characteristics of MSMEs in African countries have been found to be relevant in Nepali context. These characteristics are (European Economic Chamber, n.d.):

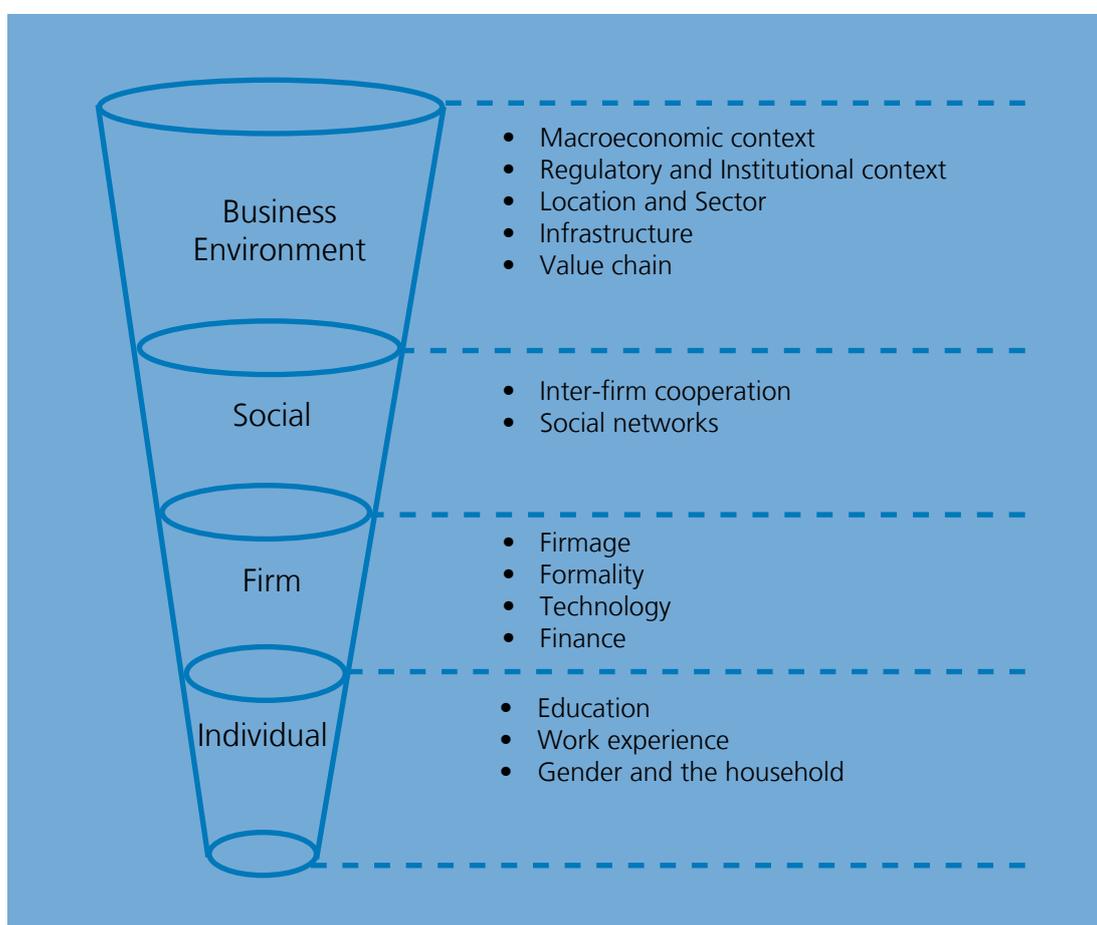
- Largely family run enterprises that are set up with family savings and support by friends and family
- A single individual often plays both the role of owner and manager and makes all the key decisions
- Low credit worthiness
- Enterprise relies largely on the skills of the founder and managerial competence requirements are not perceived to be of importance
- Staffs are recruited often without job analysis or job description and are rarely delegated decisions making authority.
- Technology used is locally innovated and is often limited in capacity and efficiency
- Largely cater to local markets
- Poor access to institutional credit for SMEs

These characteristics are a general rule of thumb. Nonetheless, it helps us draw some problems MSMEs face in order to grow.

Factors Shaping Growth Of MSEs

Nichter & Goldmark (2005) present a funnel shape figure to emphasize the several factors that shape the growth performance of micro and small enterprises (MSEs). Figure 1 shows the factors grouped into four broad categories: contextual factors related to the business environment, social or relational factors, firm characteristics, and individual entrepreneur characteristics.

Figure 1: Key factors affecting MSE Growth



Source: Nichter & Goldmark (2005)

While a separate elaborate study is necessary to determine which factors play the most prominent role in shaping the growth of MSEs such as *Kirana Pasals* in Nepal, the scope of the research is mostly oriented towards exploring the regulatory and institutional context as being very crucial for, firstly, survival and the growth of *Kirana Pasals*.

Role Of Regulations

Analysis suggests that, while some regulations may deliberately favour SMEs (many regulations exclude the smallest firms), in general the adverse impact of regulations on SMEs can be particularly harmful. This is because SMEs are less equipped to deal with problems arising from regulations since they have less capacity than larger firms to navigate through the complexities of regulatory and bureaucratic networks. (OECD, n.d.)

Gaush & Hahn (1999) indicate that regulation can have a significant adverse impact on economic growth. Specifically, regulation aimed at controlling prices and entry into markets that would otherwise be workably competitive is likely to reduce growth and adversely affect the average standard of living.

The regulatory and institutional environment in developing countries— notoriously burdensome when compared with developed countries—frequently hampers small enterprise growth. Econometric analyses underscore how these challenges disproportionately harm smaller enterprises (Beck, 2004). Regulatory and institutional challenges may also deter MSE owners from making growth-enabling investments (Nichter & Goldmark, 2005).

Studying the Legal and Regulatory Environment for Micro and Small Enterprises in Russia, Safavian, Graham & Gonzalez-Vega (n.d.) show that while taxation receives the most attention in the literature regarding the impact of regulation (on MSEs in Russia), other regulatory exigencies force enterprises to incur high transactions costs. Because of the poor drafting of laws and regulations, combined with the lack of easy access by those affected to the text of the regulations, substantial managerial and financial resources are consumed simply in identifying the statutory requirements that apply, and in determining (a) what range of approvals are needed in order to operate in full compliance with federal, regional, and local laws; (b) in what sequence; and (c) what documentation is required in each case (Buckberg, 1997). Ensuring compliance with the multitude of statutes is a major concern for the regulatory authorities, but there is little transparency and predictability and MSEs incur very high costs compared to the size of their operations (Safavian, Graham & Gonzalez-Vega, n.d.).

That said taxation is one of the main issues that surround SMEs, particularly in terms of tax design. SMEs face a disproportionate burden from tax in comparison to larger firms. In a survey conducted by OECD among its member countries, it is found that the compliance cost of tax on SMEs is much higher in terms of its sales and assets. The findings suggest that the compliance cost for SMEs is further compounded by collection enforcement cost, which make tax compliance a hassle for both the enterprises and the tax authorities. A research carried out by Ishengoma and Kappel (2011) on the effects of the business environment on the growth potential of Micro and Small enterprises in

Uganda from 1994 to 2010 found that growth potential of MSMEs are inversely related to taxes. They found that high taxes led to decreased potential for growth through low internal sources of funds and accumulation of investment, and reduced capacity to invest in productive technology. Thus factors that constrain firm's investment in turn constraints its growth potential (Gereffi 1999, Reinikka and Svensson 2001).

Politicization Of Economic Activity: More Regulations

What Simon Johnson called politicization of economic activity generally applies to the overall economic context of a post conflict and politically unstable country such as Nepal and *Kirana Pasals* seem to be no exceptions to that. Johnson et al. (1997) explain that politicization of economic activity as the exercise of control rights over firms by politicians and bureaucrats. This regulatory powers over privatized and private firms, include the ability to regulate and restrict entry, control over the use of land and real estate that private businesses occupy, the determination and collection of taxes on businesses, the right to inspect firms and close them if regulations are violated, control over international trade and foreign exchange transactions, and in some cases the power to set prices. In the next section, the exercise of such authority on *Kirana Pasals* can be seen. Political control generally reduces the profitability of doing business, and therefore adversely influences entrepreneurial activity and economic growth (De Soto, 1989). During the transition from communism to capitalism, the adverse effects of political control on growth are manifested in a number of ways. Most directly, when profits or potential profits are taken away from firms through regulation, taxation, or corruption, entrepreneurs choose not to start firms or expand less rapidly than they might otherwise. But entrepreneurs have another option, namely, to operate unofficially (Kaufmann and Kaliberda (1996); Kaufmann (1997)).

Growth And Formalization Relation In MSMEs

Large portions of MSMEs across the globe exist in informal economy. Informal economy is one where the activities are unrecognised, unrecorded, unprotected or unregulated by public authorities (Becker 2004). The importance of formalisation and the reasons to formalise or remain informal depends on the views taken towards the informal economy. One perspective is that the informal economy is a separate marginal economy that provides income and safety net for the poor (ILO 1972). This approach is falling out of favour as we are seeing increasing interconnectedness between the formal and the informal economies (UNCTAD 2001). The second approach views the informal economy as a subordinate to the formal one, where privileged capitalist dominate small entrepreneurs to lower costs (Castells and Porters 1989). The third approach views the informal economy as a by-product of over regulation and bureaucracy in the formal economy (De Soto 1992).

