

# Preparation of Performance of SME financing of commercial bank in Bangladesh- A Study on Eastern Bank Limited

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**Abstract**— The new buzzword in the banking industry, donor agencies, and even the government has been SME. Almost every bank in Bangladesh has an SME cell and new products and initiatives aimed at SMEs are a common feature in the business page of the newspapers. It would seem that financing these SMEs is guaranteed to pave the way for economic development in Bangladesh. Small & Medium enterprise development is a precondition for sustainable economic upliftment of a country like Bangladesh. It plays a dominant role for industrial development & provides employment facilities for work force. In light of its importance, Banks & other financial institution introduces SME finance in trading manufacturing & service industry to serve the entrepreneurs.

Small and Medium Enterprises (SME) in Bangladesh contributed 25% of gross domestic product (GDP) and 85% of the industrial jobs and 25 percent of the total labor force of Bangladesh in 2007 even though the prospective sector gets negligible facilitation from different support service providers. According to ADB, the country's estimated 6 million SMEs and micro enterprises firms of less than 100 employees have a significant role in generating growth and jobs. This is a sector that has its own distinct needs and requires specialized focus.

The research paper is on "Performance of SME financing of commercial bank in Bangladesh-a case study on National Bank Limited". The major objective of this research paper is to identify the performance of SME financing of commercial bank services in Bangladesh on the basis of the study on Eastern Bank Limited. Though BRAC Bank limited is the market leader of SME Banking, Eastern Bank limited launched most structured SME Banking products & services.

Our paper covers almost all the functions that the SME unit of Eastern Bank Limited as well as other banks of this kind performs. My paper covers the scope and objective of the study, background & limitation of the study as well as SWOT analysis of the research. At the very outset, I have gone for review of literature of SME Banking services of Commercial Bank in Bangladesh. Then I have gone for analysis of major facts of the study on the basis of data & information regarding the topic. I tried to mention here the government & other institutional policy on SME financing besides analyzing the performance of commercial banks in Bangladesh. After that I made some recommendation based on findings of theoretical data analysis. I strongly believe that the performance trend of SME financing of Commercial bank is a going concern. Commercial Banks of Bangladesh will keep a huge contribution in SMEs development of Bangladesh.

**Index Terms**— Minimum 7 keywords are mandatory, Keywords should closely reflect the topic and should optimally characterize the paper. Use about four key words or phrases in alphabetical order, separated by commas.

## 1 INTRODUCTION

**B**USINESS in twenty first century is very competitive and challenging. Business policies and strategies are also ever-changing. The paper has been prepared after careful observation of all the components of SME banking, annual reports of the bank, officials' direct speech and on the basis of other research material such as journal, magazines etc. This paper will provide the reader a brief insight about the performance of SME Banking in Bangladesh on the basis of SME Banking of Eastern Bank Limited.

In the present world economic situation, bank especially commercial bank is treated as the lifeblood of economy of any developed or developing country. With the tremendous in-

creased need of time commercial banks plays an important role in case of overall economic development of any country. From this timely realization, commercial banks are relentlessly trying to provide better service to their clients in order to ensure highest facility.

Financing in SME sector is a treated is the significant issue for the development of Small and medium enterprises (SMEs). Among other high performing commercial banks, Eastern Bank Limited realized the necessity of SME financing for country's overall business development and started financing these sector as per Bangladesh Bank's guideline. Showing outstanding performance, it holds a very strong position in the SME movement.

## 2 BANGLADESH BANK DEVELOPMENT GUIDELINES FOR SME FINANCING

As mentioned earlier, the purpose of the Development Guidelines is to provide directional guidelines to the banks that are considering introduction of Small Enterprises financing to entrepreneurs all across Bangladesh. These Guidelines will assist banks to develop and implement pragmatic and value added products, efficient Credit Approval & Risk Manage-

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ment processes, sound organization structure, strong credit administration and a robust collection procedure.

