

# Overall Economic Development of Bangladesh through SME Banking : A Comparative Study

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## Abstract

*SME financing is now constructing the economy building of the country with the major key role players of banking industry which will appear advanced in near future. Our major objective is to identify the contribution of banks in the development of SME sector. The study found out the current status of banks in the development of SME sector. By preparing the report the researchers gained depth knowledge about SME banking. The paper was drawn some recommendations to improve the activities of the bank, especially credit process review. The target population was total 47 banks currently operating in Bangladesh, 43 banks are commercial banks and 4 banks are specialized banks. Out of 43 commercial banks, 30 banks are Private commercial banks, 4 banks are state owned commercial banks and 9 banks are foreign commercial banks and total number of SMEs near about 79754 establishments, of which 93.6% are small and 6.4% are medium. For conducting research it was clearly revealed that the randomly chosen 24 SME entrepreneurs and 6 commercial banks (both Government and private) which represent around 21.27% of the total commercial banks. To select the sample, convenience sampling method was used in order to minimize bias. Our total sample size is 24 SME entrepreneurs and 18 bankers.*

**Keywords:** *SME, SME Financing, Banks, Economic, Development, Bangladesh.*

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## 1. Introduction

SME means Small and Medium Enterprises. Small & Medium Enterprise (SME) plays a pivotal role in the economic growth and development of a country. Actually, SME works as the platform for job creation, income generation, and development of forward and backward industrial linkages and fulfillment of local social needs. SMEs occupy a unique position in the economy of Bangladesh. Mainly private sector development depends on them. In Bangladesh the SMEs account for about 45% of manufacturing value addition. They account for about 80% of industrial employment, about 90% of total industrial units and about 25% of total labor force. Their total contribution to export earnings varies from 75- 80%. The total number of SMEs is estimated at 79754 establishments, of which 93.6% are small and 6.4% are medium which contributed around 20-25% of GDP. Small and medium enterprises (SMEs) make up the largest portion of the employment base in many developing countries and, indeed, are often the foundation of the local private sector. Now the SMEs are not only concentrated to low-tech, traditional, and agro-based economic activities; these are spread over other non-traditional manufacturing and service sector as well. In fact, the SMEs are recognized as locomotive of economic growth worldwide. To achieve high and sustained economic growth, a triggering force is mandatory to exit from endemic poverty and socio-economic deprivation. The entrepreneurs behind could—and should—play a much larger role in development, but too often are held back by a lack of ready access to financing from local formal sector financial institutions. Here lies the scope of commercial banks to offer banking facilities to this ‘missing middle’ by offering different products that are specially featured for this segment. On a long term perspective these commercial banks expect to gradually develop the creation of an entrepreneurial class across Bangladesh through proper financing and training. Commercial banks are also developing their procedure and operational guideline supported by structured recruitment process and subsequent training with a view to mitigating credit risks and 10 other risks for a smooth flow of SME financing. Most businesses in Bangladesh are in need of small short-term loans to help finance their working capital needs or purchase of fixed assets. So when a bank brings about a momentous difference in these peoples’ lives by meeting their demand, the bank is more than a bank. It’s a promise - a promise to rise against all adversities; a promise to quality livelihood; a promise to endow ordinary people with extraordinary opportunities.

## 2. Literature Review

SMEs have been identified as a thrust sector for developing economies with hugely available cheap labor - by economists around the globe as well as in Bangladesh as early as the late 1970s and early 1980s - to meet the diverse needs of a complex, growing, economy and polity, especially following the failure of large industries in the Western model to provide fast economic growth to these countries in the decades following World War II. SMEs are mainly

dependent on labor resources, simple technology, dispersed widely and flow out of the traditional skills of the people. They provide not only an economic solution, but a social and cultural solution as well. People of the country become less dependent on alien sources, their instinct of self-reliance are strengthened, which leads to internally-stimulated growth rather than externally propped-up progress. For a country like Bangladesh, SMEs can generate employment, especially in the rural areas where 88 per cent of all enterprises are SMEs, and can trigger an exit from the vicious cycle of poverty. It is pertinent to remember that two of the fastest growing economies in the world, India and China, had for years invested in SMEs through various financing, training, and protective mechanisms to foster the growth of the economy. These countries now enjoy the fruits of such foresight, thanks to these SMEs slowly graduating to large global industries. Unfortunately, there has been little work done in the country to provide support and incentives

18 for the growth of the SME sector, in spite of having similar competitive advantages in terms of labor. The government came up with an SME Policy as late as 2005 and constituted the SME Foundation in 2007. Bangladesh's fiscal and monetary policies, regulatory regimes, are still not conducive to SMEs and are more often geared towards large industries and in some cases foreign investment, which many economists would argue, do not always operate in national interest.