For the purpose of our research we aim to look at the relation between formalisation of MSMEs and their growth. Countries that improve their regulation to correspond to good practice standards can increase growth by as much as 2.3 per cent a year (Djankov, et. al. as cited in ILO, 2006). A report by OECD (2006) argues that in the short term, existence in the informal economy for MSMEs might provide a more attractive alternative. However in the long term, informality does not place these enterprises in a position to reap the full potential for growth. A study by Norris & Gabriela (2008) on regulations, growth and formality highlights the finding that firms reduce their formal operations with greater tax and regulatory burdens, but increase them with better enforcement quality. In terms of firm growth, the study found a differential impact of regulatory burden and enforcement quality on formal and informal firm growth. In particular, it shows that growth in formal firms is negatively affected by both tax and financing constraints, whereas these constraints are insignificant for growth in informal firms. The same study citing World Bank (2006) also mentions that high costs of business regulation, weak tax administration, a poor institutional framework, and weak property rights are frequently cited as major obstacles to doing business in many transition countries. Additionally, the study also suggests that there is considerable evidence that the same obstacles are also important determinants of informality (Dabla-Norris, Gradstein, and Inchauste, 2008). The theoretical underpinning for these results is related to the idea that in the absence of effective monitoring and compliance, firms respond to the increased burden of these constraints by moving into the informal sector. However, this decision affects the allocation of resources across firms' activities and can distort incentives for capital accumulation, competition, and innovation. This is because in order to avoid detection, firms may remain sub-optimally small, adopt fewer productive technologies, use irregular procurement, and divert resources to mask their activities. Being outside the regulatory and tax umbrella, informal firms can afford to be less productive than their competitors in the formal sector. However, they may also be locked out of markets for finance, technology, and legal protection. Because informal firms are typically less productive or efficient, aggregate productivity and economic growth may suffer (Norris & Gabriela, 2008).

IFC (2007) also points out that informality can take different dimensions in MSEs, which can be seen in the figure below:

Designing a Tax System for Micro and Small Businesses

MSE operates entirely outside the formal economy	MSE complies with a small number of legal and regulatory obligations, but not with others	MSE complies with most legal and regulatory obligations	MSE formally complies with legal and regulatory obligations, but not entirely respects all obligations	MSE is fully compliant with legal and regulatory obligations
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Source: *Designing a Tax System for Micro and Small BusinessesL Guide for Practitioners. IFC (2007)*

Formalisation itself might not provide direct benefits but in the long run it does the following (OECD 2006, pg. 28):

- . Provide higher quality, better paid, more sustainable jobs.
- . Reinforce the social contract between citizens and their state.
- . Strengthen the reliability of agreements between firms.
- . Build investor confidence (and increase investment).
- . Broaden the tax base (potentially permitting lower tax rates).
- . Increase information on local enterprises to facilitate deal-making and strengthen frameworks for policy advocacy.
- . Reduce the cash economy and provide more resources for intermediation by the formal financial sector.
- . Improve access to business services, formal markets and productive resources such as capital and land.

Not much work has been done on the formalisation process itself but it can be inferred that some barriers to growth are likely to correlate with barriers to formalisation (OECD 2006). One of such barriers is the regulatory barriers. Various complex and burdensome procedures that business needs to adhere to during the registration process are major hindrances for formalisation of MSMEs. Compliance to these regulations during operation, that is formal operation costs, is also a significant barrier to formalisation. Some such barriers to formalisation are: administrative barriers that is barriers to growth created by the way regulations are enforced (e.g. excessive paper work, abuse of authority), tax, compliance fees and other financial requirements, labour regulations, inefficient contract enforcement, corruption, lack of business services and lack of information (De Soto 1992; Loayza 1997; Morrisson 1995). In developing countries where these regulations are often inconsistent and unclear, they create an unsurmountable obstacle for firms seeking formality (Tokman 2001; Becker 2004) .

In addition to barriers to formalisation, Ishengoma and Kappel (2006) discuss some other factors that affect firm's decision to formalise. Growth and age of the firm is seen as one of the determinant of formalisation. The argument is that as firms grow through time it becomes more desirable for the entrepreneurs to operating formally and the benefits of formalising outweighs the cost (Levenson and Maloney 1998). However this is only realised if the legal framework caters to the needs of MSMEs. Jaeckle and Li (2003) argue that line of business also affects the firms desire to formalise. The net benefits provided by societal institutions also determine the degree and the level to

which MSMEs are willing to formalise. Knowledge of anticipated benefits and the level of enforcement exercised by the government are also found to be contributing factors in the decision to formalise (Morission 1995; Bass and Kappel 1997).

Access To Finance

In an extensive research done by Dalberg Global Development Advisor in 2011 on support to SMEs in developing countries through financial intermediaries, they found that nearly half of SMEs cite access to finance as their main hurdle to growth (Dahlberg 2011). Access to finance being a major hurdle to growth to MSMEs has also been noted by Orser (2000), Mambula (2002) and Livard Pang (2006). The Dalberg report finds that this financing gap in the developing countries is largely due to the assumption by commercial banks that cost and risk of serving SMEs are high. MSMEs get most of their access to capital through micro financing. Capital gained through micro finance is limited and often unable to provide sufficient capital required for growth. Most micro financing institution is oriented towards providing short-term loans with limited facilities of overdraft, transfers and payment (De la Torree, Martinez Peria and Schmukler 2010). However, for expansion MSMEs require long-term loans with full facilities to current accounts, transfers and payments. Furthermore, the CGAP report on Financing Small Enterprises, found out that out of the 300 micro financing institutions it surveyed in 69 countries, most of them lacked any appropriate methods of risk assessment (CGAP report, n.d). Duflow and Banerjee (n.d) state that the lack of capital inhibits MSMEs to access technological upgrades that would increase productivity and profitability.

Than (2009) cited in Harvie, Oum and Narjoko (2010) highlights access to finance being the key factor that determines the competitiveness and readiness of MSMEs to realise their potential to growth. This research finds that the problem for provision to funds are that the conditions needed to be satisfied to gain access to these funds are numerous and difficult. This is particularly so because most MSMEs do not maintain transparency of operation due to lack of formal accounting. Similarly, the 'opaqueness' of the principal-agent problem (that is the difficulty to separate distinctively the owner and the shop as separate entity), the feasibility of the loan and the capacity of the firm to pay back are difficult to assess (Torres et al 2010). This is one of the reasons why commercial banks require thorough paperwork and stringent procedures for loans to SMEs. Nofsinger and Wang (2011) also point towards a clear separation of the owner from the business entity as being a problem for loans and credit rationing to MSMEs. They also highlight the lack of collateral as being another major problem. Peterson and Rajan (1994) state that such issue arises between MSMEs and banks due to absence of information, lack of managerial capabilities, size of investment, and improper collateralisation of the SME's assets.

Harvie (2010), argues that access to finance for MSMEs are also affected by macroeconomic policies that are oriented towards industrialisation and import substitution strategies, weak institutional regulations such as lack of property rights and standard regulations in the financial system for paperwork and formalities. Weak institutions such as lack of property rights also contribute to difficulties in posting collateral. Due to irregular cash flows, and asymmetrical information, start-up firms in particular have difficulties in access to equity funds.

Freedom From Corruption As Economic Freedom

The Heritage Foundation's Index of Economic Freedom considers four categories of freedom as indispensable to economic freedom and under the first category Rule of Law, it considers freedom from corruption as a key determinant of economic freedom. The report mentions that corruption erodes economic freedom by introducing insecurity and uncertainty into economic relationships making corruption a hindrance for economic freedom. In a research done by Dobryninas and Zilinskiene (n.d), corruption was cited as a major hurdle to doing business for SMEs. In their survey of 1005 SMEs in Lithuania, 71% of business listed corruption as an obstacle to growth. The burden of corruption tends to be greater on MSMEs than on larger enterprises. A report by the United Nations Industrial Development Organisation (UNIDO and UNODC 2012) on corruption and SMEs found that micro, small and medium enterprises have higher incidence of corruption, from obtaining license and permits to additional payments for official procedures, than larger firms when taken as a percentage of revenue. Small and short profit margins make it more difficult for SMEs to refuse paying bribes as it may cause their business to shut down which would be disastrous for their livelihood. SMEs' lack of reach with bureaucrats and politician makes them more vulnerable to bribery. Furthermore, as their capital structure is not regulated, they become more susceptible to bribes and extortion. It is also suggested that due to their informal structure, the culture for engaging in bribery is allowed to persist in greater degree than larger forms with formal structures (UNIDO, n.d.). In an interesting research by Demuijnck and Ngnodjom (2012), they found that even though SMEs engaged constantly in extortion and corruption activities, they did not see themselves responsible for corruption.

Other Aspects Of MSME Growth

Financial and business development support services have also been found to important factor in the growth of MSMEs. Lack of business skills is often seen as one of the critical barriers to growth for micro and small enterprises. Mubugua, Mubugua, Wangoi, Ogada and Kariuki point towards poor managerial and entrepreneurial skills as a key hurdle to growth for MSMEs (2013). In their survey of tailoring and dressing making

MSMEs in Eldoret, they found direct relations between poor performance in these factors and poor growth. Not only do owners/managers of MSMEs tend to be poorly trained or unskilled, they are also confronted with wide range of issues due to their multi-functional role. This causes them to take up immediate issues while overlooking less obvious but more significant problems that can have critical impact (Stokes and Wilson 2010). IN addition to that MSEs in which the entrepreneurs had taken up formal training tend to show higher rate of growth. Orser (2001) similarly found positive relation between performance and high level of managerial skills. On a recent study carried out by Eshetu, Ketema and Kassa (2013) carried out a study on the economic impact of support services on micro and small enterprises using a case study in Ethiopia. From their research they found that those that participated in the support programs benefited from average increment on sales by 28%, employee level by 42% and capital asset formation by 60%. These correlations don't necessary reflect causation for growth, but outcomes of these researches do suggest managerial skills to be an important factor in growth.

It is undeniable that promotion and marketing is vital for future growth of any business. But due to the small size of the business, limited investment capital and lack of knowledge on the importance of marketing, MSEs don't often engage in marketing activities themselves. These concerns are highlighted by Opkar (2011), who argues that low demand for product and services is one of the major factor constraining growth and survival of SMEs. Similarly, Kaliyamoorthy and Parithi in their analysis of MSMEs in India, point towards the lack of organised marketing, in terms of promotion of goods and services and market research and information, as being one of the key problems. MSMEs don't naturally invest in research and development or other innovative activities which in turn hampers their long term competitiveness, sustainability and growth. These concerns are echoed in OECD (2011) report on fostering competitiveness of SMEs in Moldova. In addition to training, providing technical support services, marketing and promotion, improvement of market access for SMEs has also been identified as an important factor for their growth. Since individual SMEs have limited capital and minimal political clout, they are too small a player to individually bring about greater market access. And since MSMEs have very little point of difference from each other and that they operate with high competition, increased access to market could be a significant factor in increase growth of the whole sector. This problem is identified by Ishengoma and Kappel (2011) as they reveal a negative correlation between market access and growth for MSMEs.