It may be noted here that these are the minimum requirements and should not in any way be construed to restrict the role of the management processes through establishing comprehensive credit risk management systems.

The Process Guidelines have been organized into the following sections:

#### Policy Guidelines

- Product Program Guidelines
- Segregation of Duties
- Credit Approval

#### Procedural Guidelines

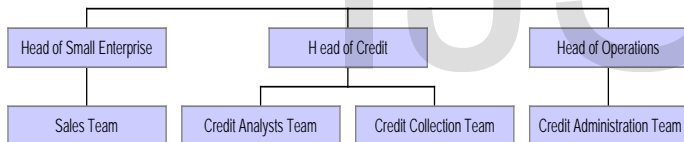
- Approval Process Credit Administration
- Risk Management
- Collection & Remedial Management

#### Preferred Organizational Structure & Responsibilities

An appropriate structure for Credit is kept in place to ensure that the segregation of the marketing / sales function from Approval / Risk Management where administration functions will be under Operations umbrella.

Credit approval should be centralized within the Credit Unit or regional credit centers where reporting should be Central / Head office Credit Unit. All applications must be approved by the Head of Credit or delegated Head Office credit executive.

The following chart represents the preferred management structure:



A separate team of Credit Administration under Operations will process and disburse all loans.

### 3 PERFORMANCE SCENARIO OF COMMERCIAL BANKS IN SME FINANCING

From our study we have come to know that United Leasing Company introduced SME in Bangladesh for the first time in the year 1989 and IDLC strongly came in the market with SME loan in 2003. Among private commercial banks, BRAC Bank from its inception started SME financing and it has coverage all over the country. BRAC Bank only emphasizes on Small enterprises. The main feature of SME Banking of this bank is that it has separate SME Unit. In last five years, BRAC Bank disbursed more than 1.5 lac SME Loans in BDT whose figure is more than TK.5000 crore. Among others Eastern Bank Ltd., Dhaka Bank Ltd. and Prime Bank Ltd. has also special focus on SME Banking. Eastern Bank Limited serves small as well as medium enterprises through their SME Banking services, which make it unique. That is why Eastern Bank Limited is treated most structured Bangladeshi owned private commercial bank in SME Banking. Among foreign Banks HSBC & SCB offer SME banking services rigorously.

In 200-01 SME sector contributed 7.2% in total GDP of Bangladesh, which increases up to 9.4% in 2006-07. With the help of SME financing 79,754 persons developed their career. Out of this 93.6% are small entrepreneurs and 6.4% are medium entrepreneurs. 40% manufacturing firms are in the range of SME financing. Among others shoe producing enterprises, RMGs industries, Agriculture, Dairy firm & poultry firms are the example in which SME loan has already kept significant impact.

### 4 PERFORMANCE SCENARIO OF EBL IN SME FINANCING

EBL has given special focus on SME- Banking since its launch in June, 2006. Year 2007 was the year of spiraling the entire SME Banking Business Unit like Process, Policy, Product development, Capacity planning and ultimately triggering the focus on the growth of the business taking all the risk factors into consideration.

SME Banking division has swung into full-fledged business operations expanding their distribution channels (which was 18 in 2008) and introduced 2 (two) asset products and 1(one) deposit product especially for the SME Customers.

Numerical data indicating the performance in different area can give a gist of SME activities in 2008. Total loans and advance reported an amazing growth of 64% whereas deposit of SME grew by 72% in 2008 over those of 2007.

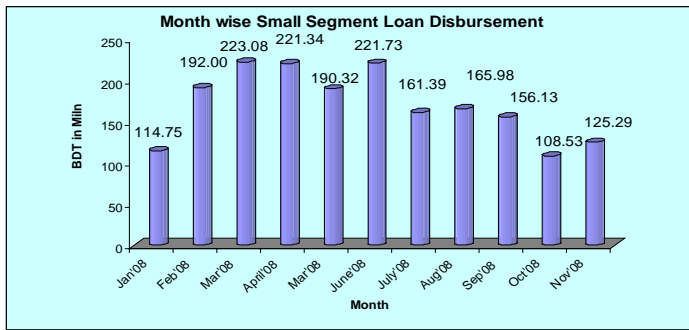
EBL correct selection of borrower, strong monitoring and business strategy was the main strength to limit the NPA rate below 1% in small segment. SME Banking division is preparing to deploy Electronic Loan Processing System to make loan processing easier and faster. Ease of payment method, expansion of distribution channel to give better access to the business community, conducting national seminar to grow awareness to the society on the prospect of this segment are few of the future initiatives EBL is taking as we did in 2008.