### **3. Objectives**

The objectives of the study are:

- To find out the reality in the SME financing at commercial Banks of Bangladesh.
- To find out the problems & prospects of SME under the Commercial Banks.

### **4. Methodology of The Study**

Methodology is the most important component in any study since it explains the procedures and methods through which a particular study will be carried out. Data are the raw materials for any study. Relevant data for the proposed research study were collected from both secondary and primary sources. Secondary data were collected from the annual reports (2011) of the selected Government & non-government banks, Bangladesh banks reports on SME, Bangladesh banks website and from websites of the selected banks, SME Organization of Bangladesh. These data were reviewed and analyzed after collection. Primary data is mainly in 2(two) types- Quantitative and Qualitative data. Qualitative data mainly gathered by conducting some interviews with SME Bankers and selected SME Entrepreneurs. However, Quantitative data will get through conducting survey through selected Questionnaire. In-depth interview technique has been used because through this approach, the deep rooted issues regarding the problems have come out plus many factors that could stimulate growth of SME

were also figured out. This would not have been possible through any other technique. Following the qualitative research, the questionnaire was prepared for quantitative research. The questionnaire prepared for the interviews was structured and responses were quantified using rating scale.

## **5. Discussion & Analysis of the Study**

### ***SME Financing By Bank in Bangladesh***

Sonali Bank is disbursing significant amount of credit under various programs like Small Enterprise Development Project, Self-help Credit Program, and Projects for Small Entrepreneurs, Special Investment Program and Agro-based Supervisory Industrial Credit etc. for the promotion and development of SMEs. The investment of private sector banks in financing SMEs remains insignificant in Bangladesh. Of all the private sector banks, Pabuli Bank, Jamuna Bank Limited, Standard Chartered Bank Ltd, Prime Bank Ltd, Dhaka Bank Ltd, Mercantile Bank Ltd, Dutch Bangla Bank Ltd, Islami Bank Bangladesh Ltd, IFIC Bank Ltd. have the leading role in SME financing. Bank of Small Industries and Commerce Bangladesh Ltd. (BASIC) are entrusted with the responsibility of providing medium and long-term loans for promotion and development of small-scale industries. The memorandum and Articles of Association of the bank stipulates that 50% of loan able funds shall be used for financing small scale and cottage industries.

### ***Current Status of SME Financing by Banks in Bangladesh***

Janata Banks are disbursing significant amount of credit under various programs like Small Enterprise Development Project, Self-help Credit Program, and Projects for Small Entrepreneurs, Special Investment Program and Agro-based Supervisory Industrial Credit etc for the promotion and development of SMEs. The investment of private sector banks in financing SMEs remains insignificant in Bangladesh. Of all the private sector banks like Pubali Bank, Standard Chartered Bank, Agrani Bank, BRAC Bank, Eastern Bank Ltd. (EBL), Prime Bank Ltd, Dhaka Bank Ltd, Mercantile Bank Ltd, Dutch-Bangla Bank Ltd, Islami Bank Bangladesh Ltd, IFIC Bank Ltd. have the leading role in SME financing. Bank of Small Industries and Commerce Bangladesh Ltd.(BASIC) and other government and private banks are entrusted with the responsibility of providing medium and long-term loans for promotion and development of small -scale industries. The memorandum and Articles of Association of the bank stipulates that 50% of loan able funds shall be used for financing small scale and cottage industries. The outstanding credit of BASIC stood at 1505.06 crore at the end of June 2012 for small and cottage industries sector.