General Characteristics

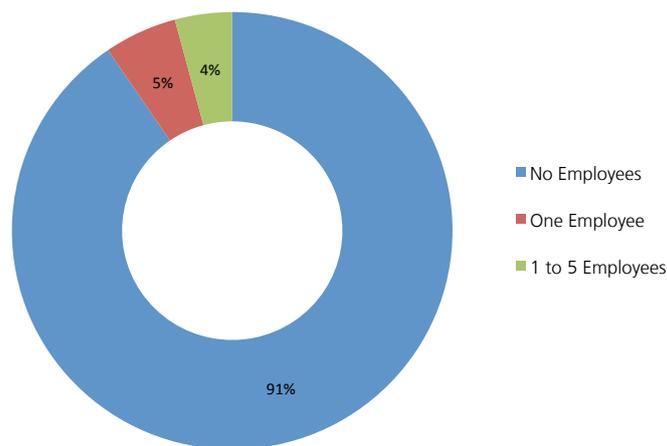
The Industrial Enterprises Act (1992) of Nepal defines cottage industry, small enterprises and medium enterprises based on level of investment and power usage. The Central Bureau of Statistics and the Ministry of Labour classifies enterprises based on employment criteria. Value Added Tax (1995) applies tax threshold based on annual turnover. Income Tax Act classifies them in line with Industrial Enterprises Act (1992). Financial Intermediary Act defines them in terms of employment (ILO 2005). The lack of a clear and uniform definition for micro, small and medium enterprises impedes the ability to formulate and implement well-coordinated and holistic policies for MSMEs. In addition to that, government policies have viewed MSMEs largely in terms of cottage industries and manufacturing industries. Very little attention has been given to MSMEs in the service sector or the trade sector.

Table 2: Ownership of Kirana Pasals

	Frequency	Percentage
Family Run	187	69.80%
Others	81	30.20%

Nearly 70% of the *Kirana Pasals* surveyed were family run stores and for 80% of the respondents, the Kirana Pasal was their major source of income and thus, their livelihood. We found that family run stores largely tend to be stores that are operating for the purpose of sustenance or were inherited. 90% of the stores in our survey did not employ help. In other words, family members that were not viewed as employees of the store and thus not compensated as such, largely ran these stores. This finding is in line with the discussion on the problems of viewing the owner and the store as separate entity for small and micro enterprises like *Kirana Pasals*. Our findings also suggest that these stores provide a major source of income of an overwhelming number of respondents (80%).

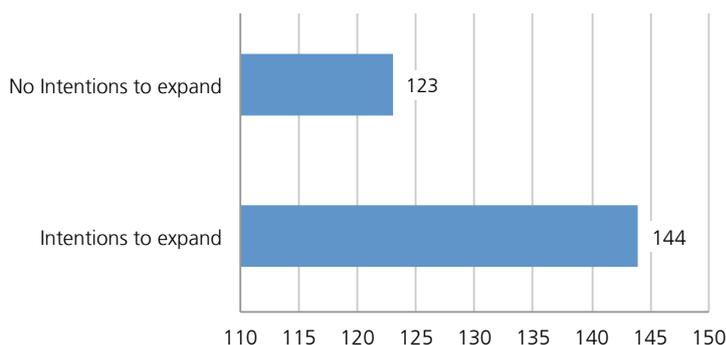
Fig. 2: Number of Employees



Findings On Factors Affecting Growth Of Kirana Pasals

Most of the respondents see that there is a clear cost advantage for them in expanding their operation. In other word, most Kirana Pasal owners/managers are in some knowledge of the economies of scale they can enjoy by expanding their operations. We found that those who saw the benefits of economies of scale more clearly were keener on expanding their business. When asked if they had any thoughts in expanding their stores in any means, 53.9 % said they were thinking of expanding while 46.1% said they had not thought of expanding. In other words, more than half of the respondents did see potential for growth. Larger stores were keener on expanding their business than smaller stores. In addition to that, stores that were open/run for the purpose of sustenance or as an inherited business were less likely to think of expanding than those that were open/run for an alternative source of income or as a business investment purely aimed at making returns. This could be due to greater risk averseness of the former two as compared to the latter two. This also implies a certain level of risk and uncertain environment that *Kirana Pasals'* face in Nepal as the ones whose livelihood depends on these stores are less likely to risk it all through expansion. This is an issue that has a direct relation to the regulatory environment that these stores face.

Fig. 3: Intentions to Expand



Meet Hari Dangol. At the age of 35, he runs a Kirana Pasal in Minbhawan, Kathmandu, to support a family of three. He got the shop as a gift from his father. The store is his family's only source of income. Therefore, he toils hard from 6 in the morning to 8:30 in the night to earn a meager Rs. 150-200 profit a day. "The smaller the goods, the higher the profit margin. For example there is some profit in selling bottled water," he says. Goods like grains and cigarettes have very little profit. Upon being asked why his store is not registered, he replies with a smile, "I really don't know why. It wasn't registered when my father bought it." So he doesn't have to pay tax. He thinks that his shop is not providing enough to sustain his family. He has to work tirelessly, all day long. He cannot rest when he wants to. To add to that, he feels that lack of good governance, political instability, inflation and corruption have hampered the business environment in Nepal. There is no real value for all the energy he spends at work. So he says that he has doubts over whether or not to continue his store.

As MSMEs, *Kirana Pasals* are subjected to several aspects of business environment when considering growth and expansion of their enterprises. Empirical results demonstrate that firms rank regulatory problems, particularly taxation, as among the most severe obstacles to the long-term success of their enterprises (Safavian, Graham & Gonzalez-Vega, n.d). Some of those major regulatory obstacles are discussed in the following paragraphs as suggested by the findings. Most of those aspects can be underpinned in the variables taken into account while determining economic freedom of a country, more particularly as used in the two indexes of economic freedom published annually by The Fraser Institute and The Heritage Foundation.

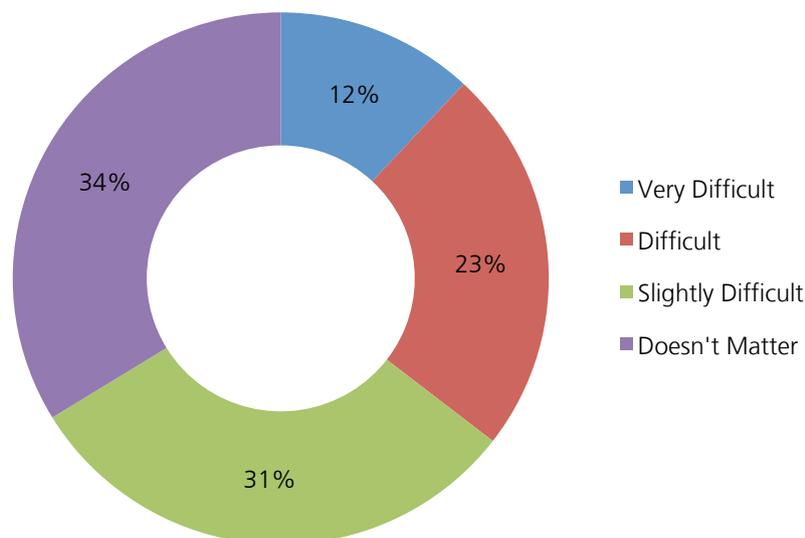
When *Kirana Pasals* consider growth, it means adding more value to products already being sold, adding the variety of products being sold (which include imported goods involving customs), falling under a higher tax bracket and so on. A simple example that came up during the research was of selling a local food item – beaten rice. Generally, beaten rice is sold right out by the sack in the shops in weights as demanded by customers. However, for ease and protection from dust and other factors, many owners started pre-packaging the beaten rice in plastic bags in standard weights such as 500 grams, 1 kg, 2 kg and so on. However, this invited another regulatory compliance of labeling the packets. The shopkeepers that came up with this innovative idea were actually persecuted by the Standards department for not labeling the packets. This is a simple example that shows that as Kirana Pasal owners consider growing, there are many issues of formalization, standardization, taxes and other regulatory and non-regulatory issues. These factors thus play a role in shaping the growth of these shops as entrepreneurs weigh extra costs and gains. Some of these factors are discussed below:

Formalisation

The legal form of the enterprises is also a key characteristic in determining the costs of market entry, access to legal recourse, access to financial services, and tax liability. Businesses registered as individual enterprises (physical persons) face a much less complex registration procedure than companies (juridical persons), and registration can usually be completed within one week for the former type of firm (Safavian, Graham & Gonzalez-Vega, n.d). This holds true in the Nepalese context too.

In order to understand the factors of business environment that affected the survival and growth of *Kirana Pasals*, the owners/managers were asked how they felt about government rules and regulations. Respondents were asked to rank on a five-point scale (ranging from very appropriate to very harmful) how helpful they thought government rules and regulations were for their business. 66.70% of the registered shops answered that it would be difficult to compete with other shops if they had to follow the rules and regulations and pay income tax compulsorily. Similarly, 64.30% answered it would be difficult. Meanwhile, unregistered shops did not show much concern regarding following the rules and regulations and paying income tax to competition with other shops.

Fig. 4: Difficulties in Remaining Competitive After Formalising



In the next paragraphs, laws that *Kirana Pasals* are subjected to and the government departments under whose jurisdictions they fall under are listed. This suggests the wide panoply of regulations *Kirana Pasal* owners have to face. It is important to note that these are only the perceptions of the respondents, which may not reflect the true constraints *Kirana Pasals* face, as many of those regulations affect enterprises indirectly and thus may not be perceived by the entrepreneurs. The survey also does not incorporate the responses of firms that either disappeared or that could not get started because of rules or regulations. Among non-regulatory constraints, those relating to location and competition from other shops were commonly cited.