There are two Segments in EBL SME Banking. One is Small Enterprise segment (SE) and another is Mid Enterprise segment (ME). SE segment started basically from July, 2006 and ME segment started from the starting of SME Banking (August 2005). ME segment belongs some loans which was disbursed by other department of EBL before starting the SME Banking.

#### 4.1 SME Loans:

In **Small Segment** up to November, 2008, the total loan disbursed amount is of BDT 3,554,995,000 and BDT 1,880,515,000 has been disbursed in 2008. Total Outstanding is BDT 2,404,829,478 up to November 30,2008 (excluding classified amount).

Figure-I: Month wise Small Segment Loan Disbursement.



In **Mid Segment** up to November 30, 2008, funded total Outstanding loan is BDT 957,559,992 (excluding classified amount).

**Total Outstanding** (funded) of SME Banking is BDT 3,362,389,470 (excluding classified amount) and BDT 3,545,128,539 (with classified amount) upto November 30, 2008.

#### 4.2 SME Banking Financial Income and Expenditure:

Table-I: SME Banking Financial Income and Expenditure as of November -2008

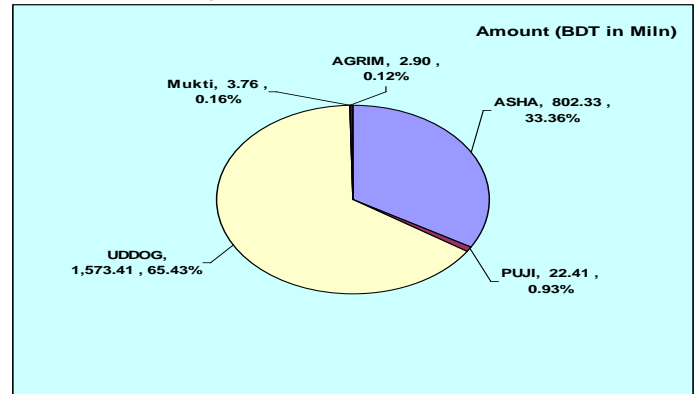
Sl.	Income / Expenditure Heads	(BDT in Mill)
1	Interest Income from Loan	464.38
2	Interest Expenses for Deposit	94.77
3	Interest Expenses for MM Borrowings	42.67
4	<b>Total Interest Expenses</b>	<b>137.44</b>
5	NII before TP	326.94
6	Net TP Income (Expense)	(138.31)
7	NII after TP	188.63
8	Fees & Commission	42.18
9	Other Operating Income	6.60
10	<b>Total Revenue</b>	<b>237.42</b>

Table-II: **Product wise Outstanding** position-Excluding classification (BDT in Miln)

Sl. #	Name of Product	O/S position (as of Dec 31,07)	O/S Oct '08 (YTD)	O/S Nov '08 (YTD)	Variance
<b>Small Segment</b>					
1	ASHA	767.95	806.03	802.33	(3.70)
2	PUJI	14.07	17.38	22.41	5.03
3	UDDOG	567.35	1,536.09	1,573.41	37.32
4	AGRIM	0.75	2.35	2.90	0.55
5	Mukti		3.45	3.76	0.31
<b>Total Small Segment</b>		<b>1,350.12</b>	<b>2,365.30</b>	<b>2,404.80</b>	<b>39.20</b>
<b>Mid Segment</b>		<b>850.15</b>	<b>947.45</b>	<b>957.54</b>	<b>10.09</b>
<b>SME Total</b>		<b>2,200.27</b>	<b>3,312.75</b>	<b>3,362.34</b>	<b>49.59</b>