### ***Portfolio Size of Different Banks in SME Sector***

**Table-1** Portfolio Size of Different Banks in SME Sector

Serial No.	Name of the Bank	Portfolio Size ( In Percentage)		
		Year-2010	Year-2011	Year-2012
01	Sonali Bank	30.46	22.57	19.02
02	Janata Bank	47.47	50.39	53.03
03	Basic Bank	73.71	72.47	61.60
04	Jamuna Bank	4.00	20.19	4.82
05	Pubali Bank	7.48	5.14	11.50
06	Standard Chartered Bank	16.00	15.45	15.25

*[Source: Annual Report of Selected Commercial Banks 2010-2012]*

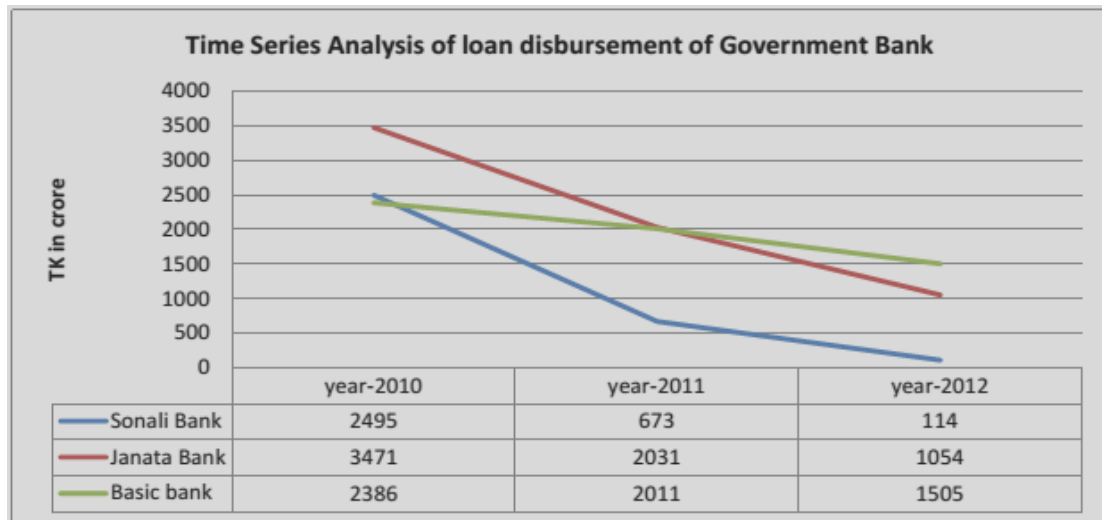
In 2010 Sonali Bank provide 30.46% of total loan in SME sector. Janata Bank provides 47.47% of total loan and Basic Bank provide 73.71% of total loan in SME sector. So we can say that Basic Bank spend more money in SME sector from their loan portfolio. This is the situation of government bank. Private bank also provide a great portion of loan in SME sector from their total loan amount. In 2011 Jamuna Bank provide 4.00%, Pubali Bank provide 7.48% and SCB provide 16.00% loan in SME sector from their loan portfolio.

In 2011 Sonali Bank provide 22.57% of total loan in SME sector. Janata Bank provides 50.36% of total loan and Basic Bank provides 72.47% of total loan in SME sector. So we can say that Basic Bank spend more money in SME sector from their loan portfolio. This is the situation of government bank. Private bank also provide a great portion of loan in SME sector from their total loan amount. In 2011 Jamuna Bank provides 20.19%, Pubali Bank provides 5.14% and SCB provides 15.45% in SME sector from their loan portfolio.

In 2012 Sonali Bank provides 19.02% of total loan in SME sector. Janata Bank provides 53.03% of total loan and Basic Bank provide 61.60% of total loan in SME sector. So we can say that Basic Bank spend more money in SME sector from their loan mix. This is the situation of government bank. Private bank also provide a great portion of loan in SME sector from their total loan amount. In 2011 Jamuna Bank provides 11.50% of total loan amount, Pubali Bank provide 4.82% of total loan and SCB provide 15.25% of total loan in SME sector.