List of major laws and policies based on which *Kirana Pasals* are subjected to government action:

- . Consumer Protection Act, 2054 (BS) and Regulations, 2056 (BS)
- . Private Firm Registration Act 2014 (BS) and Regulations, 2070 (BS)
- . Food Act, 2023 (1966)
- . Customs Act, 2064 (2007)
- . Black Marketing and some Social Crimes and Punishment Act, 2032
- . Income Tax Act, 2058 BS
- . Competition Promotion and Market Protection Act, 2063 (2007)
- . Export and Import (Control) Act, 2013 (1957)
- . Essential Commodities Control (Authorization) Act, 2017 (1961)
- . Essential Commodities Protection Act, 2012 (1955)
- . Nepal Standard (Certification Mark) Act, 1980 and Regulations (1983)
- . Industrial Enterprises Act (1992)
- . Insolvency Act, 2063 (2006)
- . The Copyright Act, 2059 (2002)
- . The Patent, Design and Trade Mark Act, 2022 (1965)

Kirana Pasals under the jurisdiction of the following major government agencies:

- . Municipality where the shop is located
- . Ministry of Commerce and Supplies – Department of Commerce
- . Ministry of Finance: Inland Revenue Department
- . Ministry of Finance: Customs department
- . Ministry of Industry: Department of Cottage and Small Industry
- . Nepal Bureau of Standards & Metrology - Department of Food Technology and Quality Control

List of places where *Kirana Pasals* are required to register:

- . Municipality or Village Development Committee – at the local level
- . Ministry of Commerce and Supplies – Department of Commerce – at the Central Level
- . Ministry of Industry – Department of Cottage and Small Industry – at the Central Level
- . Ministry of Finance – Inland Revenue Department – For Income Tax

As the above listings suggest, the laws and regulations that are applicable to *Kirana Pasals* are scattered across several acts, regulations and rules and are enforced through several government agencies. Generally, Kirana Pasal owners are aware of few of those laws that are applicable to their business but there always remain minuscule provisions and clauses which the businesses would not be in compliance with, simply because of the volume and scattered nature of those regulations, which keeps the business always on offence. This acts not only as a hindrance to growth but as a challenge in mere survival of *Kirana Pasals*. Buckberg (1997) as cited in Safavian, Graham & Gonzalez-Vega, n.d) show the impact of the burden created by the multitude of regulations saying ‘because of the poor drafting of laws and regulations, combined with the lack of easy access by those affected to the text of the regulations, substantial managerial and financial resources are consumed simply in identifying the statutory requirements that apply, and in determining (a) what range of approvals are needed in order to operate in full compliance with federal, regional, and local laws; (b) in what sequence; and (c) what documentation is required in each case. Ensuring compliance with the multitude of statutes is a major concern for the regulatory authorities, but there is little transparency and predictability and MSEs incur very high costs compared to the size of their operations.’

Citing Snodgrass and Biggs (1996), Nichter & Glodmark (2008) also expound that although small informal MSEs may be able to circumvent government regulations and taxation, as they grow they risk becoming more visible, creating disincentives to expand beyond a certain size. They also cite Winter (1995) and further add that informal firms may therefore need to “keep their heads down,” ruling out large size and rapid growth, as well as close relations with formal firms.

Meet Mr. Pavitra Bajracharya. He started running his own Kirana Pasal at the age of 10 and was threatened to be jailed by authorities for selling rice marginally above the price government dealers were supplying on. As he was just 10, a neighboring shopkeeper speaking in defense of Mr. Bajracharya was also put in jail, he recalls. Unfortunately the situation is not too far off from reality even several decades later today, he shared during an interview.

Under the Industrial Enterprise Act (1992), micro and small enterprises are required to register with the Department of Cottage and Small Industry. The Department of Industry is responsible for registration of medium and large enterprises. MSEs are required to register with both local authorities as well as central authority. When registering, the enterprises are required to submit an application at respective registration offices depending on the nature, size, location and type of business (ILO 2005).

Experts on the matter suggest that one of the key hindrances to complete formalisation is the multiple registration processes that are required with all the relevant authorities. Enterprises are required to register with Department of Cottage and Small Industry, Inland Revenue Department, and Municipality/ Village Development Committee. As these authorities don't share information on registrations with each other, enterprises are required to be registered with each one separately. The required documentation and processes differ for registration with each authority and this make the process of formalisation cumbersome and costly. The news presented below (taken from an online news portal in Nepal) also explains one aspect of the regulatory hurdles which force small enterprises like *Kirana Pasals* from starting up and even if they do start up, stay informal.

On the other hand, among those respondents that had registered, we asked how they would have ranked the registration process on a five-point difficulty scale. Around 44% of the respondents thought the process was neither difficult nor easy, and around 35% of respondents thought that the process was easy. 13.9% said it was difficult and only 5.1% said it was very difficult. In regards to the cost the cost of registration, more than half of the respondents that had registered, said they thought the cost of the registration process was affordable. Around 25% said it was costly. Most of these

Government declares NRs. 300,000 of minimum threshold to open a Kirana Pasal

Published on October 3, 2013 (translated to English from onlinekhabar.com)

The government is gearing towards strictly implementing laws to ensure registration of all businesses. It has also declared minimum investment amount to do business. This system of minimum investment threshold has been in place before the recent announcement, but this time it has increased the threshold and says it intends to implement it more strictly. According to the latest announcement, the Department of Industry is preparing to make paid up capital from NRs. 200,000 to NRs. 400,000 a requirement for all companies.

The department has proposed NRs. 600 as registration fee and NRs. 200,000 as minimum paid up capital for opening up grocery stores and stationary shops in village development committees (VDC). The threshold of minimum paid up capital is NRs. 300,00 for such stores in the metropolitan areas. Similarly, the provision mandates a minimum capital of NRs. 4,000,000 to open up a petrol pump, jewelry store, shop selling machinery and transformer and automobile shop. The regulation comes as a response to the situation whereby registered companies have

not run businesses, have misused their company names and have done businesses other than what they were registered to do. Taken from : <http://www.onlinekhabar.com/2013/10/123734/>

respondents were only partially formalised, that is they were not registered with all the required authorities, which limits extending the findings to the complete formalisation process. This nonetheless indicates that reducing the cost of the process begs more attention. This finding corroborates with that of ILO (2005) on the policy environment for MSMEs where cost of registration and renewal are indicated as major hurdles. The ILO document further adds that lack of clarity about the process itself, i.e. lack of proper information, is another major barrier to formalisation for MSEs. The cost of compliance with rules and regulations create disincentives for MSME identified as a hurdle to growth.

Fig. 5 Difficulty of Registration Process

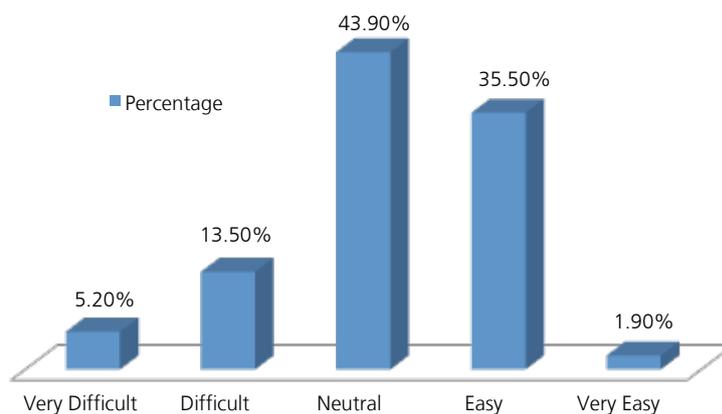
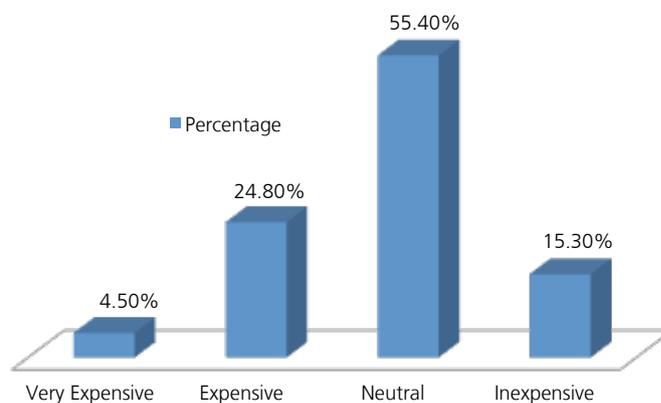


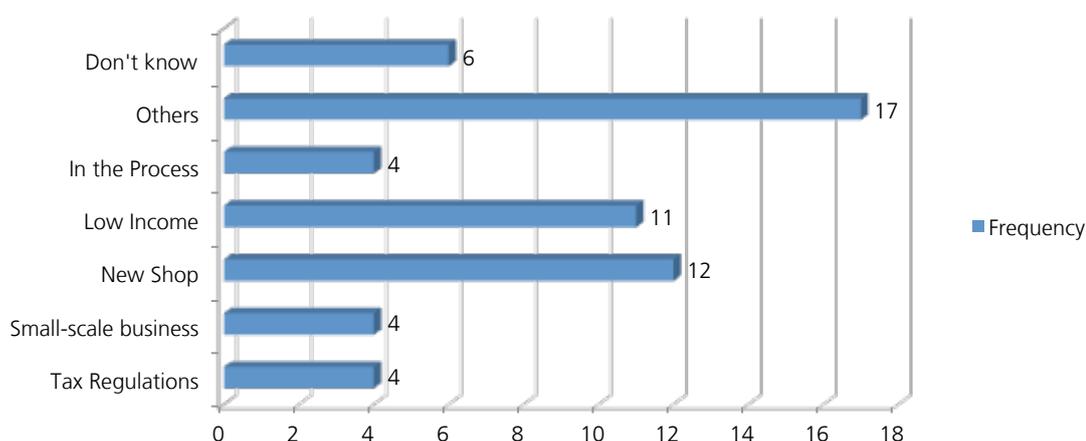
Fig. 6: Cost of the Registration Process



Hamro Samriddhi Bhandar is a store in Patan, Lalitpur district. The storeowner, who runs the store herself does not know all the regulations that have to be complied with, in order to register the business and acquire all the capital due to the plethora of regulations and procedures that a layman simply cannot understand. She admits that she couldn't grasp all the procedures and thus had her husband, who works in a different office take care of all those procedures for her. She is also dismayed by the fact that there aren't any support institutions or even any institution that helps with promoting the services delivered by stores like the ones she operates. She feels that advertising her store through any kind of media is too expensive and out of the means of businesspeople like her and thus they have to rely totally on the locals to make money. But despite such a condition, different groups show-up asking for donations and people like her cannot even deny them of any help, fearing repercussions.