Figure-II: Product wise **Small Segment Loan Outstanding**

Position-Excluding Classified as of November, 08



#### 4.3 SME Deposits:

As of November 2008 total deposit of SME Banking is of BDT 1,816,735,797 of 11,327 Accounts. Product wise deposit position is:

Table-III: Product wise deposit position

SL	Nature of A/C Name	No. of A/C	Amount (BDT in Miln)
1	CD	8,844	604.83
2	FDR	836	1,078.48
3	STD	674	82.50
4	STD-Shubidha	973	50.91
<b>Total</b>		<b>11,327</b>	<b>1,816.71</b>

#### 5 MAJOR FINDINGS

Major findings of the research are as follows:

- There is no uniform and clear-cut definition of the target market, i.e., SMEs, in Bangladesh. Nevertheless, on the basis of cross-analysis of the different definitions, merits and demerits, etc., considering investment the following definition was used for the purpose of the study
  - ✓ Small: Total investment of up to Tk. 15 million, of which not more than 10 million used as fixed capital.
  - ✓ Medium: Total investment of above 15 million, but not exceeding 30 million, of which not more than 20 million used as fixed capital
  - ✓ Moreover, these, according to their size and type of business, should require finance in the range of Tk. 1 million to Tk. 50 million for working capital, guarantees, LC, term loan, etc.
- The range of SME loan is 1 lac to 20 crore whereas 1lac to 50 lac is usually given to Small enterprise & 50 lac to 10 crore given to medium enterprises.
- SME loan is basically term financing and repaid on installment basis, but historically the business people in our country are accustomed to and prefer continuous loan (cash credit-hypo, overdraft etc) causing slow pace of disbursement of SME loans.

- A lion's share of SME loans (80%) is availed of for trading purpose, instead of manufacturing/service industries. Eventually, the purpose of SME loans to support the economic development of the country may not be served properly. As per Bangladesh Bank policy, provision on unclassified SME loans is maintained at a higher rate (2%) than the corporate and commercial lending (1%) which appears to be contradictory to the spirits of the program.
  - SME loan is predominantly supervisory credit and requires more manpower to conduct supervision, monitoring and recovery works and as such, big chunk of profit is not possible over night. Besides, the private sector banks are more profit oriented and prefer financing to big and corporate customers towards achieving year on year increased profit target.
  - As per Bangladesh Bank guidelines, SME is broadly categorized in 3 sectors: a) manufacturing, b) trading and c) service. While manufacturing and service sectors are prioritized allowing almost 100% re-finance but trading sector hardly gets 20% refinance, though it constitutes more than 80% of total SME portfolio. Besides, refinance has to be claimed on quarterly basis and replenishment is made after one month and above. As such, refinance package may not be so attractive to the banks.
  - The SME sector has grown significantly during the last 14-16 years. There are around 200,000 SMEs in the country (of which around 72% are Small and 28% are Medium). Out of these 200,000 units, only around 30% are at risk of turning "sick".
  - SMEs customers usually do not prepare any financial statement and they have shortage of necessary documents for availing a loan.
  - Most of the proprietors of SMEs are not habituated to repay their EMIs due time. Bank official usually reminds them the date but they like to make delay showing various excuse.
  - Personal guarantors, stock of the business, personal net worth of the owner as well as financial statement are key supports of the clients in getting SME loans.
    - Though BRAC Bank Ltd. Is market leader in SME banking but Eastern Bank Ltd. Introduces more structured SME Banking. BRAC Bank Ltd deals in Small Enterprises where as Eastern Bank deals in Small as well as Medium enterprises.
      - Existing policies of commercial banks regarding SMEs are not systematic, although much work has been and is being done to streamline the policies and systems. The primary survey revealed that around 76% of the proprietors of SMEs are not happy with the policies of commercial banks in Bangladesh.
      - The current system of SME financing practiced by the private commercial banks/financial institutions restricts SME access to institutional finance. The primary survey revealed that around 50% of the SMEs do not find the SME financing schemes/policies of banks/financial institutions helpful.
      - High rates of interest and administrative fees, inadequate amount of financing, bureaucratic/administrative formalities, requirement of a large number of documents, the nature and value of securities / mortgage / guarantees required, short repayment periods, etc. either keep potential customers away, or make institutional credit/financial assistance less attractive.
      - Whether they are processing a loan of \$ 10,000,000,000 or simply \$ 1, 00,000, they would each need one application form, consume almost same amount of paper works and other overheads, which is great threat for the banks as well as customers. They often show their dissatisfaction for that.
      - Banks and other financial organizations ideally target those SMEs, which fall within the purview of the "Thrust Sectors", identified by Bangladesh Bank, namely:
        1. Electronics and electrical
        2. Software development
        3. Light engineering and metal-working
        4. Agro-processing/agri-business
        5. Leather-making and leather goods
        6. Knitwear and ready-made garments
        7. Plastics and other synthetics
        8. Healthcare and diagnostics
        9. Educational services
        10. Pharmaceuticals/ cosmetics/ toiletries
        11. Fashion-rich personal effects, wear and consumption goods.
- The major barriers for SME sector development are as follows:
  - ✓ Electricity
  - ✓ Credit & working capital shortage
  - ✓ Poor law & order
  - ✓ Legal barriers
  - ✓ Excess competition
  - ✓ Technical assistance
  - ✓ Marketing
  - ✓ Raw material price