#### ***Time Series Analysis of Loan Disbursement of Selected Banks***

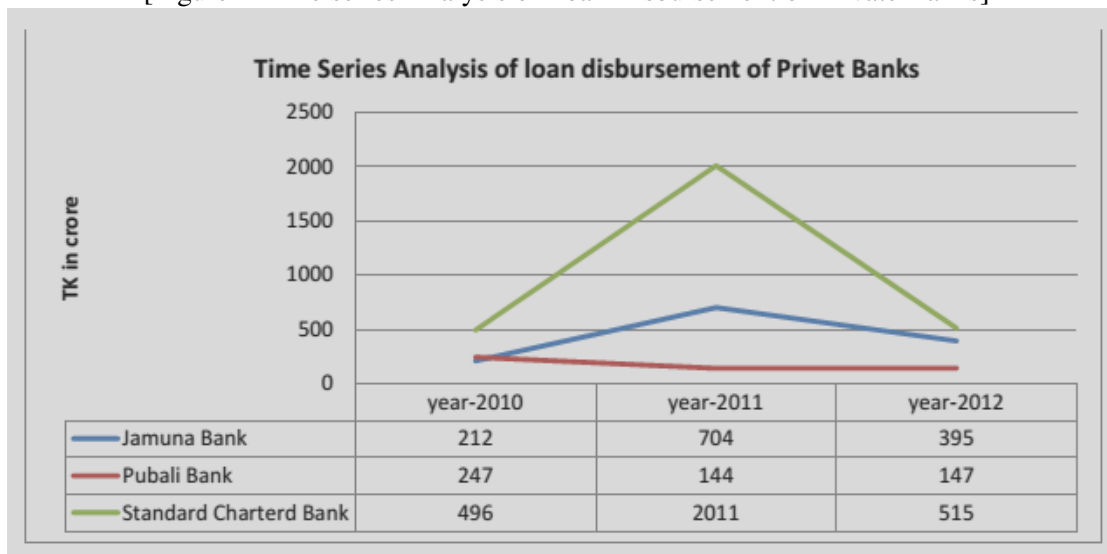
[Figure-1 Time series Analysis of Loan Disbursement of Government Bank]



[Source: Annual Report of Selected Commercial Banks 2010-2012]

Here we see that in 2010 loan distribution in SME sector of government bank was good but after 2010 it is decreasing day by day.

[Figure-2 Time series Analysis of Loan Disbursement of Private Banks]



[Source: Annual Report of Selected Commercial Banks 2010-2012]

Here we can see that in 2011 loan distribution in SME sector was increased but it is decreasing in 2012.

Table-2 Distribution of entrepreneurs whether or not they take bank loan to operate their SME

Whether or not take loan by entrepreneurs from banks	Number	Percentage (%)
Yes	15	62.5
No	09	37.5
Total	24	100

[Source: Survey of SME Entrepreneurs]

**Findings:** 62.5% that means a large number of SME entrepreneurs take bank loan to operate their SME business which is very remarkable. However about 3 out of 10 do not take bank loan to run their business.

Table-3 Distribution of entrepreneurs by their responses to the degree of satisfaction/dissatisfaction with the way of getting loan

Degree of Satisfaction/ dissatisfaction	Number	Percentage
Highly Satisfied	0	0
Satisfied	4	16.66
Neither Satisfied nor dissatisfied	16	66.24
Dissatisfied	4	16.66
Highly dissatisfied	0	0
Total	24	100
Weighted average score-3		

[Source: survey of SME entrepreneurs form Dhaka City]

**Findings:** A large number of entrepreneur's responses nighters satisfied not dissatisfied. However there are one out of five are satisfied. A sizable number of respondent are dissatisfied.

Table-4 Distribution of Entrepreneurs responses to what extent it is easy or tough to get SME loan from bank

	Number	Percentage
Very easy	0	0
Easy	3	12.50
Neither easy nor tough	20	83.33

Tough	1	4.16
Very tough	0	0
Total	24	100
Weighted average score-3.08		

[Source: survey of SME entrepreneurs form Dhaka City]

**Findings:** A large number of entrepreneur's responses neither easy nor tough to get SME loan from bank. However 12.50% people said that it is easy to get SME loan from bank. A sizable number of respondent said it is tough to get loan from bank.

Table-5 Distribution of Bank's contribution on financial and nonfinancial activities

Contribution on financial and non-financial activities	Number	Percentage
Financial activities only	12	66.66
Both financial activities only	6	33.33
Both financial and nonfinancial activities	18	100
Total	24	100

[Source: survey oon government and private banks]

**Findings:** Many banks near about four out of ten banks provide nonfinancial facilities like SME training, awareness program etc. and those are basically private bank. On the other banks six out of ten mainly public banks don't provide any nonfinancial activities.

Table -6: Distribution of Bank's contribution in SME sector

Bank's contribution in SME sector	Number	Percentage
Very much important	9	50
Very important	3	16.67
Important	3	16.67
Less Important	3	16.67
Not important	0	0



Total	18	100
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*[Source: survey on government and private banks]*

**Findings:** five out ten bankers agree that banks play a vital role in the development of SME sector in our country. One out of six said banks are very important in the development of SME sector and one out of six argues that banks have important contribution in SME sector.