During the research, we found a strong correlation between the duration of operation and registration and income and registration. We found that new shops, or shops that have been in operation for a short period of time are largely not registered but show strong intentions to register. We also found there to be a higher percentage of registration among shops that are a major source of income for the owners than among shops that were not the major source of income. This could be due to the seriousness of the owner/manager towards the enterprise. When the respondents were asked why they had not registered, the size of the store and tax regulations were often cited as the main reasons for not registering. As cited above, the fact that more of the stores that rely on *Kirana Pasals* as the major source of income are reluctant to expand further is also indicative of regulatory problems as one of the factors that constrains expansion.

Fig. 7: Reasons for Not Registering



Price Fixing By Government

According to Guasch and Hahn, (1999) high degree of regulation has an adverse effect on the economy, is usually subject to political influences, and is rarely implemented with the sole purpose of improving economic efficiency. The practice of designating the prices of commodities by the government is one of such examples. Government determining the prices of commodities sold by retail stores such as *Kirana Pasals* is a frequently reported issue in the popular media in Nepal.

As inflation grows in the country and prices of commodities rise, especially during major festivals, the government without heeding several market factors, jump at fixing the Maximum Retail Prices (MRP) of commodities generally based on the rates provided by the subsidy receiving state owned enterprise selling commodities. There have been instances of Kirana Pasal owners being held by government authorities for not selling at those designated prices.

In the Nepalese context, the Department of Customs has made it mandatory to declare Maximum Retail Price of those goods which have high value in revenue contribution and whose trading volume is high. The government move of fixing the price of commodities— which comes few times a year after media's hue and cry about rising commodity prices with generally an anti-market narrative during the festival season — is according to the Essential Commodities Control (Authorization) Act 1961. The act states "Government of Nepal may, if finds it necessary or appropriate, to increase or maintain distribution or cause to distribute or to make available of any essential commodity in low cost, control or regulate the production, distribution or trade of such essential commodity in the prescribed area by a Notified Order."

Mr. U Shrestha of U. Shrestha Mart expresses serious concern over government setting price ceilings on goods. After growing his business to the level of mini-mart from just being a Kirana Pasal, he says there are things like packaging, hiring-staff, etc. that lead to higher operation costs. But government does not regard these facts before setting price ceilings and complying with such standards drags their profitability down drastically. Mr. Shrestha then admits that the success of mini-marts is largely dependent on the suppliers. Until and unless suppliers offer credit sales, start ups cannot make the bulk purchases that they have to make in order to run mini-marts (due to insufficient capital), and this he believes is something that businessmen cannot just do away with. Therefore there are challenges for new entrants and having a sound relation with some suppliers prior to entering into the mini-mart scene is the only relief, he says.

Cross tabulation between whether or not a shop is registered and where it is registered

		Where did you register your shop?				Total
			1	2	4	
Is this shop registered?	No	66	0	0	0	66
	Yes	40	84	19	54	197
	Total	106	84	19	54	263

Out of 268 respondents we had approached during the survey, 263 respondents gave valid responses. Our goal was to test whether or not these respondents had duly registered their businesses as per the law of the land. Our preliminary research showed that a Kirana Pasal had to be registered at 4 different institutions. We coded the institutions as:

- . 1 - Municipality or Village Development Committee – at local level
- . 2 - Ministry of Commerce and Supplies – Department of Commerce
- . 3 - Ministry of Industry – Department of Cottage and Small Industry
- . 4 - Ministry of Finance – Inland Revenue Department

While 40 respondents did not answer on where they had registered their shops, we found that all other respondents had registered at only one of the four institutions as provisioned by the law.

This explains why 81.3 % of the respondents found the registration process easy to deal with and also why 70.7% of the respondents found the process to be on the cheaper side. As evinced by the table above, we can conclude that none of these stores were fully registered as per the law. These shops were only partially formalized.

When Government of Nepal (GoN) had announced to formally enforce the maximum retail price (MRP) for fifteen essential commodities ranging from rice, pulses, sugar, and flour to edible oil on September 16, 2012, an editorial published in the Himalayan Time, a national daily wrote on 2012-09-18 :

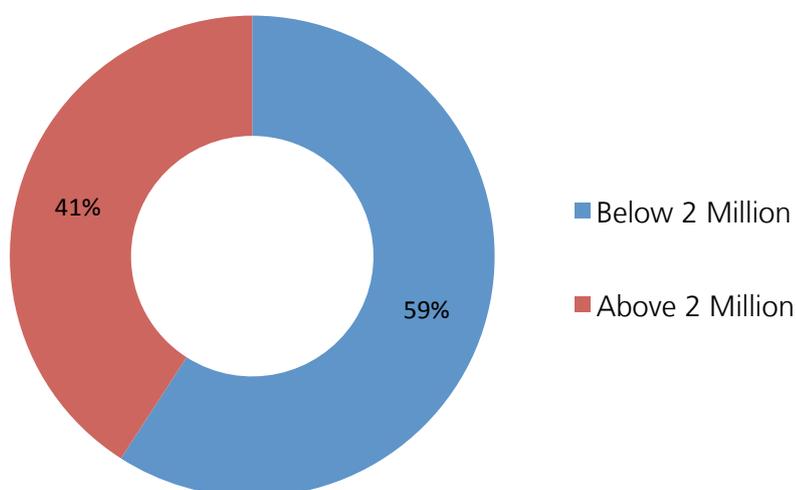
“The price of essential commodities has risen because of bandhs and strikes that have had a telling effect on the production of essential goods and in their transportation. The price rise can be attributed to them as well as the prevailing political scenario which is not favourable for economic growth, and on the other hand which is

pushing up the prices of the essentials which the impoverished people of the country are finding hard to bear. The MRP was supposed to relieve the burden of the consumers, particularly now that the festive seasons are fast approaching. Instead, the declaration of the MRP seems to have backfired. So it is not strange for the consumer activists to term the move as being a mere publicity stunt. The move is also accused of being against the open market operations, and furthermore it is also accused of being based on false price now that the present economic model of the country has changed.”

Taxes

Micro and small enterprises in the retail sector like *Kirana Pasals* are required to pay full tax amounts. Kirana Pasal owners are seen as the lowest echelon of entrepreneurs running micro enterprises whose yearly turnover generally do not exceed NRs. 20, 000, 000. The *Kirana Pasals* in the research, majority of which are registered as sole proprietorship firms, are hence registered with the Inland Revenue Department and have a Permanent Account Number (PAN) to pay their income taxes.

Fig. 8: Average Annual Sales



Business incomes with turnover of up to NRs 2,000,000 are registered as having PAN. As businesses having Income with Annual Turnover up to NRs 2,000,000 and Annual Income up to NRs. 200,000 they pay:

- In the Metropolitan or Sub Metropolitan Cities NRs. 5000
- In the Municipalities NRs. 2500
- In the rest of Nepal NRs. 1500

Those with turn over greater than NRs. 2,000,000 or income greater than

NRs. 200,000 are eligible to pay 13% VAT and Corporate tax rate for Private Limited Co., Limited Co., Partnership Firm in the retail sector – a total of 25%.

According to Nepal Tax Fact, for the fiscal year 2013/14, the tax structure looks as follows:

Table 3: Tax Structure for Fiscal year 2013/14

Taxable Income Slab (in NRs.)	Individuals		Taxable Income Slab (in NRs.)	Couple*	
	Employment	Proprietorship Firm**		Employment	Proprietorship Firm
First 200,000	1% ***	0	First 250,000	1% ***	0
Next 100,000	15%	15%	Next 100,000	15%	15%
Next 2,200,000	25%	25%	Next 2,150,000	25%	25%

Source: Nepal Tax Fact FY 2013/14 (July 2013)

*Husband and wife should elect to be treated as couples and the option is not automatic choice.

** The rates are general tax rates for general proprietorship firms and may differ according to the nature of businesses and concessions provided.

*** The 1% tax is part of the social security tax and is deposited in a separate fund in the IRD.

These taxes are subject to an annual change and also government plans and policies announced in between. For e.g. the 1% social security tax.

Rupa Dahal 30 years old and she has been running a Kirana store for 5 years now. Her husband works elsewhere and she has a son that studies in grade 3. She opened the store in order to supplement her husband's income, as even he earns only a small amount of money. She takes care of household activities and sends her kid to school in the morning and spends the rest of the day at the store. Her store is very small, selling only grains, cigarettes and some chocolates. She is really proud of herself for at least being involved in some productive activity to help the family. Her store is registered and pays regular taxes to the government. However, she feels that the tax rate is too high. A lot of goods that she sells earn her a meager 25 Paisa profit per unit and even in that she has to pay as high as 10% in taxes. Besides, the registration process is not duly implemented and a lot of stores have been running unregistered. So she feels that it is unfair to people like her that competitors do not play at a level playing field. The bad condition of roads and pollution level around her store discourages people to stop around the neighborhood to buy stuff. So she adds that it is a huge disincentive to expand, as there is no substantial profitable prospect.

Due to poor or lack of record keeping by small enterprises, it is difficult to determine the tax burden on *Kirana Pasals*. In many cases, not having books or audited accounts may also result into the amount of tax to be paid being established by the tax official based his judgment, making use of a variety of indicators, including the observed standard of living of the entrepreneur. This might results in very high tax rates for enterprises.

For Kirana Paslas with an annual turnover of NRs.20,00,000, the estimated average profit that they make is 5 percentage². This implies that their annual income is NRs.100,000. According to the above tax regime, these firms should actually be exempt from any kind of taxation. However, in reality, these stores are currently required to pay NRs.3,500 annually as tax which is 3.5 percentage of their annual income! While other citizens that report income less than a hundred thousand rupees are exempt from income tax, these store owners are forced to pay 3.5 percentage of their income as tax.