## 6. CONCLUSION

Small & Medium Enterprises (SMEs) play an important role in both the Developed and the Developing Countries including Bangladesh, socially as well as economically. After decades of research & experiments with various enterprise development models, SMEs have emerged as the cornerstone of economic development in developing countries providing the platform for job creation and economic growth.

But There are various constraints that hinder the develop-



ment of SMEs in Bangladesh such as lack of medium to long-term credit, limited access to market opportunities, technology, and expertise and business information, Lack of suitable incentives and financing sources, inefficient and limited services from relevant government agencies as well as poor capacity of entrepreneurs are other reasons for the slow growth of SMEs. Obviously, the government has many things to do to flourish the SMEs because, if they flourish, SMEs will create new entrepreneurs, generate more jobs and contribute to a great extent to the national economy.

## 7 END SECTIONS

### 7.1 Acronyms

ADB	Asian Development Bank
BIBM	Bangladesh Institute of Bank Management
BBS	Bangladesh Bureau of Statistics
BOI	Board of Investment
CIB	Credit Information Bureau
CPD	Center for Policy Dialogue
DTI	Department of Trade and Industry
EMIs	Equal Monthly Installments
FDR	Fixed Deposit Rate
FBCCI	Federation of Bangladesh Chamber of Commerce & Industries
GDP	Gross Domestic Product
GOB	Government of Bangladesh
IRIS	Institutional Reform and the Informal Sector
IDLC	Industrial Development Leasing Company of Bangladesh Ltd.
IDB	Investment Development Board
JOBS	Job Opportunities and Business Support
LDC	Least Developed Countries
LC	Letter of Credit
MEs	Medium Enterprises
NDFI	National Development Financing Institutions
NGO	Non Government Organization
NBR	National Board of Revenue
NBFI	Non Bank Financial Institution
PPG	Product Program Guide
SEs	Small Enterprises
SME	Small & Medium Enterprise
SCB	Standard Chartered Bank
SSI	Small scale Industries
SC	Savings Certificates
SIC	Standard Industrial Code
SBILC	Small Business Investment and Lending Corporation
STTP	Small business Technology Transfer program.
SBIR	Small Business Innovation Research
SCITI	Small and Cottage Industries Training Institute
SMEDA	Small and Medium Enterprise Development Authority
SOHO	Small Office-Home Office

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