## 6. Findings of the Study

- SME foundation claims that they disburse SME loan on single digit. Bangladesh Bank gives target to commercial bank to disburse loan on 10 Percent interest rates. But in reality Public banks give loan on about 14 to 15 percent and private banks give loan on about 18 to 19 percent.
- Bangladesh Bank and SME foundation claim that no collateral securities are needed for getting SME loan. But without collateral securities very few banks sanction SME loan to entrepreneurs.
- Banks are the major sources of finance for SMEs. More than 60 percent entrepreneurs receive loan from banks for their ventures.
- Bankers are not much interested on providing SME loan. As it requires continuous monitoring, much attention and more investment on less return than industrial loan. There is greater chance of SME loan to become bad loan than others.
- Banks are disbursing credit under various programs like Small Enterprise development project, self-help credit program, and projects for Small Entrepreneurs, Special Investment Program and Agro-based Supervisory Industrial Credit etc for the promotion and development of SMEs.
- The memorandum and Articles of Association of the bank stipulates that 50% of loan able funds shall be used for financing small scale and cottage industries. But in reality, banks are not in conformance with these principles.
- Many banks are facing problem to recover the loan amount provided in SME sector. For this reason, still many banks are not willing to invest much in this sector.
- From 2010, Bangladesh Bank gives target to government banks and private banks to disburse loan in SME sector. Since then it has got momentum. So Bangladesh Bank is playing a key role on SME loan disbursement.
- The target of government banks given by the Bangladesh Bank to provide loans in SME sector is normally more than the private sector.
- In general, government banks provide more credit facilities in SME sector than Private Banks.
- About 62.5% of entrepreneurs take bank loan to operate their SME business which is very remarkable.

- Banks near about two out of ten banks provide non-financial facilities like SME training, awareness program etc and those are basically private bank.
- Five out of ten bankers agree that banks play a vital role in the development of SME sector in our country.
- Foreign loan donation for SME sector remains idle for not proper disbursement of giving amount and other problems relate with the loan distribution.

#### **7. Recommendation**

- Bindings should be given by Bangladesh Bank to other commercial banks about loan disbursement on 10 percent or single digit interest rate. Otherwise, they have to face lawful action even.
- Commercial banks should consider SME loan as their Corporate Social Responsibility. So here consideration will not be profit maximization only rather social welfare.
- Banks can be inspired by giving award at the national level by the government as they provide more loans on SME sector.
- More non- financial facilities on SME sector can make the entrepreneurs greatly benefitted.
- Small & Medium Enterprise (SME) plays a pivotal role in the economic growth and development of a country. Actually, SME works as the platform for job creation, income generation, and development of forward and backward industrial linkages and fulfillment of local social needs. So SME loan disbursement should be given more emphasis at the context of Bangladesh.
- SME foundation can play more vital and proactive role by disbursing their loan through certain bank which will conform to their provision of single loan disbursement.
- Bangladesh Bank and SME foundation with taking other companies as ROBI Mobile phone can promote SME loan disbursement programs as many entrepreneurs are not much aware about the facilities.
- More rural people should be brought under SME loan facility coverage though it has the risk.
- Awards should be given at the individual level that will have contribution on SME loan disbursement and other activities of SME. As we can get a man like Nobel Laureate Dr. Muhammad Yunus of Grameen bank.
- Foreign donation for SME loan should be utilized with giving much emphasis as a greater amount of money stay idle and Donors cannot move forward with giving more money for this purpose as loan distribution amount is not at the satisfactory level.

## 8. Conclusion

SMEs are considered to be the seedbed for the development of entrepreneurial skills and innovation. Small capital requirement makes easy entry and exit possible and private sector entrepreneurial activities have many important spill over and positive externality effects. However, liberalization of the economy along with rapid globalization has posed several challenges to SMEs not only in international markets but also in the domestic economy. Since SMEs are based on relatively small investment, their survival depends on readily available markets with easy access. In today's world, market development is a much more challenging task, which requires coordinated efforts by individual business enterprises and the Government. Bangladesh has failed to maximize the benefits derived from the SME sector, which promises and needs to play a pivotal role in promoting and sustaining the industrial as well as overall economic growth. Banks are the major sources of financing for SME sector. Many of the banks are not interested to provide more loans in SME sector because sometimes they face difficulties to recover the loan amount. SMEs are the growing sector in Bangladesh and here is a great possibility to develop the socio economic condition through the development of SMEs. Banks have also a great possibility to extend their business by providing loan in SME sector.

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