Relationship between registration, taxation & business volume

					Change Statistics				
Model	R	R square	Adjusted R square	Std. Error of the Estimate	R Square Change	F Change	df1	df2	Sig. F Change
1	.804a	.646	.640	11880.247	.646	112.095	2	123	.000

- a. Predictors: (Constant), Q40 How much income tax do your business pay?, Q32 Is this shop registered?
 b. Dependent Variable: Q 55 How much sales do you do per day?

Model	Unstandardized coefficients		Standardized Coefficients Beta	t	sig	95% of Confidence Interval for B		Correlations		
	B	Std. Error				Lower Bound	Upper Bound	Zero-order	Partial	part
1 (constant)	-3372.568	6870.086		-.491	.624	-16971.483	10226.346			
Is the shop registered?	1710.767	6956.431	.013	.246	.806	-12059.062	15480.595	.065	.022	.013
How much income tax does your business pay?	2.292	.154	.803	14.925	.000	1.988	2.596	.803	.803	.801

- a. Dependent Variable: Q 55 How much sales do you do per day?

$$\hat{Y}_i = b_0 + b_1d_1 + b_2x_2$$

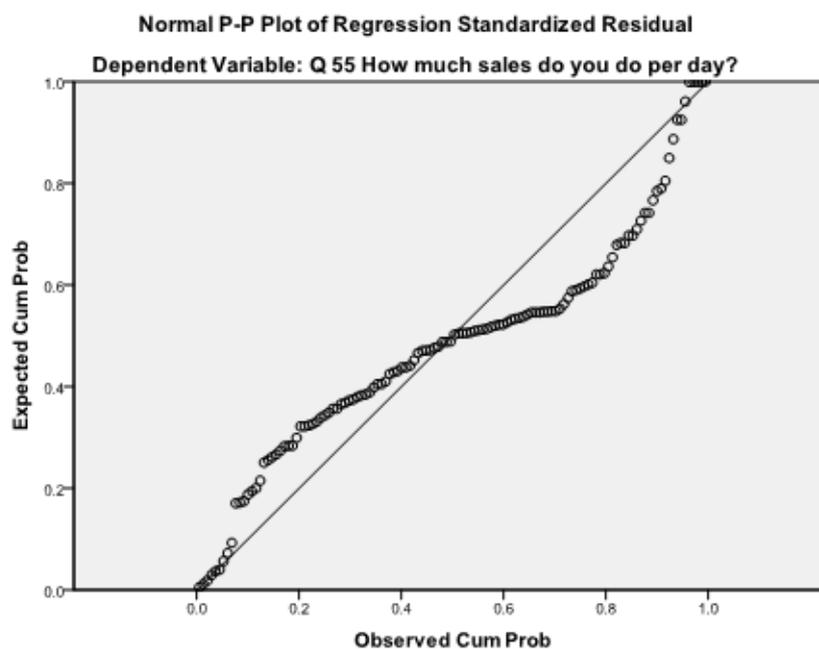
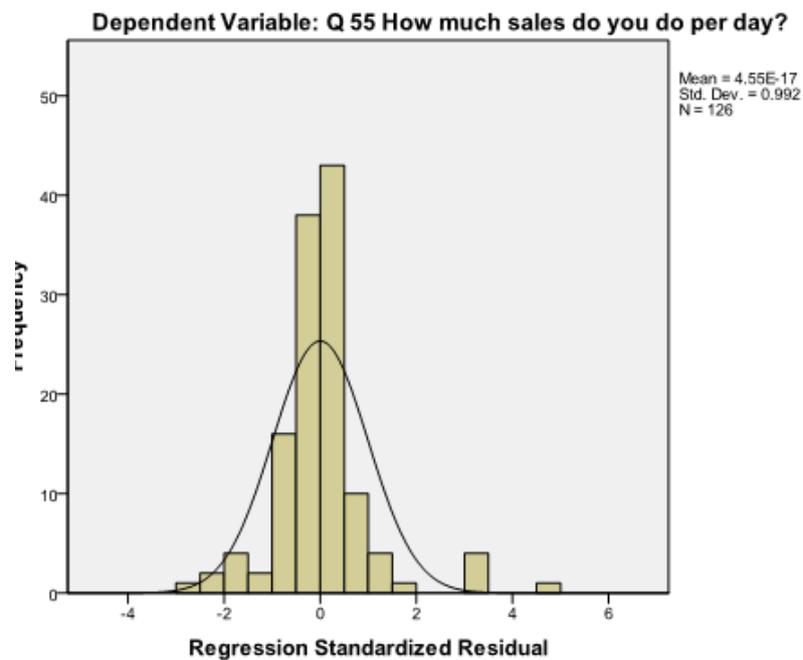
Where b_0 = constant, $d_1= 1$ if the shop is registered, $d_1=0$ if the shop is not registered, $b_1=$ the coefficient of the dummy, b_2 =coefficient of x_2 , $x_2=$ the amount of tax paid per month, $\hat{Y}_i=$ the average sales per day

² Based on estimated calculation of our research and estimations of Association of Retailers, Nepal.

The obtained equation is

$$\hat{Y}_i = -3372.568 + 1710.767d1 + 2.292x2$$

This equation shows that, if the shop is registered (at at least one of the four institutions required by law), it results in an average increment in daily sales is by NRs.1710.767. In addition, the increment in daily revenue per Nepalese Rupee tax paid to the government is NRs. 2.292. This is not a casual relation, but this correlation was obtained. The data residual is more or less normal and it is not skewed.



Standardization

Other than tax related compliance, *Kirana Pasals* are required to adopt mandatory standards defined by Nepal Standard (Certification) Act, 1980 and Nepal Standard (Certification) Regulations 1983. Quality, quantity and price standardisation have pertinent issues for *Kirana Pasals*. Sales of expired product, under weighing goods and mislabelling are some quality control issues that have received much media attention. Many Kirana Pasal owners come under the states regulatory premise on issue of standardization. It has also been pointed in our consultations that out that poor monitoring of standards higher up in the value chains, that is with the supplier and manufactures, are partially to blame for this.

Meet the owner of Milky Way Shopping Mart (Shankhamul, Kathmandu). Having returned after working at a retail store abroad for over five years, this entrepreneur expresses that he did not face a lot of challenges on the investment side due to his own savings. Although there are a lot of regulatory procedures to go through, he duly went through all of those.

However, he shared an encounter he had with a bureaucrat at his own store. He recalled that a lady from one of the monitoring departments walked into his shop and asked for special discounts. When she was denied of such preferential treatment, she said that she worked with the monitoring office and even threatened to send a monitoring team just because the storeowner did not yield to her initial request. The storeowner refused to offer her any special treatment. From this experience, this entrepreneur drew a conclusion that the regulatory body is always looking to take unfair advantage of the entrepreneur like himself and re-iterated that they have created such a business environment where small and medium entrepreneurs just cannot make a decent living. It is very hard to even lawfully toil in Nepal, he added.

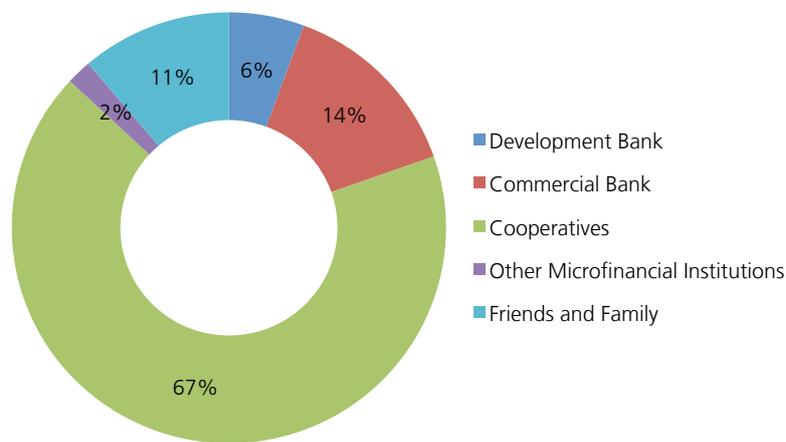
Standardisation is used an excuse to persecute *Kirana Pasals* on every aspect possible. Government standardisation includes weights, packaging and even published price list. This is often used as a measure whenever there is a political pressure from consumer groups after a bout of inflationary pressure. As a populist symbol of doing something, the government first tends to target the most accessible victims, Kirana Pasal owners, to pass the blame to these 'evil middlemen' who are apparently causing the inflation. Examples of the beaten rice case and the published price display case cited above aptly demonstrate this phenomenon.

Labour regulations and environmental regulations are other regulations that apply to MSE. However, most *Kirana Pasals* in the study did not employ help and generally had family members working in the shops without remuneration. Very few employed one or two people. Hence, labour regulations generally did not apply in the study.

Access To Finance

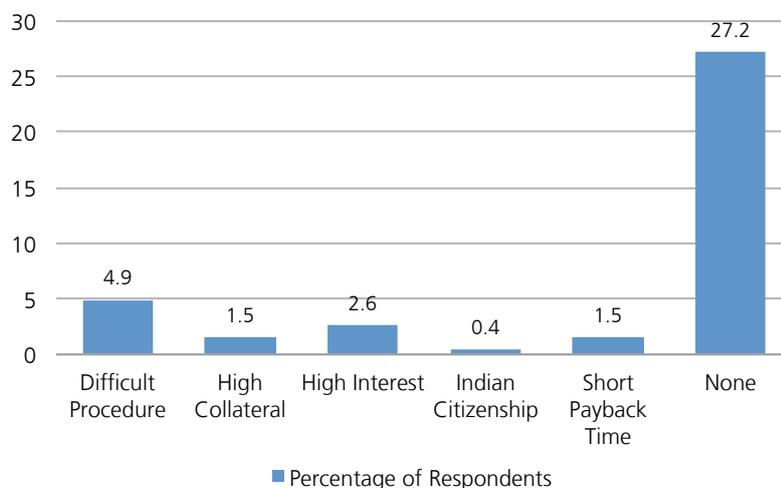
The main source of capital for *Kirana Pasals* is micro finance institutions, particularly part of the cooperative model. The popularity of such micro finance

Fig. 9: Most Approached Financial Institutions



institutions can be credited to the ease with which one can become a member of such institutions and get access to small capital. 71% of respondents in this stated that they had no problem getting access to capital. This can be contributed to the ease with which small entrepreneurs could gain access to (limited) capital from microfinance institutions. Cooperatives do door to door marketing where they approach small enterprises to become members. The industry is built largely on personal relations and community trust, and deals with relatively small amounts of capital. The procedures to become members are relatively simple, and once member, getting access to loans from the institution is easy. Deposits are collected in person from the stores daily. Members are eligible to draw loans up to three times of their cumulative deposits without collateral or any further documentation. Maturity of the loan is negotiated when applying for the loan and repayments are done in installments with flexible payment. Of those respondents that stated they had some difficulties in acquiring loans, they highlighted difficult procedure, collateral and short payback time as three main problems.

