

## Challenge Brief

### **Rationale and Objectives:**

The Cottage, Micro, Small, and Medium Enterprises (CMSMEs) sector is the largest segment of the economy in Bangladesh, accounting for 25% of our GDP<sup>1</sup> and creating employment for 7.8 million<sup>2</sup> people directly. Despite much support from the government and private sectors, the CMSMEs sector, especially in rural settings, faces several challenges in starting and growing their business. Limited access to finance has been one of the core impediments to the sectors' growth. Systematic use of digital financial services (DFS) and technology solutions in underserved markets can help grow CMSME sector. This challenge fund aims to support startups and incumbents with innovative digital solutions to improve financial access for CMSMEs by addressing the challenges they typically face, especially cottage and microenterprises in a rural setup.

### **Problem Statement:**

CMSMEs, especially cottage and micro-enterprises, including agriculturists, face great difficulty accessing financial facilities from formal financial institutions such as banks and NBFI. Only 28.4% of the 8.1 Mn CMSMEs are being served by the existing formal financial channel<sup>3</sup>. The problem goes beyond the formalization of CMSMEs, and there are limitations on both the CMSME and the financial service providers' ends. The country's CMSMEs get access to only one-third of the fund they need for running businesses, while rural entrepreneurs receive only 19% of the funds disbursed. According to recent studies, 99% of all business units in Bangladesh are CMSMEs, and 94% experienced a significant loss in 2020 due to the COVID-19 pandemic<sup>4</sup>. While the government supported entrepreneurs with a generous stimulus package, the finance ministry noted that only 10.8% of this went to cottage and micro-enterprises. A DCCI study found that 59% of CMSMEs found the stimulus application and disbursement process complex. Multiple studies point to the following barriers faced by the CMSMEs to access financial facilities:

- Lack of identity and necessary business documents
- Complexity in application and disbursement process
- High operational cost of the financial institutions for processing small amount loans for CMSMEs
- Little or no data exist for credit assessment of CMSMEs
- Lack of digital footprints of CMSMEs

### **The Challenge**

There is a need for innovative digital solutions which will help CMSMEs get better access to finance, lower their cost of capital, and steer away from exploitative, high-cost, informal

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<sup>1</sup>Bangladesh Bureau of Statistics (BBS)

<sup>2</sup> SME Foundation

<sup>3</sup> LightCastle partners 2021

<sup>4</sup> IFC 2020, MicroSave Consulting 2021

loans. In this solution, the FinLab BD, through a challenge for startups and incumbents, invites marketable solutions enabling CMSMEs to access a formal financial system.

### **Outcomes/result:**

1. Increase the accessibility of CMSMEs in the formal financial system
2. Reduce operational cost of CMSME financing through digital solutions
3. Increase the percentage of CMSME financing to facilitate Significant growth in CMSME financing

### **Overall Program Design for Challenge Fund**

A2i Innovation challenge fund is a yearly, cohort-based program that consists of three consecutive phases:

- Pre-Acceleration Program
- Acceleration Program
- Implementation Phase

Pre- Acceleration program consists of a Bootcamp and follow-up session. The expected output of this process is to identify the right startups and incumbents for taking them through the Acceleration Program. We will begin the application and selection process before starting the pre-acceleration program. The selection process will begin with the collection of applications and idea shortlisting. After receiving the applications, the preliminary screening, analyzing, and preparing a report to mention the rationale for selecting the application. The top 10 applications will participate in the Bootcamp to prepare a complete business plan and pitch. The selected applications will pitch their solution on the pitch day, followed by the Bootcamp and mentoring session. After the technical evaluation by experts, we will select the top three pitches for the Acceleration Program.

Those startups and incumbents that complete the Pre-Acceleration program and are successfully selected for the Acceleration program will receive training and mentorship dedicated to the specific needs of the challenge. In this stage, the three winners will sign an agreement paper and receive equity-free (grant) funding up to BDT 10,000,000 (maximum up to US\$100,000).

During the Implementation Phase, startups work closely with national market enablers to implement their solutions/products.

The schedule of this cohort program is as follows-