Fig. 10: Problems Faced While Acquiring Loans



The institutions favour shorter maturity as they get to collect more fees from increased turnover of loans. Almost 50% of the loans that were acquired for cooperatives had maturity of less than 1 year. Of the total loans acquired by respondents in the survey, 87.9% were short terms loans ranging from 1 year to 3 years in maturity. As the loans acquired by Kirana Pasals are largely small in amount, this short maturity does make sense. However, an interesting point to note is that for medium to long-term loans, commercial banks were more favoured to cooperatives or other financial institutions. This indicates that though micro financial institutions are better suited for short term loans, commercial banks would be the preferred option for larger loans with longer maturity that are required for growth.

Cross tabulation between whether or not an entrepreneur has acquired a loan and how much interest is paid

	How much interest rate did you pay?					Total
	Less than 5%	5-10 %	10-15 %	15-20 %	More than 20 %	
Have you ever taken a loan? Yes	4	4	18	56	12	94
Total	4	4	18	56	12	94

Here we can see that majority of respondents who had taken the loan were paying excessively high interest rates. As much as 59.5 % of the respondents who took loans were paying interest rates ranging from 15% to 20%.

Cross tabulation between whether or not an entrepreneur has acquired a loan and wherefrom

	Aggregate of labeling					Total
	Development Bank	Commercial Bank	Cooperative	Micro finance	Family and friends	
Have you ever taken a loan? Yes	4	4	18	56	12	94
Total	4	4	18	56	12	94

Upon further analysis, we can also see that majority of respondents take loans from cooperatives. As much as 67.8% of the respondents were found to be acquiring loans from cooperatives.

Cross tabulation between whether or not an entrepreneur has acquired a loan and the duration of loan

	What was the duration of the loan?				Total
	Less than 1 Year	1-3 Years	3-5 Years	More than 5 Years	
Have you ever taken a loan? Yes	58	29	4	8	99
Total	58	29	4	8	99

The above table shows that most respondents acquired short term loans whenever they did. This can be explained by the fact that most respondents also took loans from cooperatives. While 67.8% of the respondents acquired loans from cooperatives, these loans were found to be acquired for very small time periods. Cooperatives normally give out loans for short term periods, extending as much as one year. In the mean time, they also charge some of the highest interest rates on the loans they avail to small and medium entrepreneurs, because of the risks associated with the loans and relative ease of access to their funds. As much as 58.6% of the respondents acquired loans for a period of less than one year.

Micro financial Institutions (MFI) have been growing in Nepal in the last two decades. There are numerous MFIs in Nepal now and microfinance services are provided by large institutions like Grahmin Bikas Banks to smaller Financial Intermediary Non-Government Organisations to community level Savings and Credit Cooperatives. Large multinational institutions like the Asian Development Bank and United Nations, World Bank have been engaging in increasing access to funds for MSMEs through micro finance by wholesale lending. Wholesale lending institutions like Rural Self Reliance Fund, Rural Microfinance Development Centre Ltd., and Sana Kishan Bikas Bank Ltd. Commercial Banks are also a major source of funds for microfinance institutions. Commercial Banks, Development Banks and other Financial Institutions are required by the Nepal Raystra Bank to lend 4.5%, 4% and 3.5% of their loan portfolio respectively to the deprived sector (mostly made of micro and small enterprises) at a concessionary rate. These financial institutions can fulfil those commitments through direct lending to the 'deprived sector' or through wholesale lending to micro financial institutions (Shrestha 2009).

Ms. Pramila Shrestha here is 36 years of age. She has been running a store for 10 years now. She has four members in her family, but she runs the store alone. Her husband used to be a security guard at an office before, but he is currently abroad on foreign employment. She has two school going kids. Since it was hard for her husband to sustain himself on his salary, Ms. Shrestha's income from the store is pretty much the only source of income for the family. Upon asking why she started the store, she said that in the absence of her husband, and no source of income whatsoever, it was getting really hard to feed the children. So she had to come up with a business. Before that, she used to work on wage basis. She sells grains and fruits now. Grains really don't earn all that much. But fruits cover for that a little. She earns 5-10% profit on fruits in an average. Her store is not registered. She has no answers to why her store was not registered. Since she has no access to finance, she cannot expand her business further. There is a lot of competition in the market, too. She adds that since she mostly sells fruits, her goods get damaged if not sold soon. She explains that because there is no way to hedge against that risk, she doubts if her store is ever going to expand. Besides, she has to give away sizeable portion of her hard-earned income to beggars and political mafia that show up every now and then. She doesn't have a lot of faith in the government. "Politicians do not really care about what happens to us," she says. Having said that, she believes that women should be able to earn a living for themselves, no matter what.

The capital available from micro finance institutions are limited and often more expensive than loans from commercial banks and other financial institution. While loans from commercial banks charge an interest of 12 to 15 percentage, loans from micro finance institutions cost within the range of 20 to 30 percentage and in some instances even go higher. The reason for this financial gap seems to be two fold. Firstly, the procedures to get access to loans from banks and financial institution require various documents that are rather complex for small entrepreneurs to produce. Banks require documents like business plans, balance sheets, rental contract, letter of approval from municipality, tax documents, asset valuation and so on. Since most owners/manager of *Kirana Pasals* have limited capital and little formal education in business, documents like business plans, balance sheet are hard to produce. Those that operate their stores from rented property don't have formal rental contract and work largely on an informal basis with their landlords. The landlord often would not have undertaken proper procedures and received proper authorisation to rent out the property. As most of these stores often don't function in a fully formalised manner, they face problems in presenting many of these documents. Getting asset valuation is an equally time and cost consuming procedure. The problem of complex documentation is further coupled by the requirement of collateral. The owners are required to produce personal property as collateral. 75% of all loans acquired by our respondents required personal property to be placed as collateral. We found this to be particularly true with smaller stores that don't have much personal property to draw on in the first place.

Secondly, commercial banks are more reluctant to hand out loans to MSEs as the cost of loaning to MSEs in relation to the capital loaned is higher than that of large firms. Due to small loan amounts, high administrative costs and high risks, financing MSEs directly is unattractive to Commercial Banks. Instead they prefer fulfilling their deprived sector lending obligations by engaging in wholesale lending to MFIs such as Financial Intermediaries Non-Government Organisation and Microfinance banks that are registered with Nepal Rastriya Bank (Central Bank of Nepal). Commercial Banks often tend to prefer paying fines rather than fulfilling these obligations to lend to MSMEs. Other incentives include procurement preference for MSMEs but the implementation of this provision is almost non-existent (ILO 2005). Provisions of priority sector loans for micro and small enterprises are issued by Nepal Rastriya Bank to increase access to finance for MSMEs through Commercial Banks. These provisions have failed to be effective as commercial banks prefer paying fines to lending to MSMEs and increased access to finance through wholesale lending are limited by the effectiveness of microfinance as a model to provide capital to MSMEs and the effectiveness of the microfinance institution itself.

Corruption

In Transparency International's Corruption Perception Index, Nepal was ranked 139/176 countries in 2012 (Transparency International 2013). Nepal scored 27 out of a 100. These poor scores are reflected in the concerns raised in our consultations about bribery that *Kirana Pasals* are forced to partake in, particularly during the process of formalisation. According to Klitgaard (1988) (as cited in Safavian, Graham & Gonzalez-Vega, n.d.), corruption in most countries is attributed to a substantial amount of discretionary power exercised in carrying on the work of a modern administration. With regards to the multitude of regulations *Kirana Pasals* have to comply with, Buckberg, (1997) argues, the lack of clear, published requirements facilitates corruption because applicants cannot independently verify the requirements for approval.

The concerns for *Kirana Pasals* were not so much large bribes to high officials, rather numerous petty bribes to low level officials. It was noted that, when undertaking official work, Kirana Pasal owners were required to pay 'tea money' to low-level officials to get the processes done. From the survey data however, we found that only 2% of our respondents engaged in bribing government officials. This runs contradictory to popular discourse.

Table 4: Involvement in Bribery

	Frequency	Percent
Yes, have paid bribes	5	1.9%
No, have not paid bribes	258	96.3%

Notwithstanding some response inaccuracies due to the reluctance to divulge correct information regarding partaking in bribery, the limited number of official process these shops undergo could account for the low involvement in bribery of government officials. As many of these shops are registered with at least one authority, this data would indicate that incidence of bribery during registration, that is, during the process of formalisation and with law enforcement bodies is low for *Kirana Pasals* in the Kathmandu Valley.

Barriers To Exit

Ease of exit from a venture that has gone bad can be as important as ease of entry when a bankrupt person or an insolvent company and its directors wish to "wipe the slate clean" and restart in another capacity (FIAS & SEDF, 2007). Hence, barriers to exit are also barriers to growth, which retailers in Nepal have to face. The World Bank's Doing Business Report 2013 ranks Nepal 121st in the world in terms of ease of closing

a business. As per the report, a firm heading towards insolvency can expect to lose 5 years of time, 9% of the estate as costs and a gain of less than 25%. They could close up operations but they would still officially be active. This also creates problems in keeping up to date information on these stores. Since it is more difficult to exit the business, this serves as a major barrier to registration of *Kirana Pasals*. If it is very difficult to get out of the business, there is no incentive to register the business in the first place.

Others

Number of support services have been developed to assist MSMEs in training, marketing, credit and technologies services. Most of these services operate in rural areas and thus many of these services are not available to *Kirana Pasals* in the Kathmandu Valley. Some successful initiatives are Micro Enterprise Development Program, Federation of Nepalese Cottage and Small Industries, Small Industries Promotion Program, multiple microfinance services, and District Chamber of Commerce and Industries. Cottage and Small Industry, and Cottage and Small Industries Development Board (CSIDB) have been involved in providing business development services aimed at improving business skills of MSE entrepreneurs. A number of private organisations have also been involved in providing managerial skills to micro entrepreneurs. Donors such as UNDP have also assisted programs and projects like MEDEP. MEDEP is one of the few programs that have aspects of marketing in their projects. Many programs don't have marketing aspects aimed at promoting MSMEs good and services. Even those organisations that promote MSEs focus on cottage industries and industrial enterprises. There are a number of governments, non-government , and community based programs aimed at promoting socially and economically deprived groups (ILO 2005).

Stuti mini-mart, in Thapagaon, Kathmandu, is one of the rare success stories in Nepalese consumer goods market. Having put to test on all aspects of doing business in Nepal, the store now boasts three outlets in different parts of the city of Kathmandu. Mr. Hemant Dangol, the retail manager at the mart expresses the non-existence of any support institution or representative association for the start-ups in the country. He expresses that Mini-marts require a high initial investment and the operating cost is very high, while return on investment is low. The only relief that a mini-mart can enjoy comes from the fact that they practice bulk buying, which makes it easier for them to get supplies on credit. In order to garner profit, it is important for them to be able to change the consumers' habits and make them realize that buying in Mini-mart does not mean that the price of products will necessarily be costlier. This very fact, Mr. Dangol iterates is very hard to communicate to the Nepalese consumers as they firmly believe that mini marts are high-end and overprice the goods they sell. Although he admits that his business in particular did not face a lot

of challenges while acquiring initial capital, he does feel that there are a lot of regulations that have to be complied with. He reflects upon all the market research that were conducted prior to opening up the store and admits that it is very hard for ordinary Kirana Pasal owners to carry out such researches and thus, when they make a leap from Kirana Pasal to mini-marts, they may suddenly find that it is neither as easy nor as profitable as being just a Kirana Pasal.

Besides the above-mentioned challenges, the overall business environment of Nepal stands as a challenge to many small shop owners and one of those issues is frequent strikes that take place. Samriddhi Foundation & FNCCI (2013), state that there were 57 bandhs (general strikes) during September 2012 – August 2013. All businesses are forced to shut down and transportation is not allowed by protesting political groups who using violence for enforcing such bandhs. Problems of improper documentations higher up in the value chain also create challenges for retailers like Kirana Stores as they in turn would not be able to produce proper documentation for the authorities.

Mr. Saroj Thapamagar is the owner of 'Saroj Store.' He has been running the store with his mother for the last 3 years. Both his sisters are students, while his father works abroad. The store supplements the money that the family receives via remittance. They bought a small Kirana store in the neighborhood as an investment. The store runs from 5:30 in the morning to 8:30 in the night. On an average, he sells around Rs. 7000 worth of goods a day and earns 5% profit in it. Among the goods he sells, due to high volume of sale, he says that grains earn him the highest. That aside, bottled water is the other commodity that earns a sizeable profit. His store is not registered. He says that the house owner suggested him not to register the store, as it really does not matter whether or not it is registered. He has a plan to expand the store in the future if he sees it feasible. He finds strikes as the major hindrance to such storeowners. He earns absolutely nothing during strikes. To add to that, policemen do not allow opening the stores till late in the night. Sometimes, the police even show up drunk and start verbally abusing people like him.

In addition to problems mentioned above, our findings suggest that most *Kirana Pasals* in Kathmandu Valley don't have either access to or knowledge of support services. Findings from our consultations with experts suggest a stark void of these services for *Kirana Pasals* in the valley. This could be because most of these services are focused on MSEs in the manufacturing sector and operate in rural areas. However in

regards to getting help from the government or courts to deal with problems like bribery and extortion, only 50 % of our respondents said they could get such help. This indicates weak legal support to these enterprises. In addition, we found that support from the community still plays a larger role than the support provided by the government or other institutions.

The lack of support services in setting up mini markets or departmental stores make it more difficult for *Kirana Pasals* to grow into vertically into bigger stores. The buying behaviour of the lower income group (where due to cash flow problems often purchase in credit), and the 'premium' perception of department stores might not make vertical expansion attractive for Kirana Pasals as they would lose a large chunk of this segment. Poor economic growth that stifles demand of more premium goods could also make departmental stores less attractive option for growth. In addition to that, many of the problems that plague Kirana Stores, like access to finance and lack of incentives and collective promotion also affect mini marts and small department stores.

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PART IV

RECOMMENDATIONS

Based on this preliminary analysis of *Kirana Pasals* in Kathmandu, the regulatory environment pertaining to registration, taxation and standardisation are immediate areas of concern. In a country that practices progressive taxation and espouses the values of 'social justice' it is ironic to see the most vulnerable strata of entrepreneurs being victimized by regulations and bureaucracy simply to achieve populist ideals of 'doing something about middlemen and inflation'.

Therefore, based on the research and analysis presented forward, we propose the following recommendations that are easy to follow and implement:

1. What Are *Kirana Pasals*?

The biggest regulatory burden perhaps stems from the fact that there is no clear definition in the regulatory regime of what constitutes a 'Kirana Pasal'. Therefore, any reform geared towards *Kirana Pasals* growth needs to start with a clear definition of what constitutes a 'Kirana Pasal'.

2. Where To Register?

The second step in reform requires defining a one agency that records the registration of *Kirana Pasals*. The fact that these agencies require to register in multiple agencies naturally render them informal even if they are registered with any one particular agency. Such an agency should be a decentralized body such that *Kirana Pasals* have an easy access to it. Any other government agency that requires this information can easily tap into the database of this one agency. In Nepal, the Municipality in urban areas and the Village Development Committee (VDC) in rural areas seem to be the most feasible option under the current governance structure. As long as the registration requirement is limited to being registered with this one particular agency, it would be easy enough

for these entrepreneurs to understand and comply. This would also make them formal thereby rendering them the benefits of being a formal enterprise.

3. How Much To Pay As Taxes?

The taxation regime currently in place seems to be in conflict with itself. While a plethora of regulations under income taxation requires *Kirana Pasals* to be tax exempt, another regulation requires them to pay 3.5 percentage of their income as tax. During the course of this research many shop owners expressed willingness to follow tax regime if it were simplified. Therefore, reforming the tax code and reducing it to simply have all *Kirana Pasals* pay 1 percentage of their annual profits for as tax would widen the tax bracket and also help *Kirana Pasals* operate legally. This kind of regime can be administered through the Retailers' Association such that the tax procedure is simple and facilitated by the association and any kind of shopowner can comply without having to hire brokers and lawyers to deal with the taxation complexity that exists today. This would also facilitate their growth.

4. What Standards To Follow?

Kirana Pasals that we reached out during this research were also happy to comply with standards as long as they were rational standards. It would be highly presumptuous to imply that a government bureaucrat who has never operated a Kirana Pasal would be better able to fix standards for *Kirana Pasals*. Therefore, Retailers' Association which is more than happy to take up this job could function as a voluntary standards organization and issue certification to *Kirana Pasals* that are willing to comply with its' standards. This would benefit the consumers in providing them with assurance on the quality of the product they are buying at the price that they are willing to pay and also decrease the arbitrariness of persecution based on random standards set by bureaucrats.

5. Where To Get The Investment To Grow?

One of the primary issues of concern for *Kirana Pasals* is access to finance for being able to expand. In order to deal with this problem, one area to work in is to ease up regulations to establish insurance for *Kirana Pasals*. The Cooperative Model is a round-about way of approaching this problem. However, if the insurance industry regulations eased up, the risk associated with this sector would also be minimized. This would then provide an incentive for commercial banks to enter this market and provide loans on the basis of business plans rather than on collaterals. This requires reforming

the regulation of directive lending as well which is not necessarily achieving any of its intended consequence but instead is perversely providing added benefits to micro finance institutions which do not get transferred to the ultimate beneficiaries that it is intended for.

6. How To Exit?

Exit rules need to be simplified especially those pertaining to tax. The *Kirana Pasals* should be able to exit with relative ease as they have very less assets and should have the provision to declare bankruptcy when the enterprise fails. This would allow these entrepreneurs to move on from sunk enterprises while freeing up resources in the economy. This requires a major overhaul in the exit regulation in Nepal.

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AN INTRODUCTION SAMRIDDHI, THE PROSPERITY FOUNDATION

Samriddhi, The Prosperity Foundation is an independent policy institute based in Kathmandu, Nepal. It works with a vision of creating a free and prosperous Nepal.

Initiated in 2007, it formally started its operations in 2008. The specific areas on which the organization works are:

- Entrepreneurship development
- Improving business environment
- Economic policy reform
- Promoting discourse on democratic values

Centered on these four core areas, Samriddhi works with a three-tier approach—Research and Publication, Educational and Training, Advocacy and Public Outreach.

Samriddhi conducts several educational programs on public policy and entrepreneurship. It is dedicated to researching Nepal's economic realities and publishing alternative ideas to resolve Nepal's economic problems. Samriddhi is also known for creating a discourse on contemporary political economic issues through discussions, interaction programs and several advocacy and outreach activities. With successful programs like "Last Thursdays with an entrepreneur" and "Policy Talkies" it also holds regular interaction programs bringing together entrepreneurs, politicians, business community, bureaucrats, experts, journalists and other groups and individuals making an impact in the policy discourse. It also hosts the secretariat of the 'Campaign for a Livable Nepal', popularly known as Gari Khana Deu.

One of Samriddhi's award winning programs is a five day residential workshop on economics and entrepreneurship named Arthalya, which intends to create a wave of entrepreneurship and greater participation among young people in the current policy regime.

Samriddhi is also committed towards developing a resource center on political economic issues in Nepal called Political Economic Resource Center (PERC) currently

housed at Samriddhi office. It also undertakes localization of international publications to enrich the political economy discourse of Nepal. Samriddhi was the recipient of the Dorian & Antony Fisher Venture Grant Award in 2009, the Templeton Freedom Award in 2011 and the CIPE Global Leading Practice Award in 2012.

(For more information on the organization and its programs, please visit www.samriddhi.org)

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